Office of Superintendent of Schools
Board Meeting of February 13, 2013

January 30, 2013

Financial Services
Richard H. Hinds, Chief Financial Officer

SUBJECT: **RENEWAL OF DISTRICT'S PROPERTY INSURANCE PROGRAM**

COMMITTEE: **INNOVATION, EFFICIENCY & GOVERNMENTAL RELATIONS**

LINK TO STRATEGIC FRAMEWORK: **FINANCIAL EFFICIENCY/STABILITY**

The School Board is required to carry property insurance on all school buildings and all school plants including contents, boilers and machinery, except buildings of three classrooms or less, pursuant to the provisions of Section 1001.42(9)(b)(8)(d), Florida Statutes. Additionally, pursuant to the provisions of the Robert T. Stafford Disaster Relief and Assistance Act (Stafford Act), FEMA funding becomes available after a disaster declaration from the President of the United States of America. FEMA has recently taken a very strict position on the required purchase of coverage following the receipt of FEMA funds, which Miami-Dade County Public Schools has received, resulting in increased scrutiny of property owner's coverages by FEMA.

The structure of the District's property insurance program is also of vital interest to the financial markets which hold the Master Lease for the District's Certificate of Participation (COP's). Section 5.3 of the master lease states that any policy of all risk property insurance must be obtained from a commercial insurance company or companies rated A+ by A.M. Best Company, or in one of the two highest rating categories of Moody's and S&P, or otherwise approved by the Credit Facility Officer.

The current property insurance program's term is May 1, 2012 to May 1, 2013. The strategic approach to renewal of the District's all risk, replacement cost property insurance program has been that the Board authorize a structure for renewal which includes coverage and premium goals at its February Board meeting, in order for staff to meet with worldwide markets to obtain the best renewal terms for purposes of capacity and pricing. The final structure of the bound program is then brought back to the Board at its May Board meeting for confirmation and tweaking, if necessary.

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Staff has already begun meeting with underwriters from worldwide carriers specializing in catastrophic coverage, which has been the focus since the District suffered a $95 million loss from Hurricane Andrew in 1992. Subsequent storms in 2004 and 2005 including Katrina, Rita, and Wilma were appreciably under the District's windstorm deductible, but FEMA claims have been filed and are still open.

2012 ATLANTIC HURRICANE SEASON

The 2012 Atlantic Hurricane season which ended on November 30, 2012 produced 19 named storms, of which 10 became hurricanes, with one becoming a major hurricane. The number of storm is also well above the average during a hurricane season of 12 storms. The number of hurricanes is also above the average of six, but the number of major hurricanes is below the average of three. This season marks the second consecutive year that the mid-Atlantic and Northeast suffered devastating impacts from a named storm. Storms Sandy, and Irene last year, caused fatalities, injuries and tremendous destruction from coastal storm surge, heavy rainfall, inland flooding and wind. Storms struck many parts of the country this year including tropical storms Beryl and Debby in Florida, Hurricane Isaac in Louisiana, and Post-tropical Cyclone Sandy in New Jersey. An interesting aspect of the season was its early start with two tropical storms Alberto and Beryl, developing in May before the season officially began.

Hurricane forecasters remind us that a well-established climate pattern puts us in an ongoing era of high activity for Atlantic hurricanes that began in 1995. Since that time, more than 70 percent of seasons have been above normal, including 2012. Historically, Atlantic high-activity eras have lasted 25-40 years, with the previous one occurring from the mid-1930's until 1970. Several inter-related atmospheric factors contribute to these high activity years, including warmer Atlantic Ocean temperatures, an enhanced West African monsoon and reduced vertical wind shear.

TROPICAL STORM (SUPER STORM) SANDY AND GLOBAL PROPERTY CAPACITY

Superstorm Sandy is on track to become the third most expensive hurricane in United States history behind only Hurricane Katrina and Hurricane Andrew. Insured losses for Sandy are running at $25 billion in claims paid so far, compared with $48.7 billion for Katrina and $25.6 billion (2012 dollars) for Hurricane Andrew. Estimates of total economic damages from Sandy are estimated to exceed $50 billion. While it is clear that the effects on the southeast coast from a storm like Sandy would have appreciably less impact, the worldwide catastrophic insurance marketplace will be affected from the Sandy loss.

For many years, staff has met with key underwriters from markets including Lloyd's of London, Swiss Re and Munich Re to highlight the District's significant hurricane resistant construction standards and hurricane preparedness plans. This reputation in the worldwide marketplace will continue to have a significant positive influence on carrier's decision as to where to put their CAT capacity and how much they will charge for such capacity. The fact is however that there is a finite amount of CAT capacity available in the worldwide insurance/reinsurance marketplace and as more entities access these markets, the more strain there is on capacity and pricing.

Taking into consideration to above-average activity in recent Atlantic hurricane seasons, as well as recent losses which significantly impacted the industry, including the 2011 Japanese Earthquake/Tsunami; Christchurch, New Zealand Earthquake and two seasons of significant losses in the southern United States from tornados, pricing and capacity issues are affecting renewal terms and conditions. South Florida as a major catastrophic-prone area is already suffering from the insurance industry's decision to restrict available coverage and charging more for the coverage which is available. Entities with large property values such as Miami-Dade County and Miami-Dade County Public Schools have taken the necessary steps to reduce double digit premium increases by assuming very large hurricane deductibles of $100 - $200 million per loss. With more insured losses worldwide, there will be additional stress on the worldwide insurance marketplace as it relates to available capacity and the cost to access that capacity.

UPDATE FROM 2012 RENEWAL

At the Board meeting of February 15, 2012, the Board authorized staff through its insurance broker, Arthur J. Gallagher Risk Management Services, Inc. to secure and bind maximum available limits of all-risk, replacement cost property insurance coverage in anticipation of obtaining $200 million in coverage limits, with annual premiums for all property insurance premiums and fees not to exceed $22.3 million, effective May 1, 2012. This authorization contemplated a decrease in coverage of $50 million from the previous program due to a hardening of the global insurance marketplace, and the strain on the District's Capital Budget from where property insurance premiums are typically paid.

At the Board meeting of May 16, 2012, staff reported that the authorized $200 million in coverage had been secured and bound, effective May 1, 2012 with all premiums of $21,969,025.60, including applicable state fees, representing savings from the authorized budgeted amount of $330,974.40. Because of the fiscal challenges to the District's Capital Budget, the decision was made to split the cost of the coverage with 56% of premiums for property and flood coverage being paid from the Capital Budget and the remaining 44% from the General Fund.

As part of commission caps in place pursuant to the District's contract with Arthur J. Gallagher Risk Management Services, Inc. (AJG), which became effective January 1, 2011 for a five-year term, consisting of 8% Retail Brokerage; 4.25% Domestic Wholesale Brokerage; and 6% International Wholesale, AJG and staff have negotiated specific additional services when carrier commissions exceed District contractual caps. As in the 2012-2013 renewal, 100% of commissions received in excess of caps are re-directed in value-added project which reduce District wide risk exposure. In 2011-2012 part of the $102,469 in available funding was spent to have appraisals completed for School and Non-School locations to benchmark proper replacement cost valuation as well as a comprehensive modeling report which was completed by Global Risk Miyamoto. This hurricane modeling report provided information which resulted in a 50% reduction in projected Probable Maximum Loss (PML) calculations under RMS v.11 which had been projecting $1.8 billion PML loss. This analysis was a key factor in staff's ability to secure limits for the current renewal at aggressive pricing in the marketplace.

Available funding from the 2012-2013 renewal with previous year's balance amounting to $197,798.97 has been allocated for additional appraisal services, as well as a four year contract with Exigis Risk Management Information Systems (RMIS) to provide the Office of Risk and Benefits Management with a state of the art risk management information system which will track exposures, claims, policies, certificates and trends while providing state of the art reports and on demand process analytics.

Authorization was also received at the Board meeting of May 16, 2012 to authorize the Superintendent to seek a letter of reasonableness of its current property insurance program from the State of Florida, Department of Insurance Regulation, or designee, pursuant to the requirements of Section 406 of the Federal Stafford Act. The provisions of this act require that the individual state's Insurance Commissioner certify that the property insurance carried by an insured is "reasonable" based upon market conditions.

Staff was again successful, as it has been for over 10 years, in obtaining a letter of reasonableness. This determination, dated September 4, 2012, proved to be more difficult than in previous years as Senior Attorneys for the Office of Insurance Regulation questioned the District's decision to purchase reduced limits of coverage than in previous years, resulting in a reduction in premium expenditures. Continuing to convince insurance regulators that $200 million of coverage, subject to a flat $100 million deductible per loss on total insurance values of approximately $8 billion will undoubtedly prove to be difficult.

PROPERTY VALUATION

The Office of Risk and Benefits Management works closely with Facilities Management staff to determine appropriate valuation of all District property on a per-square foot basis. Proper valuation is critical in all property transactions so that the insured is not subject to a penalty at the time of loss. Undervaluing or overvaluing can have a detrimental effect on the ability to negotiate renewal terms and conditions of large property valuations.

District property valuation is based on replacement cost values (replacing old with new at the time of loss), excluding land values, on a per-square foot basis. Total District square footage, as determined by the Florida Inventory of School Houses (FISH) reports is used in conjunction with the per-square foot replacement cost figure to determine total insured values (TIV) for insurance purposes. The values utilized for the past few years, using a blended rate for non-instructional facilities, elementary, middle and senior high schools, in conjunction with actual appraisals are as follows:

YEAR	VALUATION	TOTAL INSURED VALUE (TIV)
2006	$129/sq. ft.	$6.84 Billion
2007	$150/sq. ft.	$7.59 Billion
2008	$170/sq. ft.	$8.68 Billion
2009	$188/sq. ft.	$9.08 Billion
2010	$170/sq. ft.	$8.10 Billion
2011	$170/sq. ft.	$8.23 Billion
2012	$160/sq. ft.	$7.88 Billion
2013	$160/sq. ft.	$7.89 Billion

The overall reduction in reported replacement cost values from $9.08 Billion to $7.88 Billion from 2009 to 2012 reflects the reduction in cost of construction due to the economic downturn. In addition to physical buildings, these figures include valuations for all owned vehicles, mobile broadcasting equipment, WLRN aerials and antennas, as well as all furniture, fixtures and equipment (FF&E) in all facilities. To better value the District's investment in technology at schools and offices, the percentage of building values used for determining FF&E is being increased from 17% to 20%. For purposes of negotiating the renewal, the very small increase (.13%) represents a flat TIV from last year.

RECOMMENDATIONS FOR RENEWAL

As mentioned previously, the Office of Insurance Regulation (OIR) was skeptical of the District's decision to drop from $250 million of coverage for the 2011-2012 policy year to $200 million for the 2012-2013 policy year. While available funding from both the Capital budget and General Fund budget is expected to very tight for the upcoming 2013-2014 fiscal year, the risk of not receiving a reasonableness confirmation from OIR puts possible FEMA funding in peril.

Taking into consideration the amount of risk the District is assuming with a $100 million per loss hurricane deductible, the ability to prove to OIR that the District is willing to re-invest some additional money into the property program is vital. Therefore, staff is recommending renewal of its current $200 million program limits, along with a goal to replace the previously purchased layer of $50 million excess of the $200 million for a total program of $250 million in coverage limits. Taking into consideration the changes in the marketplace due to the 2012 Atlantic Hurricane season, and the recommended additional layer of coverage, staff is seeking authority for premium expenditures not to exceed $25 million for coverage effective May 1, 2013 to May 1, 2014. This strategy will represent a coverage increase of 20% (from $200 million to $250 million), with an increase in premium expenditures of 12%, and provide additional leverage with the OIR.

Contained in the 2012-2013 Millennial Access Platform (MAP) initiatives was MAP Property Insurance Program Re-Structuring. Outlined in the MAP is that the amount of property coverage secured by the District has ranged from a high of $750 million to a low of $150 million, with costs and terms subject to annual changes. Key worldwide carriers have been meeting with staff to review opportunities which could include multi-year commitments for coverage capacity as well as introduction of a loss sensitive strategy where carriers would refund a portion of premium in years without paid losses, and charge surcharges for years with paid losses.

The District's current program consists of layers of coverage beginning with a layer of coverage in the amount of $100 million, excess of deductibles and retentions. Two additional layers of $50 million excess of underlying layers of coverage to the current $200 million. Multiple carriers participate in each layer, with some carriers/markets participating in one, two or all three layers. Currently, 20 insurance markets provide coverage, with the lead markets being Lloyd's of London, Lexington Insurance Company and Swiss Re. In order to successfully re-structure the program, all participating carriers in a layer would have to agree to all terms and conditions of the changes, or the program would risk non-concurrence of coverage.

While key markets are still interested in discussing possible re-structuring of the program for the upcoming renewal of May 1, 2013, the losses from the 2012 Atlantic Hurricane Season has caused some reluctance among others. Staff will continue dialogue which hopefully could lead to a program with some certainty of coverage availability and pricing beyond one year at a time.

TERRORISM INSURANCE ACT AND COVERAGE

The Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) plays a key role in ensuring that property owners have available and affordable insurance options necessary to protect their assets against the financial consequences of foreign and domestic terrorist events. This Federal backstop is up for Congressional reauthorization in 2014 and is a major focus of the Risk and Insurance Management Society (RIMS) Governmental Affairs platform. Mr. Scott B. Clark, Risk and Benefits Officer served as International President of RIMS in 2011 and remains very active in the Governmental Affairs area of the society.

This coverage is crucial to adequately protect District assets. Financial markets which currently underwrite the outstanding $2.84 billion in Certificates of Participation (COP's), as well as markets which may underwrite portions of the General Obligation Bond (GOB) proceeds, will be very interested in the specifics of the District's property insurance program, including coverage for Terrorism. Staff is recommending that the District continue to purchase terrorism coverage for its 2013 - 2014 renewal. The cost of this coverage has continued to plateau with the current Federal backstop in place. The current annual premium for coverage which consists of $50 million in limits of property damage and $10 million of bodily injury coverage is $116,495. Staff is recommending that this coverage be renewed effective May 1, 2013 with annual premiums not to exceed $125,000.

NATIONAL FLOOD INSURANCE PROGRAM (NFIP)

Purchase of this coverage is a requirement of the Federal Stafford Act, which along with property insurance coverage provides access to FEMA public assistance grants. Premiums for this coverage are written on a building-by-building basis. Over the past two years, the Federal Government re-mapped Miami-Dade County's flood maps, with the result affecting 212 locations where rate increases for non Post Firm buildings averaged 4%. Other increases ranged from 9% for buildings rated as Post Firm (V) to 6% for Post Firm (A).

The annual budget for NFIP coverage has ranged from a high of $3.8 million in 2011-2012 to the current budget of $2.8 million for 2012-2013. The reduction was as a result of NFIP's implementation of the Preferred Risk Policy (PRP) which was designed to help ease the financial burden of affected properties. NFIP has gone on record indicating that premium reductions put in place as a result of PRP; however the program has continued to sink further into debt following the significant flood losses being reported in the aftermath of Sandy. At this time, staff is recommending that the NFIP budget for 2013-2014 remain at the expiring $2.8 million to cover all buildings in affected flood zones, with the understanding that if Congress raises rates mid-year, additional authority may be required.

At the time Tropical Storm Sandy hit the northeast coast of the United States, the NFIP program was already in debt by approximately $17 billion, stemming from significant claims arising after Hurricane Katrina in 2005. In January, 2013, Congress passed legislation which would increase the borrowing authority for NFIP by one-third from $20.775 billion to $30.425 billion. Congress just this past July, 2012 reauthorized the NFIP program's authorization extending the program until September, 2017.

STAFF AND BROKER MEETING WITH PROPERTY UNDERWRITERS

The value of meeting with representatives from key property markets cannot be overstated. A limited number of insurers possess needed catastrophic coverage capacity in the worldwide market. With storms Irene in 2011 and Sandy in 2012 significantly impacting the Northeast United States, it is anticipated that the eastern seaboard will be viewed as a prime hurricane risk, thus changing available coverages for that marketplace. Miami-Dade County Public Schools as one of the nations' largest property owners must have access to a significant portion of that sought after capacity.

To accomplish that, meetings will be held with current and prospective markets to secure needed capacity for renewal at the most competitive rates. The focus of these meetings will be to reiterate the building codes used to build educational facilities in South Florida and how these construction methods dramatically differ from buildings in the northeast affected by Tropical Storm Sandy. Discussions will also take place on the additional investment in the District's infrastructure which will be made over the next number of years as a result of the successful passage of the General Obligation Bond Issue.

It is important to re-state that the viability of the District's property coverage programs, including terrorism and flood must be acceptable to the holders of the District-issued Certificates of Participation (COP's), FEMA, and the financial markets which will invest in the District's General Obligation Bond (GOB) program. To accomplish these goals, staff will be meeting with various underwriters representing domestic and international markets, and will bind and secure all available coverage effective May 1, 2012, subject to a maximum property insurance premium of $25 million. An item confirming all coverage terms, premiums and conditions will be brought back to the Board meeting of May 8, 2013.

RECOMMENDED: That The School Board of Miami-Dade County, Florida:

1. Authorize staff, through Arthur J. Gallagher Risk Management Services, Inc., to secure and bind maximum available limits of all-risk, replacement cost property insurance coverage in anticipation of obtaining $250 million in coverage limits, with annual premiums for all property insurance premiums and associated fees not to exceed $25 million, effective May 1, 2013, with payment of such coverage to be funded from the District's property insurance budget, with a full report including confirmation of coverages, carriers, deductibles, costs and terms to be submitted to the Board its meeting of May 8, 2013

2. Authorize staff, through Arthur J. Gallagher Risk Management Services, Inc., to secure and bind terrorism coverage in the amount of $50 million property damage/$10 million bodily injury, effective May 1, 2013 with an annual premium not to exceed $125,000, including state fees, with payment of such coverage to be funded from the District's property insurance budget; and

3. Authorize renewal of flood insurance coverage with the National Flood Insurance Program (NFIP), through Arthur J. Gallagher Risk Management Services, Inc., for all properties required by the Federal Government to be covered with estimated premiums not to exceed $2.8 million for coverages effective for the 12-month period of May 1, 2013 to May 1, 2014.

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