



## City Council Staff Report

DATE: November 5, 2008 Consent Calendar  
SUBJECT: Renewal of Excess Earthquake/Flood Insurance Coverage  
FROM: David H. Ready, City Manager  
BY: Douglas Holland, City Attorney

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### SUMMARY

On July 1, 2008, the City purchased a primary layer of coverage for earthquake/flood insurance in the amount of \$2.5 Million. In addition to the primary layer of coverage, the City normally purchases excess coverage, also known as Differences in Coverage (DIC), insurance. Last year, the City Council authorized the purchase of an additional \$22.5 Million in excess insurance coverage for a total of \$25 Million in coverage. The current excess insurance policy is set to expire on November 20<sup>th</sup>. The requested action would authorize staff to purchase an additional \$22.5 Million in excess insurance coverage, for a combined total of \$25 Million, in earthquake and flood insurance protection through July 1, 2009.

### RECOMMENDATION:

1. Adopt Resolution No. \_\_\_\_ "A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF PALM SPRINGS, CALIFORNIA, APPROVING THE PURCHASE OF \$22.5 MILLION IN EXCESS EARTHQUAKE/FLOOD (DIFFERENCE IN CONDITION) INSURANCE FROM LLOYDS OF LONDON IN AN AMOUNT NOT-TO-EXCEED \$330,799.21 FOR POLICY YEAR 2008-2009.
2. Authorize the City Manager to execute all documents necessary.

### STAFF ANALYSIS:

Hurricane Katrina, which caused nearly \$50 billion in insured losses, was the single most destructive natural catastrophe in U.S. history. The massive loss in both lives and property caused by this disaster has led insurers, rating agencies and catastrophe modeling firms to reconsider all prior assumptions concerning disaster risks. As a result, insurance premiums have increased significantly making property insurance almost unaffordable for some public agencies. In addition, the insurance market that writes catastrophic coverage (flood, wind, and earthquake) has reduced available insurance capacity further increasing costs.

ITEM NO. 21

Recent assessments by catastrophe modeling firms indicate that the destruction that could be caused by a massive California earthquake is of the same order of magnitude as the worst hurricane scenarios – a Category 5 storm striking Miami and moving up the Florida coast, or a Category 5 storm raking the New Jersey coastline before crashing into New York City. The USGS predicts that there is a 62% probability of at least one magnitude 6.7 or greater quake, capable of causing widespread damage, striking the San Francisco Bay region before 2032. While making no specific timeframe projections, a recent, widely reported study by Yuri Fialko of Scripps Institute of Oceanography at the University of California, San Diego, indicates that, as a result of 300 years of unrelieved, steadily building tension, a segment of the San Andreas fault running through Palm Springs and a number of other cities in San Bernardino, Riverside and Imperial counties “could rupture at any moment,” possibly producing a M7+ quake. One catastrophe modeling company estimates that a rupture along this segment of the San Andreas Fault in Southern California could result in as much as \$300 billion in property damage.

The City is self-insured and purchases various lines of insurance each year for additional protection. Flood and earthquake is almost always excluded from commercial property policies and must be purchased separately. In July, the City Council approved the purchase of an “All Risk Property” insurance policy, which included \$2.5 Million in primary earthquake/flood coverage.

The City’s property schedule has a present net replacement cost of \$335 Million (2006). While it is highly unlikely that the City would have to replace every single facility in the event of an earthquake, there are several facilities, such as the Airport and Wastewater Treatment Plant, which are considered critical to the continued operations of the City. These two facilities alone have an estimated replacement cost of over \$120 Million. In reality, the actual cost is probably in excess of \$200 Million, if both facilities were totally destroyed.

To ensure that there is sufficient coverage to repair and/or replace City facilities that could be damaged in a flood or earthquake, the City has historically purchased Differences in Coverage (DIC) insurance to augment its primary earthquake/flood insurance policy. Last year the City Council purchased a single DIC policy of \$22.5 Million from Lloyds of London. Staff is proposing that the City continue with Lloyds and purchase a single policy of \$22.5 Million for the rest of the fiscal year in the amount of \$330,799.21. Staff is recommending that the policy should terminate on July 1, 2009, which is the date on which all other City insurance policies expire. Our insurance consultant and broker believes that the City will be better positioned to negotiate favorable rates on the City’s policies if the terms of all policies are coterminous.

Last year staff observed that significant increases in insurance costs caused many public agencies to reduce their limits or drop DIC coverage altogether. While the City could purchase less insurance, or only maintain the primary level of earthquake/flood insurance coverage, staff does not recommend this course of action based on recent actions taken by the Federal Emergency Management Agency (FEMA). Normally, the


federal government reimburses 75 percent of eligible costs incurred by local governments and special districts in the event of a catastrophic disaster. The remaining 25 percent is generally funded by state and local governments. Following the aftermath of Hurricane Katrina, FEMA is now reviewing whether the local government or special district requesting federal disaster assistance has adequate insurance in place, or the financial capacity to purchase such insurance prior to providing such assistance. According to FEMA guidelines (44 CFR Part 206), local government agencies that fail to maintain proper property insurance can be denied federal disaster assistance.

The current insurance market makes it financially cost prohibitive to purchase insurance to cover the entire property schedule. However, based on the FEMA policy regarding disaster assistance funding, staff believes that the City needs to maintain a reasonable level of coverage to protect its interests and to demonstrate good faith compliance with federal regulations concerning disaster assistance. Therefore, it is recommended that, in addition to the primary coverage, the City Council authorize the purchase of an additional \$22.5 million in insurance. This will continue to provide the City with a combined total of \$25 Million in earthquake/flood coverage.

FISCAL IMPACT:

The City budgeted adequate funds to cover the cost of all insurance, including the DIC, and there are sufficient funds in the Risk Management program to cover this expense.

  
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Douglas Holland, City Attorney

  
for Thomas J. Wilson, Asst. City Manager  
David H. Ready, City Manager

Attachment:

Resolution Approving Excess Earthquake/Flood Insurance Coverage for the period of November 20, 2008 through July 1, 2009

RESOLUTION NO. \_\_\_\_\_

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF PALM SPRINGS, CALIFORNIA, APPROVING EXCESS EARTHQUAKE/FLOOD COVERAGE IN THE AMOUNT OF \$22.5 MILLION AT A COST NOT-TO-EXCEED \$330,799.21 FOR POLICY YEAR 2008-09.

WHEREAS, the City of Palm Springs is located in the vicinity of several known active and potentially active earthquake faults, including the San Andreas, the San Jacinto and the Elsinore faults; and

WHEREAS, the topography of the City makes it prone to flooding, especially during times of heavy rainfall; and

WHEREAS, each year the City purchases a primary earthquake and flood insurance policy; and

WHEREAS, the City supplements its primary insurance policy with excess coverage to properly protect its public facilities from catastrophic loss from earthquake or flood; and

WHEREAS, the City's insurance broker has solicited proposals from various insurance companies for excess insurance coverage and is recommending that the City purchase a \$22.5 Million policy from Lloyds of London; and

WHEREAS, the City Council desires to purchase excess insurance coverage to properly protect public property from earthquake and flood damage.

NOW THEREFORE BE IT RESOLVED by the City Council of the City of Palm Springs, California approves the purchase of excess insurance coverage from Keenan & Associates for policy year 2008-09:

| Earthquake/Flood (Difference in Condition)<br><b>Excess of \$2,500,000 Primary</b>                       | Premium 11/20/08 through 07/01/09<br><b>Net of Commission</b> |
|--|---|
| First Layer Excess Coverage: \$22.5 Million<br>Insurance Company: Lloyds of London<br>Best's Rating: N/A | <b>\$330,799.21</b>   |

ADOPTED THIS 5<sup>th</sup> day of November, 2008.

\_\_\_\_\_  
David H. Ready, City Manager

ATTEST:

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James Thompson, City Clerk

CERTIFICATION

STATE OF CALIFORNIA )  
COUNTY OF RIVERSIDE ) ss.  
CITY OF PALM SPRINGS )

I, JAMES THOMPSON, City Clerk of the City of Palm Springs, hereby certify that Resolution No. 22098 is a full, true and correct copy, and was duly adopted at an adjourned meeting of the City Council of the City of Palm Springs on the 5<sup>th</sup> day of November, 2008, by the following vote:

AYES:  
NOES:  
ABSENT:  
ABSTAIN:

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James Thompson, City Clerk  
City of Palm Springs, California