DIVISION OF ADMINISTRATION

**OFFICE OF RISK MANAGEMENT**

# COMMERCIAL INSURANCE PLACEMENT REPORT AND FINANCIAL ANALYSIS

Fiscal Year 2019

Effective July 1, 2018 pursuant to R.S. 39:1484(A)(4)(b) and 1540.

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## EXECUTIVE SUMMARY

Fall 2017, the Office of Risk Management (ORM) was again authorized to procure services of a third-party insurance broker, in accordance with industry best practices and R.S. 39:1484(A)(4)(b) and 1540. ORM contracted with Arthur J. Gallagher Risk Management Services, Inc. (AJG) February 1, 2018 for a five-year period to January 31, 2023 to provide brokerage and related services to ORM. Together ORM and AJG have continued to clarify and improve insurance insurers' understanding of the State's insurability and in bringing insurers to the table who previously had not offered coverage. Second, ORM has sustained the previously increased coverage limits, (in some cases doubled or tripled), which brought the State's insurance limits into closer alignment with the exposure of the highest valued structures. Third, these coverage increases have been accomplished while reducing and then maintaining the State's premiums, such that the State is getting more coverage, which better matches the State's needs, while saving taxpayers more than $9 million annually. Fourth, the State was able to sustain a flat property rate for the 2018/19 policy period while negotiating a competitive rate for the 2019/2020 policy term. With the most recent storm seasons- 2017 and currently 2018-, the ability to lock in the future rate cannot be overstated. Key to the 2018/19 renewal negotiations was the returning of the Recovery School District schools to their home school boards. This resulted in a Total Insured Value change and difference to the overall risk. K-12 schools perform less well in industry underwriting modeling programs. Conversely, higher education institutions generally perform higher than the average in underwriting models.

Pursuant to the original legislation addressed in Act 715 Louisiana Legislation 2014, ORM identified key targets/goals:

- To assure and obtain competitive pricing for insurance including full transparency related to revenue;
- To validate and certify a global marketing effort;
- To create strong market relationships between the State and potential insurers, necessary for on-going program support;
- To improve coverage terms;
- To obtain multi-year contract terms and rates;
- To reduce dependence on wholesale brokers, thereby saving public dollars;
- To create long-term program stability;
- To improve the quality of data provided to the marketplace;
- To enhance coverage and resources for the State's fine arts assets and unique culture;
- To further, expand a focus on Higher Education and their specific needs.

ORM is pleased to report that without exception, July 1, 2018, each key target goal identified was met. Detailed information of the lines of insurance secured in addition to a fiscal analysis follow in this report.

## STATEWIDE PROPERTY PROGRAM OVERVIEW

The State through its Broker, continued to build upon its newly founded market relationships to place insurance effective July 1, 2018 on total property values of $16,798,990,022.
ORM and AJG met with over fifty global insurers/underwriters to discuss and negotiate the best terms for the State. The significant outcomes of the meetings concerning the 2018 placement are as follows:

- For this renewal, all carriers agreed to extend the 2017 rate terms for an additional year through at least July 1, 2019 (instead of 2018 as originally agreed). Negotiations succeeded in creating a stable rate environment even another year forward, to July 1, 2020 in part by locking the London markets to only a 5% rate increase for 2019/2020- this subject to a favorable loss ratio specific to the State.

- The Lloyds marketplace also agreed to a "No Claims" bonus of 3.75% for the 2018-2019 term.

- It is important to note these changes were negotiated with the Lloyds underwriters during the marketing meetings held spring, 2018 following a very difficult earnings year for the marketplace in 2017.
    - Hurricanes Harvey, Irma and Maria cost the industry billions of dollars;
    - Attritional losses such as hail damage and wildfires added to the overall loss picture.
    - 2017 was one of the hardest years in the insurance industry – surpassing even Hurricane Katrina.

- AIG (Lexington) applied a 5% rate reduction, based on the 2017-2018 performance, as previously agreed. For the 2019-2020 term, Lexington has agreed to lock in a 5% rate increase subject to the State sustaining a 0% loss ratio.

- The majority of the remaining domestic markets have agreed to a 5% rate increase in 2019 if the State sustains a 0% carrier loss ratio.

- The total "No claims" bonus to be paid in 2018 by Underwriters at Lloyds to the State for the 2017-2018 policy term is $514,739.43.

- The Named Hurricane wording remains in place for the 2018-2019 policy term. This unique coverage is not available to most insureds. This previously negotiated wording opened up Tropical Storm limits to the very top of the program, $800M. Had a tropical storm hit the state, the limit available would have been $800M in lieu of $400M as in past years.

  The markets also agreed to continue with a $25,000,000 Per Occurrence Named <u>Hurricane</u> in lieu of Named <u>Windstorm</u> for Higher Ed Locations and a $25,000,000 Per Occurrence Named <u>Hurricane</u> in lieu of Named <u>Windstorm</u> for Non-Higher Ed Locations, subject to a $50,000,000 Per Occurrence Maximum.

## Statewide Property Program – Market Participants

| | | |
|---|---|---|
| Allianz Global Corp | Capsicum Re | Starr Companies |
| Allied World Assurance Corp. | Colony Insurance Company | SwissRe Insurance |
| Amlin Insurance | Hallmark Specialty Insurance Co. | Westchester Fire Insurance |
| Arch Capital Group | Ironshore Insurance Ltd. | XL Insurance America, Inc. |
| Axis Insurance U.S. | Lexington Insurance Co. | Parametric via CapsicumRe |
| Berkshire Hathaway | Lloyds of London | |
| BRIT Insurance | Nephila | |
| Canopius U.S. | RSUI Insurance | |

The program is diverse by design and reflects an expanded cross section of the insurance marketplace: Domestic, Lloyds of London, Bermuda, Treaty Reinsurers, Parametric and Insurance Linked Securities (ILS) program participants.

## Statewide Property Program: Coverages, Limits and Pricing

The following chart shows the renewal coverage bound on July 1, 2018.

| Coverage | Limits | Price |
|---|---|---|
| Named Hurricane<br>Flood<br>Fire and AOP (All Other Perils) | $400M<br>$325M<br>$800M | $20,678,766 |
| Fine Arts | $300M | $188,475 |
| Boiler and Machinery | $250M | $289,165 |
| Terrorism (incl. Nuclear, Chemical, Biological, & Radiation (NCBR) | $150M | $162,500 |
| Agent Fee (Property and Casualty) | | $1,050,000 |
| *Total | | $22,368,906 |

## Fine Arts Policy

The stand-alone policy insuring the State's substantial fine arts assets renewed July 1, 2018. The limit of coverage increased to $400M for 2018 from $300 M in 2017. This separate coverage limit of $400M is in addition to the master property policy described above. The definition of fine arts is broad by design and coverage enhancements are specific to the fine arts exposure, which include a specialized adjusting team.

## Property Brokerage Fees

For the past three years, the broker's fee for property placements was $880,000 annually and $200,000 annually for casualty placements. The broker's contract was just renewed in 2018 for a five-year term for $1,050,000 annually for property and casualty placements combined, which is $30,000 less each annum as compared to the previous three years.

## Financial Analysis (Statewide Property Program)

Act 374, which was signed into law by Governor Edwards on June 7, 2016, eliminated the requirement for ORM to pay surplus lines taxes and surcharges. The combined savings for these taxes/surcharges equaled $931,061.97 in for 2018/19.

### Combined Limit and Pricing Comparison – Statewide Property

| | FY 17-18 | | FY 18-19 | | Pricing Increase (+)/Decrease(-) |
|---|---|---|---|---|---|
| **Coverage** | **Expiring Limits** | **Expiring Price** | **Renewal Limits** | **Renewal Price** | |
| Named Hurricane | $400M | $21,261,031 | $400M | $20,624,766 | ($636,265) |
| Parametric | $0.00 | $55,000 | $1.25M | $54,000 | ($1,000) |
| Flood | $325M | Incl in above | $325M | Incl in above | Incl in above |
| Fire and AOP | $800M | Incl in above | $800M | Incl in above | Incl in above |
| Fine Arts | $250M | $163,505 | $250M | $188,475 | $24,970 |
| Boiler and Machinery | $250M | $292,495 | $250M | $289,165 | ($3,330) |
| Terrorism | $150M | $209,500 | $150M | $162,500 | ($47,000) |
| **Total** | | **$21,981,531** | | **$21,318,906** | **($662,625)** |

*The agent fee shown for 17/18 is specific to property only. The agent fee shown above for 18/19 includes BOTH casualty and property.

## Casualty Insurance

### Casualty Renewal Overview

#### State's Wet Marine Program: Hull & Machinery, Protection & Indemnity, Vessel Pollution Excess Coverage

The marketing process was similar to the property renewal. The worldwide marketplace was again approached. Terms and conditions were renewed with a positive impact on the State's program. Expiring marine pricing was $$508,090 after the continuity credit. The renewal pricing is $521,776 plus an additional market continuity credit of $95,516, resulting in a $47,668 cost savings to the State effective July 1, 2018.

#### SMG and the Louisiana Stadium and Exposition District (LSED) for operations at the Mercedes-Benz Superdome, Smoothie King Center, & Champions Square

Coverage is obtained by ORM on behalf of the above named insureds as per written contract. Coverage was marketed globally with the following results:

- Crime – Coverage remained with Hiscox with a flat renewal for a total annual premium of $13,385.
- Workers Compensation- Coverage remained with LWCC with a renewal premium of $745,738. This is an increase of $127,223 over expiring due to a 8.47% payroll increase and a loss experience deterioration, resulting in an e-mod increase of 10.38%
- Excess Commercial General Liability limits are $100M – Coverage includes law enforcement liability as per the expiring policy. The renewal premium had a premium increase of $25,934 for a total of $615,414. This increase is attributed to estimated increased exposures for the coming year. Estimated admissions receipts are .48% above 2017 and annual attendance is anticipated to increase 4.47% for the coming year.

#### STATE OF LOUISIANA

- Cyber Liability- Coverage was written for the State's Office of Technology Services (OTS) and the agencies/departments that fall under OTS for IT services. As the insurance program continues and the State's IT work becomes more aligned within all agencies , data collection will be undertaken and coverage expanded as it makes sense to do so.
    - Coverage includes the following:
        - Network Security Privacy Liability
        - Data Recovery and Business interruption
        - Multimedia Liability
        - Privacy Regulatory Defense and Penalties
        - Notification

  This coverage was renewed July 1, 2018 with Lloyds of London. Limits were renewed with limits of $20M for Each and Every claim with a $20M policy aggregate. Named Higher Education institutions are included, per the expiring policy with a sub-limit of $10M Each and Every Claim subject to a $10M aggregate limit. The renewal premium for 2018 is $496,650, which is an increase in premium of $23,650. This increase is due to the State lowering the deductible from $1 Million to $750,000 per occurrence.

- Disaster Management- This coverage insuring all state agencies renewed July 1, 2018 with Lloyds of London with limits of $1M per occurrence/$5M policy aggregate. The renewal pricing is $56,250 annually; a $10,311 increase over the expiring term. This coverage provides on-site response services to manmade and natural disasters that cause a loss of three lives or more. It includes the establishment of family assistance centers near the location of the incident, media support, assistance to victims' families, assistance to first responders and other types of necessary resources consistent with managing the aftermath of a crisis.
- Aviation General Liability, Aviation Excess Liability & Aviation Hull – This coverage was also renewed effective July 1, 2018. Aviation General Liability is written with National Union Insurance Company with a $25M Each Occurrence Limit. Aviation Liability including Hulls is also written with National Union Insurance Company with a $10M Limit Including Passengers and Hull Coverage per scheduled units. Excess Aircraft Liability is written with QBE Insurance with a $15M xs $10M limit. Total Aviation premium for 2018 is $569,952, which represents a savings of $8,108 over the prior year.

### Combined Limit and Pricing Comparison – Statewide Casualty

| Casualty | FY 17-18 | | FY 18-19 | | Pricing |
|---|---|---|---|---|---|
| **Coverage** | **Expiring Limits** | **Expiring Price** | **Renewal Limits** | **Renewal Price** | **Increase (+)/ Decrease(-)** |
| Wet Marine<br>Premium Continuity Credit | | $556,635<br>($47,848) | | $556,635<br>($95,516) | ($47,668) |
| Hull | Replacement | Incl in above | Replacement | Incl in above | - |
| Protection and Indemnity (P&I) | $100M | Incl in above | $100M | Incl in above | - |
| Pollution | Incl in above | Incl in above | Incl in above | Incl in above | - |
| Crime (incl. employee theft) – SMG and LSED | $500,000 | $13,385 | $500,000 | $13,385 | $0.00 |
| Workers Compensation – SMG and LSED | Statutory | $618,515 | Statutory | $745,738 | $127,223 |
| Employer's Liability | $1M | Incl in above | $1M | Incl in above | - |
| Excess CGL - SMG and LSED | $100M | $589,480 | $100M | $615,414 | $25,934 |
| Cyber Liability (new) | $10M/$10M | $473,000 | $20M/$20M & $10M/$10M Higher Ed | $496,650 | ($23,650) |
| Disaster Management (new) | $1M/$5M | $45,939 | $1M/$5M | $56,250 | $10,311 |
| Aviation | $25M Liab $10M Incl Hulls | $573,142 | $25M Liab $10M Incl Hulls | $569,952 | ($3,190) |
| Agent Fee | | $110,000 | | Included in Property Placement Fee | ($110,000) |
| **Total** | | **$2,359,106** | | **$1,905,223** | **($29,818)** |

## Brokerage Fees

As stated above, the fee for the Statewide Casualty Program is *included* within the annual Property Placement Fee for a combined total of $1,050,000 for 2018, which is a $30,000 annual decrease from expiring.

### Licensed Professional Liability

Many of the State's Higher Education Institutions offer internship programs through outside businesses and non-profit agencies as part of the curriculum, such as a nursing internship through a local hospital for example. Many third party providers/businesses require evidence of professional liability and general liability coverage from the student and institution before they will allow students to intern at their facility. The State provides casualty coverage for the institutions, but per state law has been unable to include the students as insureds. In the past, this has created a challenge for those institutions as well as their students depending on cooperation of third parties to assist with their internship curriculums. Coverage was renewed effective July 1, 2018 with United Educators Insurance Company to provide coverage to those students participating in qualifying programs at specifically named institutions. Limits remain unchanged from the prior term, $1M per claim/$5M policy aggregate. Certificates of insurance are provided by AJG to the institutions to evidence coverage for the students.

This policy was renewed effective July 1, 2018 with United Educators Insurance Company for an annual premium of $152,296. The premium increase of $30,109 is attributed to lowering the deductible from $5,000 per occurrence to no deductible. The cost is not borne by the State, but is left to each participating institution to manage.

# Additional Benefits

## Improved Data Project

As part of the brokerage services scope of work, AJG's team collected Secondary Construction/Occupancy/Protection/Exposure (COPE) information on 763 of the State's highest valued buildings in 2015, expanded this to 3533 locations in 2018. In addition, training was provided for Sedgwick so that the secondary modifier information collection will continue in the future. It is anticipated that by the end of the next fiscal year, we will have the secondary COPE data for 100% of the State's buildings.

Secondary COPE data is used to impact catastrophe modeling reports of large, highly valued property schedules, such as the State's, utilized by the insurance marketplace to better assess the State's risk and catastrophic exposure. The addition of the COPE data and supplemental information about positive changes in the State's physical environment (New Orleans levee improvements, adoption of uniform building codes) generated significant positive developments to the State's modeling results and underwriting review, see below:

## 2017 Modeling Results:

**Hurricane** *(Incl Storm Surge)*
State of Louisiana has approximately $16.7 Billion in values exposed to hurricane related events in the State of Louisiana. **Figure 1-1** illustrates the probability of ground up losses exceeding various amounts due to one event in a given year, as described by the Occurrence Exceedance Probability (OEP). The 250yr event loss probability is commonly used by the insurance marketplace as a gauge for insurance pricing.

| Critical Prob. | Return Period | AIR | | RMS | |
|---|---|---|---|---|---|
| | | Ground Up | Gross Loss | Ground Up | Gross Loss |
| 0.10% | 1,000 | $1,813,572,272 | $1,760,815,080 | $1,438,663,347 | $1,385,500,629 |
| 0.20% | 500 | $1,378,915,439 | $1,326,505,414 | $1,065,535,573 | $1,011,869,722 |
| **0.40%** | **250** | **$1,113,835,277** | **$1,062,414,678** | **$743,231,433** | **$691,535,591** |
| 1.00% | 100 | $644,484,032 | $593,408,841 | $412,227,961 | $361,640,631 |
| 2.00% | 50 | $343,052,527 | $292,333,963 | $235,458,644 | $185,144,961 |
| 5.00% | 20 | $172,420,747 | $122,102,739 | $82,907,202 | $32,868,416 |
| AAL | | **$39,123,226** | **$26,825,866** | **$19,751,948** | **$13,645,158** |

*Figure 1-1*

## 2018 Modeling Results:

**Hurricane** *(Incl Storm Surge)*
State of Louisiana has approximately $16.8 Billion in values exposed to hurricane related events in the State of Louisiana. **Figure 1-1 & Figure 1-2** illustrates the probability of ground up losses exceeding various amounts due to one event in a given year, as described by the Occurrence Exceedance Probability (OEP). The 250yr event loss probability is commonly used by the insurance marketplace as a gauge for insurance pricing.

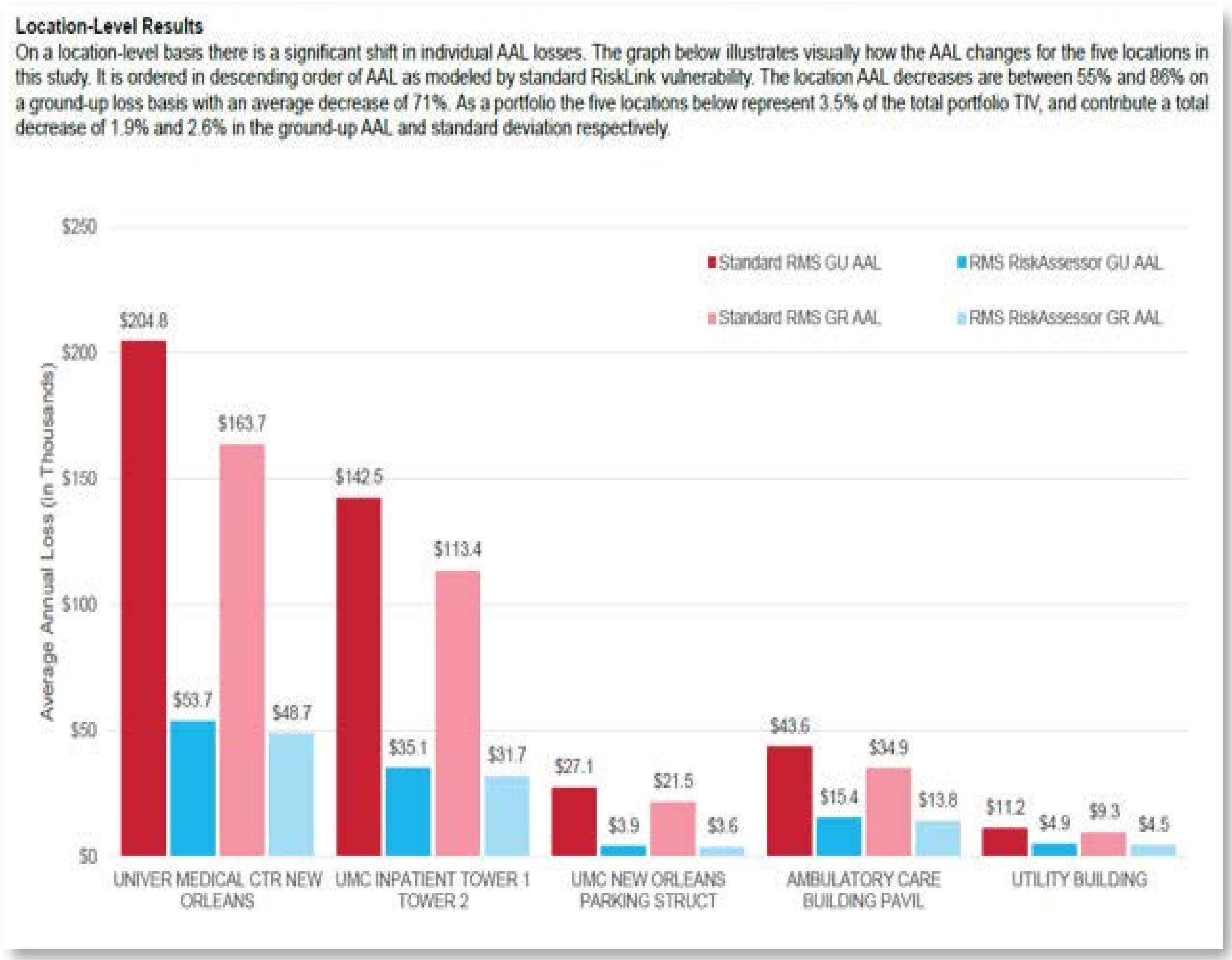
| Critical Prob. | Return Period | RMS | |
|---|---|---|---|
| | | Ground Up | Gross Loss |
| 0.10% | 1,000 | $1,405,031,686 | $1,352,237,542 |
| 0.20% | 500 | $1,021,006,787 | $968,505,023 |
| **0.40%** | **250** | **$697,787,881** | **$646,155,264** |
| 1.00% | 100 | $379,427,327 | $328,728,353 |
| 2.00% | 50 | $212,617,954 | $162,446,496 |
| 5.00% | 20 | $71,783,130 | $21,754,084 |
| AAL | | **$17,921,914** | **$12,351,528** |

*Figure 1-1*

## "BESPOKE" CAT MODELING INVESTMENTS
## IMPROVED DATA PROJECT

In late 2017, the first pilot bespoke project for the State was completed, using the comprehensive engineering data for the University Medical Center in New Orleans. This data project had a direct, positive result on the State's property rate for the 2018/19 renewal. Because this analysis was provided directly by RMS, an unbiased and credible source of data, the carriers trusted and factored this information into their underwriting decisions for 2018 and will continue onto the future.

This is a long-term investment in being able to quantify the State's true risk to the market. The next bespoke project to be completed is the Superdome.



## Reduced Dependence On Wholesale Brokers

A significant factor in the reduction of brokerage fees in 2015, 2016, 2017 and 2018 was the reduced dependence on wholesale brokers. The State saved $3.1 million dollars in brokerage fees in 2015 as AJG placed much of the coverage directly rather than through the utilization of a wholesale broker. If you extrapolate this across the last four years, the saving in wholesale brokerage fees alone is near $12.4 million dollars. Both domestic and international wholesale brokers were used only when needed. Additionally, when AJG did use wholesale brokers, both AJG and ORM were present during the presentations enabling ORM and AJG to maintain control of the placement. The fees for the domestic wholesalers are included in the contract brokerage fee of $1,050,000. The international wholesale brokers (London and Bermuda) received a 5% wholesale fee (included in the premium), compared to double-digit fees in past programs.

The following markets were directly placed by the broker, without wholesale broker assistance:

- AIG
- AWAC
- Berkshire
- Canopius US
- CV Starr
- Chubb
- Ironshore
- Lexington
- National Union
- SwissRe
- United Educators

## Focused Higher Education Program

The participation in the Internship liability coverage program has significantly increased since inception in 2016. We expect this trend to continue. Round table discussions on risk management specific to higher education have been ongoing since fall, 2015 and will continue quarterly and regionally. The response to this has been positive. AJG continues to bring a higher education practice and reputation to the table to assist with the State's exposures concerning higher education risks.

# In Summary

ORM's intent is not only to save money and significantly improve coverage limits - both of which have been accomplished, but also to take steps necessary to create a long lasting property program that will stand against another severe storm season through multi-year rate and participation guarantees to gain rate protection and program stability. Protecting the State's budget and being able to cost effectively insure the State's assets remains paramount through the process with Each and Every renewal.

The success of the placements for 2015, 2016, 2017 and 2018 are evidenced by the pricing, coverage terms and number of markets competing for participation in the State's program.

The substantial dollar savings for all lines of coverage placed in the commercial market for ORM include significantly increased limits, coverage improvements, program stability, and market relationships, would not have been possible under the old insurance procurement model. The enactment of Act 715 in the 2014 Regular Session, which allowed ORM to select a broker rather than bidding a predetermined insurance program, facilitated the tremendous impact made on the insurance marketplace. This impact is evidenced in the program presented in this report.

For clarification, the savings shown in this report is based on actual commercial premiums paid for coverage placed for FY 17-18 versus FY 18-19.

Thanks to the State legislature, this is the beginning of ORM's success story. Resources made available pursuant to their approval of legislative changes will assist ORM in its on-going efforts to drive down the cost of risk and provide stability for the State for years to come.