Metro

Los Angeles County
Metropolitan Transportation
Authority
One Gateway Plaza
3rd Floor Board Room
Los Angeles, CA

Board Report

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FINANCE, BUDGET AND AUDIT COMMITTEE
JUNE 15, 2022

SUBJECT: EXCESS LIABILITY INSURANCE PROGRAM

ACTION: APPROVE RECOMMENDATION

RECOMMENDATION

AUTHORIZE the Chief Executive Officer to negotiate and purchase Public Entity excess liability policies with up to $300 million in limits at a cost not to exceed $23 million for the 12-month period effective August 1, 2022, to August 1, 2023.

ISSUE

Metro's Public Entity excess liability insurance policies (which includes transit rail and bus operations) expire August 1, 2022. Insurance underwriters will not commit to final pricing until roughly six weeks before our current program expires on August 1st. Consequently, we are requesting a not-to-exceed amount for this renewal pending final pricing and carrier selection. Without this insurance, Metro would be subject to unlimited liability for bodily injury and property damage claims resulting from, primarily, bus and rail operations.

BACKGROUND

Our insurance broker, USI Insurance Services ("USI") is responsible for marketing the excess liability insurance program to qualified insurance carriers. Quotes are currently being received from carriers with A.M. Best ratings indicative of acceptable financial soundness and ability to pay claims. The premium indications below are based upon current market expectations. Final pricing; however, is not available until approximately 30 days prior to binding coverage.

Metro established a program of excess liability insurance to protect against insured losses. Each year, Risk Management meets with USI to prepare for the upcoming marketing process and secure the data required to approach underwriters and obtain the most competitive coverage and pricing available.

Initial discussions begin in the third quarter of the fiscal year through an evaluation of market conditions to determine the availability of coverages and at what levels of premium. Once established, an annual stewardship meeting is conducted in February to identify what data will be required including loss development, ridership projections, and revenue hour estimates. Risk

Management obtains status data including targeted completion dates of various projects to provide an accurate account of the present and future liability exposures within the agency.

Once internal data is collected, the data is forwarded to USI to present to the domestic insurance marketplace as well as international markets in London and Bermuda. Due to timing requirements, USI approaches underwriters in March and April to ensure that data is deemed current. Initial indications of interests and costs generally become apparent in late April or early May.

USI provides a not-to-exceed number that serves two functions. First, the number provides an amount that Risk Management may approach the CEO and Board to obtain approval for binding of the new program, which mitigates a potential gap in insurance coverage. And second, the number allows our broker ample time to continue to negotiate with underwriters to ensure that Metro obtains the most competitive pricing available.

DISCUSSION

Staff and USI developed a 2022-2023 Public Entity excess liability insurance renewal strategy with the following objectives. First, our insurance underwriter marketing presentations emphasized the low risk of light rail and bus rapid transit services in addition to safety enhancements and pilot programs added over the past years in order to mitigate insurer's concerns with increased operating exposures. Second, we desired to maintain a continuing diversified mix of international and domestic insurers to maintain competition and reduce our dependence on any single insurance carrier. Third, we desired to obtain total limits of $300 million while maintaining an $8 million self-insured retention for rail claims and up to $17.5 million for all other claims but were open to increasing our self-insured retention structure if needed to retain reasonable premium pricing.

USI is presenting Metro's submission to all potential insurers in the U.S., London, European and Bermuda markets representing over 25 carriers in order to create competition in all layers of our insurance program. Our broker communicated with principals in the markets starting in February of this year. Insurance executives both nationally and internationally articulated continuing increased underwriting discipline particularly for transportation and public entity risks. Insurers asked for detailed loss information on Metro claims and performed detailed actuarial valuations on our book of business to establish their premiums. We are awaiting final insurance quotes from carriers for the Public Entity policies from our broker.

Last year, we obtained $300 million in Public Entity coverage with $8 million retention for rail claims and $10 million for all other claims with selected additional retention up to $7.5 million. The relatively calm market we enjoyed for over 20 years changed drastically over the last four years. Extensive loss development specifically related to auto liability, caused the market to "harden" significantly the last several years resulting in less carrier capacity and higher premiums. The trend continues this year. "As we enter the second quarter of 2022, we expected to see more of a slowdown of the hard market conditions than what has materialized. Even with many carriers reporting improved loss ratios and record earnings, tightening capacity and rate increases are not quite behind us...", according to the State of the Market Q2-Q3 | 2022 report from Amwins.

USI faces many challenges in marketing Metro's liability insurance renewal. Carrier results from public agencies, particularly in California, have been significantly worse than other states and carriers have been leaving the marketplace. A very limited pool of carriers is willing to even consider writing public entity policies. Metro is no exception primarily due to the size of our system and the fact that we are in Los Angeles County (considered to be a plaintiff-friendly jurisdiction). The loss development the carriers are experiencing on their accounts, including Metro, resulted in many of the carriers ceasing operations entirely in California, with some of them pulling out of the U.S. entirely. In 2020, Metro lost nearly $100 million in capacity (including our lead incumbent carrier of many years). The loss in capacity resulted in Metro assuming additional risk in the first layer of coverage. Replacing retreating carriers of our program proved challenging. Metro's recent loss history has not proven stellar. Consequently, we anticipate another rate increase in our Public Entity general liability program premiums.

Metro's August 1st insurance placement will reflect higher insurance premiums necessitated by tightened underwriting guidelines and negative developments in auto liability losses. USI recommends a bifurcated program where Metro will retain an $8 million self-insured retention on rail related risks. Our program also includes a self-insured retention of up to $17.5 million for bus and other non-rail related risks. Carriers are not willing to insure Metro's bus operations risk for less retention. We were presented with several approaches within our bus program where Metro will retain a higher self-insured retention within the first layer to reduce our renewal premium. These quotes are still pending. USI will continue to seek options (including alternate retentions and quota share options) and more favorable premiums until our renewal date.

To put our renewal into perspective, a recent Chubb benchmark report provides the following insight: "In 2021, the forces fueling liability and loss trends grew even more powerful. Social inflation -- estimated to have increased commercial auto liability claims alone by more than $8 billion in the last decade -- is exacerbated by surging social consciousness, ideological divides, and economic inflation, with the United States experiencing its highest inflation rate increase in over forty years. Litigation funding by third-party investors seeking portions from plaintiffs' recoveries reached $17 billion in 2021, and the attractive returns from financing commercial lawsuits, mass torts, and other cases are drawing new categories of investors and facilitating more litigation. Meaningful tort reform does not appear to be coming to the rescue." (Chubb Liability Limit Benchmark & Large Loss Profile by Industry Sector 2022).

Attachment A provides an overview of the current Public Entity program, renewal options and estimated associated premiums, and the agency's loss history. The Recommended Program, Option B, includes total limits of $300 million with a bifurcated retention and provides terrorism coverage at all levels. Attachment B shows the tentative program carriers selected and program structure.

DETERMINATION OF SAFETY IMPACT

Approval of this recommendation will not impact the safety of Metro's patrons or employees.

FINANCIAL IMPACT

Funding for eleven months of $18 million for this action is included in the FY23 Budget in cost center 0531, Risk Management - Non Departmental Costs, under projects 300022 - Rail Operations - Blue

Line, 300033 - Rail Operations - Green Line, 300044 - Rail Operations - Red Line, 300055 - Gold Line, 300066 - Rail Operations - Expo Line, 300077 - Crenshaw Line, 301012 - Metro Orange Line, 306001 - Operations Transportation, 320011 - Union Station, and 405533 - Commuter Rail in account 50602 (Ins Prem For Gen Liability). Additional funding of $3 million required to cover premium costs beyond FY23 budgeted amounts will be addressed by fund reallocations during the year.

The remaining month of premiums will be included in the FY24 Budget request, cost center 0531, Risk Management - Non Departmental Costs, under projects under projects 300022 - Rail Operations - Blue Line, 300033 - Rail Operations - Green Line, 300044 - Rail Operations - Red Line, 300055 - Gold Line, 300066 - Rail Operations - Expo Line, 300077 - Crenshaw Line, 301012 - Metro Orange Line, 306001 - Operations Transportation, 320011 - Union Station, and 405533 - Commuter Rail in account 50602 (Ins Prem For Gen Liability).

Impact to Budget

The current fiscal year funding for this action will come from the Enterprise, General and Internal Service funds paralleling funding for the actual benefiting projects charged. No other sources of funds were considered because these are the activities that benefit from the insurance coverage. This activity will result in an increase to operating costs from the prior fiscal year.

EQUITY PLATFORM

There are no equity impacts anticipated as a result of this action.

IMPLEMENTATION OF STRATEGIC PLAN GOALS

The recommendation supports strategic plan goal # 5 “Provide responsive, accountable and trustworthy governance within the LA Metro organization.” The responsible administration of Metro’s risk management programs includes the use of insurance to mitigate large financial risks resulting from unlimited liability for bodily injury and property damage claims resulting from, primarily, bus and rail operations.

ALTERNATIVES CONSIDERED

Various deductibles and limits of coverage options were considered as outlined in Attachment A for the Public Entity program of insurance. Option A maintains the current $300 million limits and bifurcates the program to achieve self-insured retentions (SIR) for bus and non-rail operations at $10 million plus a 50% share of losses in the primary layer plus a $2.5 million self-insured layer and a SIR for rail operations at $8 million without any additional share of losses. The Option B structure increases Metro’s SIR for bus and non-rail operations to $12.5 million plus a 50% share of losses in the primary layer with no self-insured layer. Option C increases the SIR to $15 million plus a 50% share of losses in the primary layer for bus and non-rail operations. Option B is recommended as the most cost effective while retaining a reasonable amount of risk. Option A is not recommended given the estimated 50% increase in premium expense. Option C is not recommended since the reduction in premium does not justify the increased SIR.

NEXT STEPS

Upon Board approval of this action, we will advise USI to proceed with the placement of the excess liability insurance program outlined herein effective August 1, 2022.

ATTACHMENTS

Attachment A - Options, Premiums and Loss History
Attachment B - Proposed Public Entity Carriers and Program Structure

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