REPORT TO THE LEGISLATURE

OWNER CONTROLLED INSURANCE PROGRAM STATUS REPORT

APRIL 2009

Prepared by the California Department of Transportation
Division of Construction
Office of Risk Management

Report to the Legislature

Owner Controlled Insurance Program
Status Report
April 2009

Purpose

This is the third annual report prepared in accordance with the Budget Act of 2006/07 which states:

1. ***Owner Controlled Insurance Program.*** By April 1 of 2007, 2008, and 2009, respectively, the Department of Transportation (Caltrans) shall report to the Joint Legislative Budget Committee and the policy committees on transportation on the following:

    - The type and value of projects included in the pilot.
    - The amount that Caltrans would have paid contractors for comparable insurance coverage in the absence of an Owner Controlled Insurance Program (OCIP), as identified in documentation submitted with contractors' bid statements.
    - The amount the department paid in insurance premiums, deductibles, program administration, and any other OCIP-related costs incurred during the pilot.
    - The estimated net cost or benefit of implementing the pilot, as identified by comparing contractors' estimates for insurance costs in the absence of an OCIP to the amount the department paid in insurance-related costs under the OCIP.
    - An assessment of the projects that were best suited for inclusion in an OCIP and the projects that were least well suited, in terms of cost-effectiveness.

Type and Value of Projects Included in the Pilot

The fiscal year 2006/07 budget bill provisions limit the size of the OCIP pilot program to projects totaling no more than $750 million in estimated capital cost of construction. Eight projects were scheduled to be included in the program to comprise the $750 million. Because the project awarded costs have been considerably below cost estimates, a project has been added to the list presented in last year's report to help the program reach its dollar value goal. This project is the Yerba Buena Island Transition Structure (YBITS), part of the San Francisco-Oakland Bay Bridge Seismic Safety Project. The current total estimated project construction costs equal $655 million. More projects may be added in the future to obtain a $750 million Rolling Owner Controlled Insurance Program (ROCIP).

Caltrans developed and applied selective risk management screening criteria to update the list of candidate OCIP projects. The type of projects include highway and bridge projects that range in construction size from $15 million to over $180 million and are geographically located throughout California. Four projects have been awarded to contractors while four others have had bids submitted and opened as of this report. Exhibit 1 below shows the projects included in the OCIP and their status.

Exhibit 1 - Status of OCIP Project Enrollment

Caltrans Rolling Owner Controlled Insurance Program Project Status Summary Report As of 01/05/09										
Status Info	R6 65 03-333814	R6 10 03-166624	03 10 03-166813	R6 680 04-253794	R6 680 04-[illegible]	03 680 04-253783	03 15 08-[illegible]	R4 101 04-[illegible]	YBT8-1 04-012084	Total Estimated Project Construction $ mil
Advertised	3/10/08	5/12/08	7/28/08	6/30/08	9/22/08	9/29/08	9/29/08	10/20/08	8/11/08	
Pre-Bid Meeting	3/20/08	N/A	N/A	N/A	N/A	N/A	N/A	N/A	NA	
Addendum	4/14/08	6/27/08	N/A	8/6/08	N/A	N/A	N/A	N/A	NA	
Bid Opening	**5/21/08**	**7/3/08**	**9/25/08**	**8/19/08**	**12/10/08**	**12/16/08**	**12/11/08**	**12/17/08**	**7/14/09**	
Award	6/18/08	7/17/08	10/6/08	9/2/08	TBD	TBD	TBD	TBD	TBD	
Approval	6/30/08	8/08/08	10/23/08	9/16/08	TBD	TBD	TBD	TBD	TBD	
Pre-Construction Meeting	8/12/08	8/27/08	12/2/08	9/23/08	TBD	TBD	TBD	TBD	TBD	
Notice to Proceed	9/2/08	9/26/08	1/2/09	11/3/08	TBD	TBD	TBD	TBD	TBD	
Insurance Credit Data Received	**90%**	**70%**	**No**	**50%**	**No**	**No**	**No**	**No**	**No**	
Low Bid (in millions)	$137	$15.5	$131.6	$37	$37	$27	$51.8	$38	$180 (estimated)	$655<$750
Original Engineer's Estimate (in millions)	$216	$40	$153	$61	$47	$46	$7M	$56	$180	
Contractor	DeSilva Gates/ FCI	Griffith Company	Atkinson Contractors, LP	Bay Cities Paving	TBD	TBD	TBD	TBD	TBD	

Identification of Contractor Insurance Costs in Absence of an OCIP

Contractors and subcontractors participating in the OCIP are contractually obligated to remove insurance costs from their bids. Caltrans developed contract provisions instructing the contractors and subcontractors on how to identify and remove their insurance costs. Contractors and subcontractors use a worksheet, "ROCIP Form 1" to calculate the premiums they would have paid in the absence of the OCIP.

At the time of this report, Caltrans continues to receive worksheets as contractors are enrolled on the first three projects. A number of worksheets from subcontractors are still being submitted. For cost comparison purposes, this report uses only costs associated with the three projects for which limited data is available.

In the absence of an OCIP, calculations to date show contractors would have charged Caltrans $1,517,216 for insurance on the three projects in Exhibit 2. Caltrans anticipates that this amount will rise substantially as more worksheets are submitted and as more projects are enrolled into the ROCIP. Exhibit 2 below shows identified contractor credits to date.

Exhibit 2 - Preliminary Contractor Insurance Credits

Contract No.	Description	Project Value	Contractor Credits
03-3338U4	State Route 65 Lincoln Bypass	137,000,000	1,102,758
07-166824	Interstate 10 HOV Lanes	15,500,000	265,574
04-253794	Interstate 680	37,000,000	148,884
TOTAL		189,500,000	1,517,216

(Note: credits are incomplete. The broker OCIP administrator is still awaiting documents from various contractors.)

In the traditional method of insuring construction risks, in which contractors provide their own insurance, these costs would have been passed through to Caltrans with a markup for contractor profit and overhead. Markup is not included in this report, but most construction sources concede that a contractor's markup usually ranges from 10 percent to 15 percent.

Contractor credits include premium costs for general liability, workers' compensation, and "umbrella" or "excess" liability insurance for these projects. These credits are the amounts the contractors would have paid to their insurers and subsequently included in their bids for non-OCIP projects. In an OCIP, the contractors credit to Caltrans insurance costs they otherwise would have paid by excluding them from their bids.

OCIP-Related Costs

OCIP-related costs incurred on the ROCIP pilot program consist of Caltrans staff time, consultant service fees, and OCIP broker/administrator fees over a period of nearly two years. Costs for these services total approximately $1.5 million of which approximately 25 percent is attributable to the three projects in Exhibit 2. Many of these costs have involved set-up activities, including development of procedures, information system creation, insurance placement for the entire duration of the ROCIP and more. OCIP-related costs expended to date ($0.75 million/year) are lower than original estimated costs of $1.352 million per year. As more projects are enrolled into the ROCIP, the rate of OCIP expenditures may increase to the level more consistent with original estimates.

In addition to the OCIP-related costs, the direct cost of the OCIP consists of premiums paid to the insurers. Insurance premiums attributed to each project are calculated on construction value

and paid to the insurance company in full as the project is enrolled into the ROCIP. Because of delays in receiving contractor premium credit worksheets, and the fact that the program is "loss sensitive" (costs are ultimately determined by losses), cost comparisons at this time are inaccurate as to ultimate cost. Such comparisons understate the contractor credits and likely overstate the ultimate OCIP comparative cost.

Exhibit 3 shows costs incurred by the OCIP. Premium amounts shown for the primary OCIP are for the fixed costs only and do not include losses, of which there have been none. However, Caltrans will be responsible for losses up to an "aggregate stop loss" maximum. For the entire ROCIP, maximum *potential* losses could reach an estimated $9.904 million. Caltrans' experience on other OCIPs has shown very low losses; Caltrans anticipates similar results from this pilot program.

Exhibit 3 – OCIP-Related and Direct Expenses

Cost Item	Program Amount	Amount allocated to currently enrolled projects	Comment
OCIP Administrator	$173,000	$43,250	The OCIP insurance broker/administrator is responsible for most of the processing functions and insurance placement. Initial startup costs include marketing insurance coverages, setting up management information system, preconstruction and pre-bid meeting attendance, and presentations to contractor groups. Much of these costs will be amortized over the life of the program.
Caltrans Staffing	$840,000	$210,000	Work on this program is performed principally by the Caltrans Office of Risk Management (ORM), on an "additional assignment" basis. Staff has been involved with this program since 2005. Initial cost is high due to start-up activities. This cost is expected to substantially decrease in future implementation.
Risk Management Consulting	$487,000	$121,750	Consultants with specialized expertise have been involved with the program since 2006 and have assisted and augmented ORM staff in many areas, including broker procurement, program design, development of handbooks, manuals and guidelines, workshops, contract review and revision, marketing, and other areas. A number of these costs will be amortized over the life of the program and beyond.

Primary OCIP premiums (Fixed Cost)	$718,205	$718,205	As this is a loss-sensitive program, high losses will increase the primary premium up to an aggregate maximum for the program. Fixed cost will increase as more projects are awarded and enrolled into the ROCIP. Currently, only three projects are enrolled.
$25 million Excess Liability OCIP premiums (Fixed Cost)	$388,000	$388,000	Fixed OCIP cost for the $25 million excess liability layer. Instead of requiring the contractors to carry this limit, Caltrans purchases this coverage for them under the OCIP.
$275 million Excess Liability OCIP premiums (Fixed Cost)	$665,000	$0	In implementing an OCIP, it is customary to carry high excess liability limits. Caltrans has chosen to purchase an additional excess liability limit of $275 million for the program. This protection is a business decision and reflects prudent risk management. Caltrans has no intention to offset this cost with contractor credits. Most contractors do not purchase coverage of such magnitude and, therefore, could not provide credits. Nevertheless, Caltrans anticipates that ultimately cost saving at the primary coverage level will offset the cost of the excess liability protection.
Total OCIP premiums and related costs	$3,271,205	$1,481,205	The OCIP cost allocated for the enrolled projects ($1,481,205) is the number being used to compare to contractor bid credits for a more accurate cost comparison.

Estimated Net Cost or Benefit

For the three projects shown in Exhibit 2, the $1,481,205 estimated incurred OCIP cost compared to the $1,517,216 estimated contractor credits indicates a net benefit of $36,011. Both estimate costs will increase as program data develops, and the net benefit may increase or decrease. Additional contractor bid credits for contracts already awarded shall be reported in the near future thereby increasing the contractor credit amount. OCIP costs will increase as losses, if any are paid.

Assessment of Individual Projects in Terms of Cost-Effectiveness

All projects selected seem well suited for inclusion into Caltrans' ROCIP. The three highway construction projects for which enrollment is substantially complete are still in the early stages of construction. Insufficient data exists to determine if any projects have characteristics that render

them best-suited for inclusion into the ROCIP or least suited in terms of cost-effectiveness. Caltrans will be able to make a more accurate assessment of project inclusion and cost-effectiveness as more enrollment data is received and all projects are enrolled into the ROCIP.