



MEMORANDUM

June 15, 2012

**TO:** Board of Mayor and Aldermen

**FROM:** City Administrator Eric S. Stuckey  
Assistant City Administrator Russ Truell

**SUBJECT:** Insurance Escrow Deposit

**Purpose**

The purpose of this agenda item is to inform the Committee of a proposed escrow deposit with our new insurance carrier, Travelers Insurance.

**Background**

The Board of Mayor and Aldermen recently approved a contract with Travelers Insurance to cover the city’s insurance requirements for property, casualty, liability and workmen’s compensation. Typically, insurance carriers require some form of collateral or credit enhancement to cover the cost of possible “run off” claims at the end of the annual contract. Travelers requested a letter of credit from the City. Because of the uncertainty in the banking industry and financial markets, the cost for letters of credit, even for financially strong entities like the City of Franklin, is quite high relative to the interest that is earned on deposits. For that reason, City staff asked Travelers to be creative and find an alternative method to satisfy their credit requirement: either a direct deposit with the company or a joint interest-bearing bank account.

To their credit, Travelers agreed to accept a deposit from the City as an alternative. To offset the loss of interest that the city would receive on those funds, Travelers applied a discount to the workmen’s comp premium. This is an arrangement that is beneficial to the City and still satisfies the insurance company. The total amount of deposit will be \$378,554.

**Financial Impact**

No impact to the General Fund, as premium discount offsets opportunity cost of deposits.

**Options**

Approve or disapprove the proposed advance deposit with the insurance company.

**Recommendation**

Staff recommends approval.

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**Sold Proposal**

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KEY DATES	Commencement Date	Billing Frequency	Billing Basis
<b>Deductible Plan</b>			
Deductible Plan Losses	July 01, 2012	Quarterly	Paid
Deductible Plan Claims Handling Reimbursement Charges			
Workers Compensation	July 01, 2012	Quarterly	Paid
Deductible Plan Administrative Expense Reimbursement Adjustment	January 01, 2014	Annually	As per Expenses Part of Cover Page
<b>Non-Loss Responsive Premium(s)</b>			
Non-Loss Responsive Premium(s) Adjustment	January 01, 2014	Annually	As per Non-Loss Responsive Premium part of the Cover Page

- Paid Basis means the amount of each loss actually paid within your plan layer.

IN CONSIDERATION OF OUR OFFERING A DEDUCTIBLE PLAN TO YOU AS PART OF THE LOSS RESPONSIVE RATING PLAN COMPONENT OF OUR PROPOSAL, YOU REPRESENT TO US, AS PART OF YOUR ACCEPTANCE OF OUR PROPOSAL, THAT YOU WILL REIMBURSE US FOR DEDUCTIBLE PLAN LOSSES, ALLOCATED LOSS ADJUSTMENT EXPENSES, DEDUCTIBLE PLAN CLAIMS HANDLING REIMBURSEMENT CHARGES, DEDUCTIBLE PLAN ADMINISTRATIVE EXPENSE REIMBURSEMENT AMOUNTS, APPLICABLE PREMIUM TAXES (IF ANY) AND ANY OTHER DEDUCTIBLE PLAN CHARGES IN ACCORDANCE WITH THE TERMS OF THIS PROPOSAL AND THAT YOU WILL COLLATERALIZE YOUR REIMBURSEMENT OBLIGATION USING COLLATERAL ACCEPTABLE TO US IN FORM, CONTENT, ISSUER AND AMOUNT. YOU UNDERSTAND AND AGREE THAT THIS REPRESENTATION TO US BY YOU CONSTITUTES A MATERIAL REPRESENTATION AND THAT YOUR WILLINGNESS TO PROVIDE US WITH THIS REPRESENTATION IS A MAJOR REASON WHY WE ARE OFFERING YOU A DEDUCTIBLE PLAN AS PART OF OUR PROPOSAL.

**COLLATERAL REQUIREMENT**

	Cash Collateral
Amount Required for All Policy Years	\$378,554
Currently Holding	\$0
Additional or (Return) Amount Due	\$378,554
<b>Collateral Schedule</b>	
Amount Due July 01, 2012	\$378,554

With respect to any form of Collateral other than any Letter of Credit we are currently holding, should your insurance program with us be cancelled or non-renewed, we may at our sole option require you to substitute as Collateral a Letter of Credit satisfactory to us in form, content, issuer and amount for the full amount of such Collateral.

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You shall provide such Letter of Credit within fifteen (15) days after your receipt of our notice of the need for any such change in Collateral.

We and you agree that prior to a default we may deplete the cash Collateral and apply such funds against your WC Deductible Plan Obligations. If we require additional cash Collateral and you fail to deliver such additional cash Collateral, we may stop depleting the cash Collateral we hold and bill you for any Obligations. Such actions shall in no way affect the continuing validity of our security interest in the remaining cash Collateral.

**CASH COLLATERAL ADJUSTMENT**

The amount of cash Collateral held for this Policy year will be adjusted, subject to the Collateral and Remedies Section of the Agreement, pursuant to the formula set forth below.

Cash Collateral = ((Incurred Deductible Losses X (1 + Deductible LCF)) X Loss Development Factor) – ((Deductible Losses X (1 + Deductible LCF)))

Losses referenced in the formula are valued as of the Adjustment Dates noted below. The Loss Development Factors referenced in the formula above are also set forth below. "LCF" refers to Loss Conversion Factor.

**Workers Compensation and Employers Liability**

<u>Adjustment Date</u>	<u>LDF</u>
As of 01/01/14	1.161
As of 01/01/15	1.080
As of 01/01/16	1.050
As of 01/01/17	1.034
As of 01/01/18	1.026
As of 01/01/19	1.021
As of 01/01/20 and annually thereafter	1.000

We will immediately adjust the amount of additional cash Collateral we require pursuant to the formula if, at any time between the scheduled dates referenced above, the amount of cash Collateral we are holding falls below \$75,711, and you shall deliver to us such additional cash Collateral as set forth in the Collateral and Remedies Section of the Agreement.

In addition, we may require of you at any other time between adjustments an increase in the amount of cash Collateral we hold, or in the amount of any Letters of Credit we take as a substitute for the cash Collateral. The amount of the increase will be determined by us in the good faith exercise of our business judgment. Within fifteen (15) days after we have given you written notice of such an increase in cash Collateral, you will deliver to us the additional cash or increase in the amount of the Letters of Credit as is acceptable to us.

**SUBSTITUTION OF COLLATERAL**

**WITH RESPECT TO THE CASH COLLATERAL:**

Subject to your payment of an Administrative Fee as set forth below, you may substitute at any time for the cash Collateral a Letter of Credit (in addition to any other Letter of Credit we may be holding to secure your Obligations to us) which complies with the terms of the Agreement.

$$\text{Administrative Fee} = \$13,000 \times \frac{\text{Cash Collateral Balance at Substitution Date}}{\text{Total Cash Collateral Paid By You}}$$

The Administrative Fee generated by this formula is a fee for the Agreement for this program effective date only. Should a Letter of Credit be substituted for the cash Collateral at any time, a Total Administrative Fee will be assessed to you. This Total Administrative Fee will be the sum of your Administrative Fees for all Agreements for all program years.