



Date: February 28, 2022
To: Self-Insurance Trust Fund Board
From: Jim Smith, City Attorney
Jason Reed, Deputy City Attorney
Lisa Lorts, Risk Management Claims Analyst
Subject: The City of Mesa's Property and Public Liability Trust Fund

I. Purpose.

This report addresses the financial status of the City's Property and Public Liability Trust Fund (the "PPL Trust Fund"), a budgetary recommendation for the PPL Trust Fund, and a proposal that the Board recommend that the City Council adopt a resolution that will facilitate the City's annual purchase of insurance.

II. PPL Trust Fund Finances.

In accordance with state law, the PPL Trust Fund covers the following costs and expenses:

1. Costs associated with staffing the litigation unit in the City Attorney's Office;
2. Payouts and defense costs of third-party claims and lawsuits filed against the City and its employees; and
3. The City's insurance premiums.

In FY 20/21, the PPL Trust Fund incurred \$7.7 million in costs: \$4.5 million for claims and lawsuits; \$2.0 million for insurance; and \$1.2 million for the staffing costs of the litigation unit. For FY 21/22, the City estimates that it will have \$7.0 million in costs: \$3.0 million estimated for claims and lawsuits; \$2.3 million for insurance; and \$1.7 for the staffing costs of the litigation unit.

III. Litigation Expenses.

A. The City's Litigation Unit.

The City's litigation unit defends the City and its employees in nearly all third-party liability claims and lawsuits. In contrast, many cities hire outside counsel to handle their claims and lawsuits. By handling most of the City's litigation matters internally, the City recognizes significant cost savings for the PPL Trust Fund.

For example, in FY 20/21, the staffing cost for the litigation unit was \$1.2 million. During that fiscal year, the litigation unit managed approximately 221 claims and 29 lawsuits. During that same year, the City retained outside counsel to defend the lawsuits associated with seven different incidents. The cost of outside counsel for those lawsuits was approximately \$890,000.

By handling litigation matters internally, the City's litigation unit develops a strong working knowledge of the City's operations and reinforces strong working relationships with City employees. This also helps the City recognize significant cost savings because, in contrast with outside counsel, the litigation unit does not spend time and money on getting up to speed regarding the City's operations and witnesses whenever a new claim or lawsuit is filed.

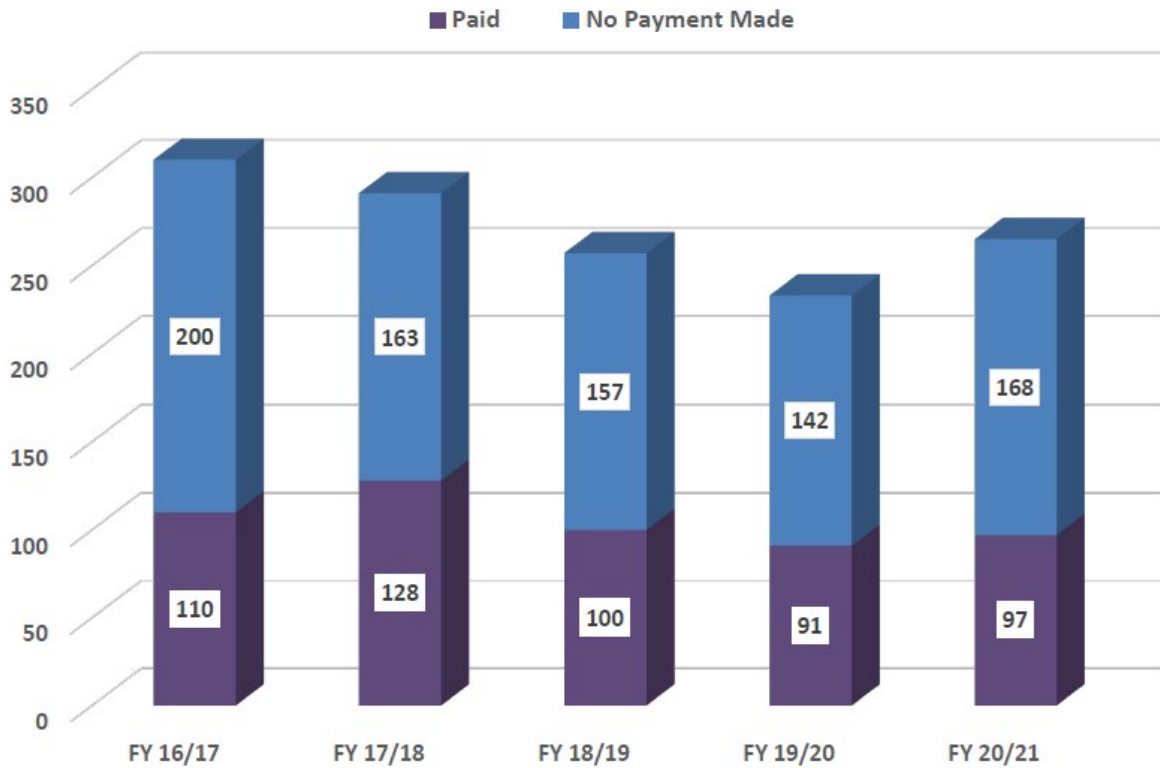
The City Attorney's Office also works with City departments to help reduce the City's financial exposure and explore areas of improvement. This collaborative effort typically results in identifying better practices, implementing additional training, and increased liability sensitivity.

In the past year, the litigation unit has achieved some significant successes, including obtaining summary judgment in multiple lawsuits against the City's Police Officers. Since July 2020, the litigation unit obtained summary judgment in 11 cases, dismissal in 11 cases, and prevailed in three appeals. In total, the litigation unit settled and resolved approximately 258 claims and lawsuits in 2021.

B. Claims Against The City.

The City receives around 250 claims and 32 lawsuits each year. As shown in the following chart, the City is able to resolve a majority of these claims and lawsuits without making a payment to the claimant.

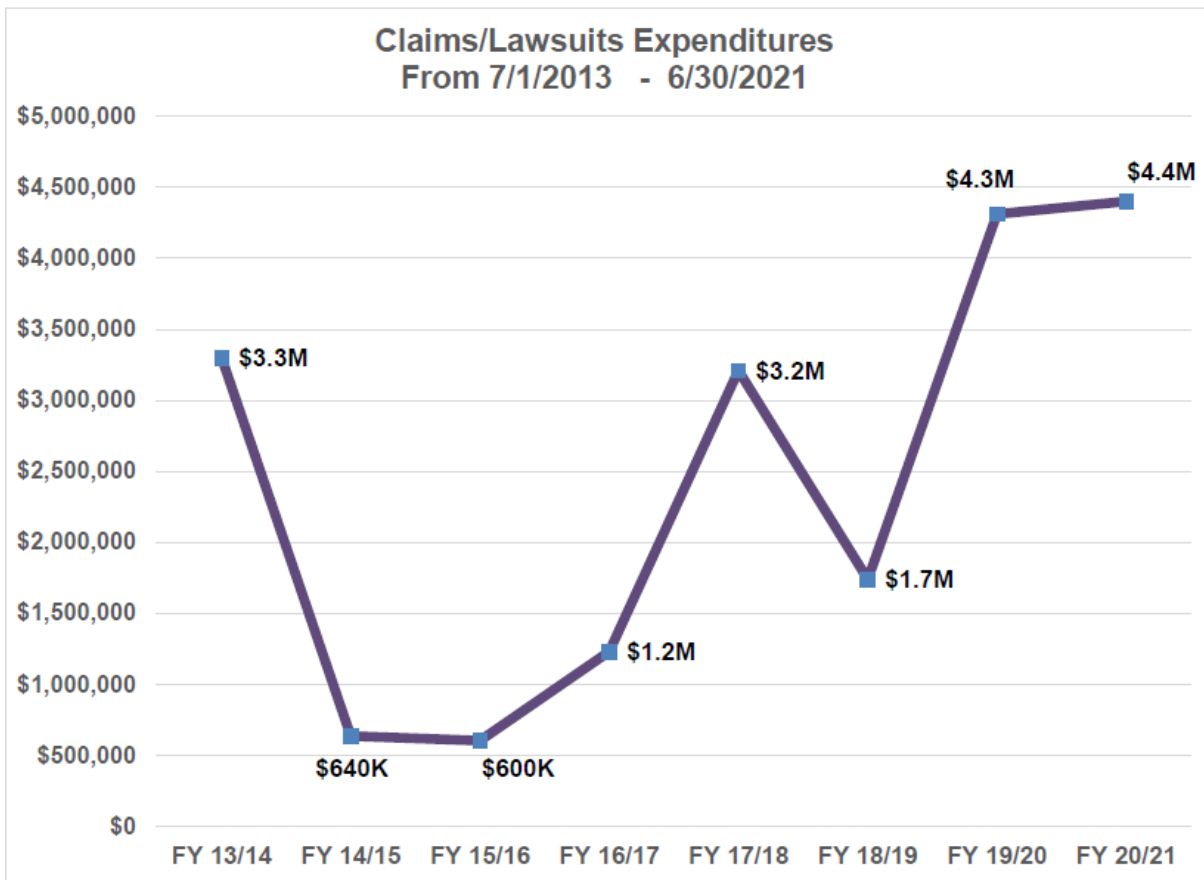
**Closed Claims/Lawsuits
FY 2016 - 2021**



Based on national and local trends, the City anticipates that the number of claims and lawsuits filed against the City will increase. Specifically, cities that experience significant population growth (like the City of Mesa) experience an increased number of claims and lawsuits. This increase can be attributed, at least in part, to the additional services that large cities provide and the number of employees that the City has working with the public. Larger cities simply receive more claims than smaller cities.

In addition to an increased number of claims and lawsuits, the City also anticipates that litigation costs will increase. Some of those increasing costs include larger damage awards, increased outside counsel fees, higher expert witness fees, increased technology costs, and attorney fee shifting provisions.

The following chart shows the annual claim-related payouts from the PPL Trust Fund. The variation in the annual payout depends primarily on whether high-exposure cases were resolved during a particular fiscal year.

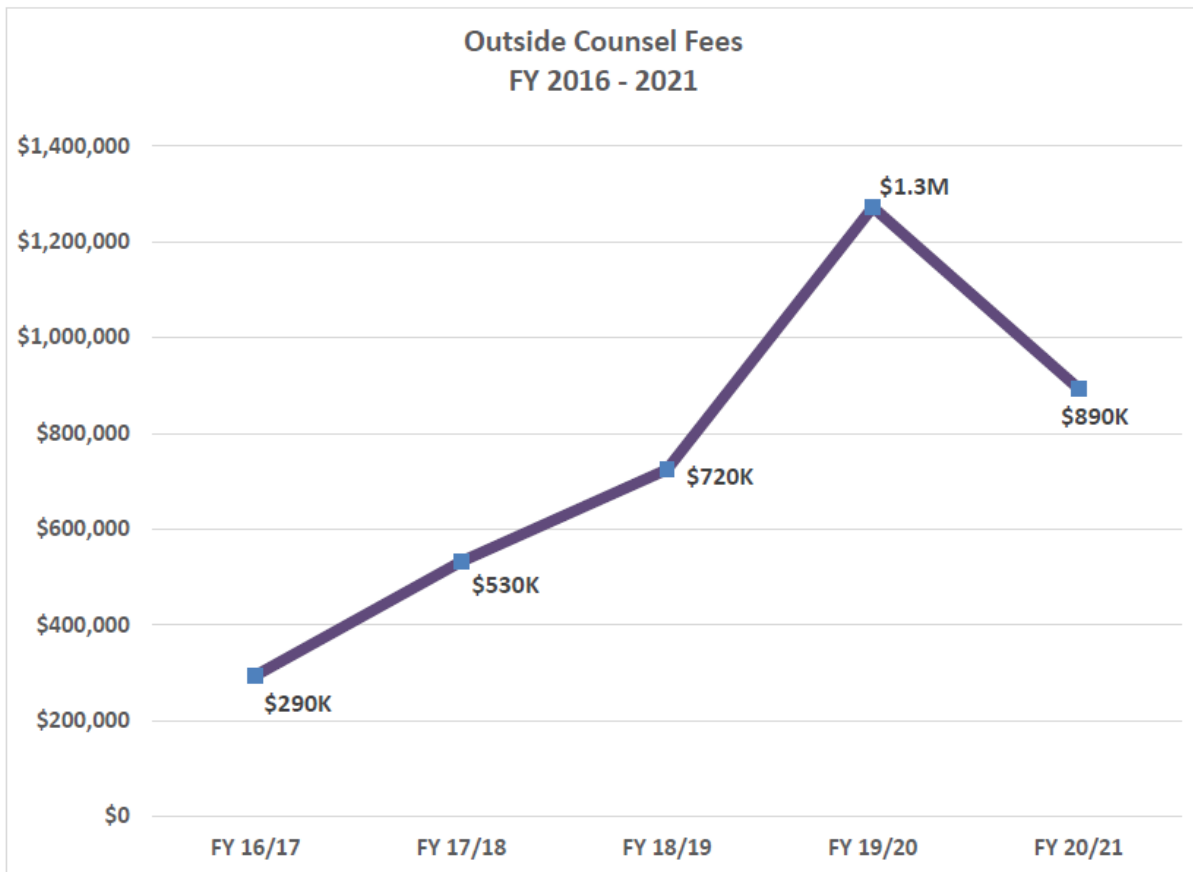


Considering the factors listed above and the number of high-exposure cases that the City is currently defending, pressure may be placed on the PPL Trust Fund if a jury awarded significant damages in one or more of the City's high-exposure cases.

C. Outside Counsel.

The City generally retains outside counsel when a conflict of interest prevents the City's litigation unit from defending the lawsuit, when a particular expertise is needed, and/or for certain high-exposure claims that may erode the City's SIR.

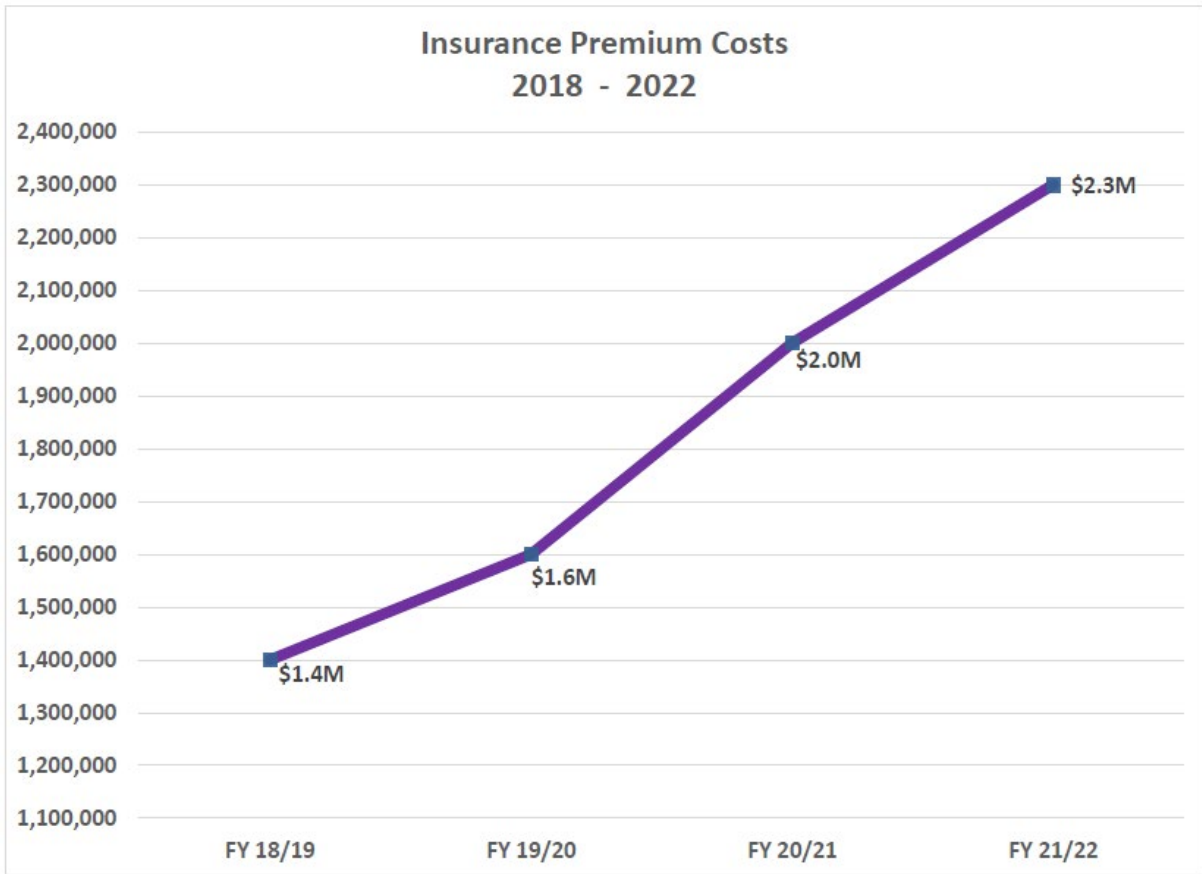
Because high-exposure cases can last for several years, the City can continue to incur costs for outside counsel until these matters are resolved. The following chart, for example, shows the amounts spent on outside counsel for the last five years.



To help limit the PPL Trust Funds’ exposure to the cost associated with outside counsel, the City works with outside counsel to efficiently manage those cases. Some of those strategies include retaining outside counsel with specific expertise, exploring areas for dispositive motions, using offers of judgment to limit plaintiffs’ ability to shift their attorney fees to the City, exploring reasonable settlement proposals, and expanding the City’s capacity to handle cases and claims internally.

IV. Insurance.

The insurance market for municipalities has been very challenging the last couple of years. Shown in the following chart, the City has seen a significant increase in its insurance premiums for the last four years.



Various factors are contributing to these increased premiums. Because the City anticipates that these factors will continue for the foreseeable future, the City anticipates that insurance premiums will continue to put pressure on the PPL Trust Fund.

For example, several carriers that previously provided municipal insurance have withdrawn from the market due to factors like the increasing number of lawsuits, the increasing cost of litigation, rising settlement costs, and civil unrest. With fewer competitors in the market, the remaining carriers are able to raise premiums for the available insurance capacity.

Other factors affecting the insurance carriers and contributing to the lack of capacity include inflationary pressures (that affect the carriers' investment profitability), natural disasters (floods, winter storms, fires) where carriers have made a significant payout, and challenges within the reinsurance market.

These challenges have led to premium increases for municipalities, including the City of Mesa. For example, last year, the City's property insurance premium increased by

approximately 12 percent, and the City's excess liability insurance increased by 44 percent. For Cyber insurance, the City previously had \$10 million in coverage for a premium of \$85,000. This past year, however, the City could only procure \$1 million in coverage for a cost of \$55,000. While the City sought additional quotes for cyber insurance, at least 15 carriers declined to submit a quote to the City.

The above-listed challenges are not unique to the City of Mesa, and different municipalities are exploring options to manage their increasing insurance costs.

For example, the City of Tucson has historically carried \$50 million in excess liability coverage. This past year, due presumably to cost and lack of capacity in the insurance market, Tucson only purchased \$35 million. Taking a similar approach, Glendale went from \$50 million in excess liability coverage to \$40 million, and Tempe went from \$40 million to \$30 million.

For its part, the City historically purchases \$50 million in excess liability insurance and maintains a \$3 million self-insured retention. Once the City's SIR is completely eroded, the excess liability insurance is intended to cover the remaining expenses, costs, and verdicts (up to an annual \$50 million maximum) associated with defending and resolving the underlying claim or lawsuit.

For next year's renewal, the City intends to explore various options to manage the cost of the City's insurance. Options may include reducing the total insurance coverage, modifying coverage amounts, and modifying the City's deductibles and SIR.

Due to market conditions (fewer carriers, reduced capacity in the insurance market, increased premiums, decisions have to be made on short notice), however, the City continues to need flexibility in its ability to purchase insurance and/or adjust coverage amounts.

In 2020, the City Council provided that flexibility by adopting a resolution that permitted the City Manager to purchase insurance in 2020 and 2021 without the City Council's pre-approval.

That flexibility became crucial in 2021. Specifically, two days prior to the expiration of the City's then-current insurance coverage, the City had only obtained quotes for \$30 million in excess liability insurance (instead of the usual \$50 million). Over the next four days, the City was able to renew negotiations with certain carriers, and the City eventually obtained the full \$50 million in excess liability insurance. That said, the City was not able to finalize the full amount of its excess liability insurance coverage until after the previous policies had expired, and the carriers had agreed to backdate coverage (so that there was no gap in coverage).

Without the flexibility provided by the Council's 2020 resolution, the City would not have been able to procure the full amount of excess liability coverage.

In order to continue to provide the City with flexibility in purchasing insurance, the City proposes that the Board recommend that the City Council pass and adopt the attached resolution. Similar to the City's 2020 resolution, the attached resolution permits the City Manager and the City Attorney to jointly purchase insurance for the City for the next five years. The City Attorney will then provide updates to Council regarding the amount and cost of insurance that the City purchased.

For example, in 2022, the City may not be able to purchase the full \$50 million in excess liability insurance due to either availability or cost. In addition to that, based on the fact that some carriers will not provide final quotes until a day or two before the deadline for purchasing insurance, the City likely will have very little time to decide on what type and how much insurance to purchase.

By adopting and passing the proposed resolution, the City anticipates that it will be in a better position to navigate market conditions, to negotiate favorable terms, and to manage the cost of the City's insurance by, among other things, potentially purchasing a lower amount of excess liability insurance, changing carriers, and/or adjusting the City's SIR.

V. Summary And Recommendation.

The City has had a successful year in managing the claims and lawsuits filed against the City and its employees. The City also anticipates coming in under budget. As a result, the City can carry that savings into the next fiscal year and allow for a smaller contribution from the City to the PPL Trust Fund.

That said, pressure continues to exist on the PPL Trust Fund based on, among other things, high-exposure claims and the rising cost of litigation, outside counsel fees, and insurance. To ensure that the PPL Trust Fund maintains the ability cover the costs and expenses necessary to protect the City, the City recommends a City contribution of \$6.0 million for FY 21/22 so that the PPL Trust Fund will have an ending balance of \$11 million.

The City also proposes that the Board recommend that the City Council pass and adopt the attached resolution that would provide the City with flexibility in purchasing the City's insurance.

EXHIBIT A

RESOLUTION NO. _____

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MESA, MARICOPA COUNTY, ARIZONA, AUTHORIZING THE CITY MANAGER AND THE CITY ATTORNEY TO PURCHASE INSURANCE FOR THE CITY INCLUDING PROPERTY, LIABILITY, CYBER RISK, AND AVIATION INSURANCE AND AUTHORIZING ADDITIONAL INSURANCE PURCHASES AND RENEWALS.

WHEREAS, the City obtains insurance for the City of Mesa through the City's Property and Public Liability Trust Fund ("PPL Trust Fund") including property, liability, cyber risk, and aviation insurance annually in November of each year; and the City contracts with an experienced, national insurance broker ("City's National Broker") to assist and represent the City in procuring and selecting such insurance.

WHEREAS, these insurance policies for municipalities generally can only be purchased on an annual basis with annual renewals.

WHEREAS, even with City's National Broker, obtaining insurance for municipalities has become more complex and challenging, and obtaining or renewing insurance occurs near the renewal period or at other times of the year when additional policies may be needed with short notice; and therefore obtaining this type of insurance is a professional service.

WHEREAS, the City has historically obtained excess liability coverage, above the self-insured retention ("SIR"), of fifty million dollars, but obtaining this level of excess coverage has become extremely difficult for municipalities with some municipalities lowering their excess coverage or having gaps in their stack of excess coverage, and the City also had difficulty obtaining its excess coverage stack this past November with the City only able to obtain the full fifty million dollar excess coverage stack the day after the previous policies expired.

WHEREAS, the insurance market for municipalities makes it difficult to obtain insurance, has had unprecedented cost increases, and requires the ability to make decisions on short notice regarding the amount of insurance to obtain (e.g., excess liability coverage, cyber-insurance) based on costs and availability and the ability to modify deductibles or the SIR.

WHEREAS, the City Council would keep the excess liability coverage at its historical number of fifty million dollars if the insurance markets had not and did not continue to change; however, because of unprecedented costs and difficulties in obtaining such amount of excess coverage, City Council recognizes that the City, through the City Manager and the City Attorney, may need to reduce this amount in the future based on costs or availability.

WHEREAS, the City Council therefore finds it is appropriate that the City Manager and the City Attorney are jointly, through the City's National Broker, authorized to purchase and renew insurance coverages, including the ability to change carriers, to add additional insurance or excess layers of insurance, to reduce the total insurance coverage layers or amounts (e.g., reduce the excess liability coverage), to modify coverage amounts, and to modify deductibles and the City's SIR as appropriate or as needed so long as the City Attorney provides periodic updates to Council on the amounts of insurance obtained and costs.

WHEREAS, the Self-Insurance Trust Fund Board for the City of Mesa has recommended that the City Council pass and adopt this resolution that allows the City Manager and the City Attorney to jointly purchase insurance for the City.

BE IT RESOLVED BY THE CITY COUNCIL OF THE CITY OF MESA, COUNTY OF MARICOPA, ARIZONA, AS FOLLOWS:

Section 1: That the City Manager and City Attorney jointly are authorized, through the City's National Broker and with funds from the PPL Trust Fund, to obtain and enter into new insurance agreements for a period of five years (i.e., 2022/23, 2023/24, 2024/25, 2025/26, and 2026/27) for the benefit of the City, including property, liability, cyber risk, and aviation insurance coverages, and including the ability to change carriers, to add additional insurance or excess layers of insurance, to reduce the total insurance coverage layers or amounts (e.g., reduce the excess liability coverage), to modify coverage amounts, and to modify deductibles and the City's SIR as appropriate

Section 2: That the City Attorney shall provide periodic updates to Council on the amounts of insurance obtained and costs.

PASSED AND ADOPTED by the City Council of the City of Mesa, Maricopa County, Arizona, this ____ day of _____, 2022.

APPROVED:

Mayor

ATTEST:

City Clerk