

# **Office of Inspector General**

**City of New Orleans**

## **Evaluation of City Property and Casualty Insurance Program**

**E. R. Quatrevaux  
Inspector General**

**Final Report**  
April 26, 2012

OFFICE OF INSPECTOR GENERAL  
CITY OF NEW ORLEANS



ED QUATREVAUX  
INSPECTOR GENERAL

April 26, 2012

Re: Evaluation of City Property and Casualty Insurance Program

I certify that the inspector general personnel assigned to this project are free of personal or other external impairments to independence.

A handwritten signature in blue ink, appearing to read 'E.R. Quatrevaux', is positioned above the printed name.

E.R. Quatrevaux  
Inspector General

# Evaluation of City Property and Casualty Insurance Program

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## EXECUTIVE SUMMARY

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The Office of Inspector General of the City of New Orleans (OIG) conducted an evaluation of the City's policies and practices relating to the management of property and casualty risks, including the risk of damage or loss caused by flood, fire, natural disaster, etc. The objectives of the evaluation were to determine whether the City prudently managed these risks and to evaluate procurement and contracting practices relating to an insurance producer of record.

The City managed its property and casualty risks primarily through the purchase of property insurance and National Flood Insurance Program (NFIP) flood insurance, at a cost of \$1.6 million and \$300,000 per year, respectively. The City selected policies with the dual goals of providing insurance coverage and meeting standards set by the federal government to maintain eligibility for federal assistance in the event of a future disaster. In 2007 the City was certified by the Louisiana Department of Insurance as having "reasonable" insurance coverage, sufficient to meet federal requirements. Our review of City insurance policies found that:

- The statement of values (a list of covered properties) for the City's master property insurance policy was out of date and contained errors and deficiencies.
- The City maintained insurance policies that appeared inconsistent with the City's overall approach to managing property and casualty risks.

The City purchased insurance policies through a producer of record that acted as the City's agent. The producer helped the City solicit quotes from insurers, select coverage levels, purchase policies, and make renewal payments. The contract stipulated fees for service up to an annual maximum of \$80,000, although the City automatically paid the maximum fee without requiring documentation of the services provided. The producer was also entitled to commissions on flood insurance policies, which in 2011 came to \$60,000 in additional compensation. In early 2011 the City solicited proposals for a new producer of record contract. The City selected a proposal but did not execute a new contract before this evaluation was completed. Our review of the City's management of the producer of record and the selection process for a new producer found that:

- The City did not manage the producer of record contract to maximize the value of the producer's services or provide sufficient oversight to ensure that the work was commensurate with the fees.
- The selection process for a new producer of record did not generate price competition.
- The selection committee did not explain the reasons for the proposal ratings, obscuring the decision making process.

Based on these findings, we recommended the following steps for the City to improve the effectiveness and efficiency of the property and casualty insurance program:

1. The City should request that the State review the City's property and flood insurance program to verify continuing eligibility for Stafford Act waiver certification.
2. The City should undertake the necessary steps to develop an up-to-date and accurate statement of values for its master property insurance coverage.
3. The City should develop a risk management plan for the property and casualty program.
4. The City should develop a new request for proposals (RFP) for a producer of record contract.
  - a. The RFP should solicit competitive prices for a fee-based contract.
  - b. The RFP should include clear standards for evaluating qualifications.
  - c. The selection committee should adhere to the instructions in Executive Order MJL 10-05 by providing written explanations of numerical scores.
5. The City should improve oversight of the producer of record and include clear performance standards in the contract.

*A draft of this report was provided to the Risk Management Division, City Attorney's Office, and Chief Administrative Office for review and comment prior to publication. The City's Response is appended in full to this report.*

*Relevant portions of the City response to this report follow each recommendation; all are direct quotes excerpted from the City's official response to the internal review draft.*

## I. OBJECTIVES, SCOPE, AND METHODOLOGY

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The Office of Inspector General of the City of New Orleans (OIG) conducted an evaluation of the City's policies and practices relating to the management of property and casualty risks, including the risk of property losses caused by flood. The objectives of this evaluation were to determine whether the City prudently managed its property and casualty risks through the purchase of insurance or other means, and to evaluate procurement and contracting practices relating to the use of a producer of record for insurance.

The scope of this evaluation included insurance policies and other activities that fell within the City's property and casualty risk management program, including the contract for a producer of record to assist with the procurement of insurance policies. Evaluators reviewed risk management activities and insurance policies in place during 2011 and examined solicitation and contract documents from 2006 through 2011.

Evaluators interviewed the City's Risk Manager, representatives of BRK Insurance, Inc. and AmWINS Brokerage of Georgia, LLC, as well as officials at the Louisiana Department of Insurance and Governor's Office of Homeland Security and Emergency Preparedness (GOHSEP). Evaluators reviewed documents provided by the aforementioned parties, the City's Bureau of Purchasing, and Fidelity National Property and Casualty Insurance Company. Documents included insurance policies; commission information; solicitation documents; proposals submitted by various respondents; evaluations of proposals, contracts and extensions; and invoices and billings from the current producer of record.

The evaluation was conducted in accordance with the Principles and Standards for Offices of Inspector General for Inspections, Evaluations, and Reviews.<sup>1</sup> This report includes findings and recommendations intended to improve the management of property and casualty insurance, improve procurement and contract oversight practices, and eliminate unnecessary costs.

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<sup>1</sup> Quality Standards for Inspections, Evaluations, and Reviews by Offices of Inspector General, *Principles and Standards for Offices of Inspector General* (Association of Inspectors General, 2004).

## II. INTRODUCTION

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Risk management, according to the Public Risk Management Association (PRIMA), is “the process of identifying, evaluating, selecting and implementing actions to eliminate or reduce harm.”<sup>2</sup> Once risks have been identified and evaluated, a risk manager must decide whether to transfer a risk by purchasing insurance or to retain the risk and maintain reserves to self fund any losses. This decision should be made through a deliberate process that uses historical data to analyze potential loss in terms of severity and frequency and systematically reviews the cost of available alternatives. In all cases, comprehensive risk management also entails steps to reduce uncertainty, prevent accidents, and minimize risks. Examples of significant risks that could result in economic loss to the City of New Orleans include:

- Property loss caused by fire, theft, vandalism, accidents, natural disasters, etc.;
- Legal liability caused by actions of City employees and officials, or conditions of City-owned properties;
- Extra expense to maintain services, remove debris and perform cleanup after a disaster;
- Workers’ compensation costs caused by injuries to employees; and
- Criminal or dishonest acts of employees or others.

The City’s Risk Manager, who heads the Risk Management Division in the City Attorney’s Office, is responsible for developing policies and implementing programs to control and minimize the City’s losses from accidents, disasters, and other events. This includes responsibility to manage the City’s insurance policies and self-insurance programs. The Risk Management Division consists of three City employees: the Risk Manager and two Claims Adjusters.

The major risk categories handled by the Risk Manager were property and casualty, liability for damages caused by accidents or actions of City employees, unemployment, and workers’ compensation. With a few exceptions, the City did not purchase insurance for liability risks in 2011. The City self funded losses and claims from motor vehicle accidents, premises and other types of liability, unemployment, and workers’ compensation. These programs are considered “self-insured.”<sup>3</sup> The primary insurance policies the City purchased were to cover damage to City property from fire, wind, flood, and other causes.

### PROPERTY AND CASUALTY INSURANCE

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In 2011, the City paid a producer of record under a 2009 contract to assist the City’s Risk Manager in the placement of property and casualty insurance.<sup>4</sup> The producer of record consulted with the Risk

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<sup>2</sup> PRIMA risk management glossary, [www.primacentral.org](http://www.primacentral.org).

<sup>3</sup> The City budgets for anticipated annual costs of workers’ compensation, unemployment, and minor accident claims, but does not maintain reserves to fund other liability risks.

<sup>4</sup> The term “producer of record” refers to a licensed insurance agent authorized by the City to place specified insurance coverage on behalf of the City.

Manager to determine insurance needs, solicited quotes from insurance underwriters or wholesalers, met with the Risk Manager to select policies, and handled the placement of insurance in accordance with the Risk Manager's instructions. Most of the City's major property and casualty policies were purchased through the producer of record, though the Risk Manager purchased some smaller policies directly from wholesale brokers.<sup>5</sup>

The property and casualty insurance program included two major policy types: specialized flood insurance underwritten by the federal National Flood Insurance Program (NFIP) and general property insurance underwritten by commercial insurance companies. The City's program also included a variety of minor policies such as employee and public official dishonesty bonds, fine art insurance (for the New Orleans Museum of Art), special events insurance (for Gallier Hall), boiler and machinery insurance, and accident insurance for volunteers. Premiums for the program's policies totaled about \$2.3 million per year in 2011, with about \$1.6 million spent on general property insurance, \$300,000 on flood insurance, and a total of \$400,000 for the other various policies.

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## FEMA DISASTER ASSISTANCE ELIGIBILITY REQUIREMENTS

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Decisions about the City's property insurance coverage were based in part on requirements imposed by regulations promulgated under the federal law known as the Robert T. Stafford Disaster Relief and Emergency Assistance Act (Stafford Act), which established the Federal Emergency Management Agency (FEMA) Public Assistance program.<sup>6</sup> The City has relied heavily on the FEMA Public Assistance program to repair damage to City-owned property caused by Hurricanes Katrina and Rita and must meet FEMA Public Assistance program requirements to maintain eligibility for this assistance in future disasters. As a condition of eligibility, federal regulations require the City to maintain insurance to protect against future property loss from the same types of hazards.<sup>7</sup>

The City purchased two types of insurance in 2011 to satisfy FEMA requirements: NFIP flood insurance and general commercial property insurance.

### A. National Flood Insurance Program

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FEMA regulations required the City to maintain coverage through the National Flood Insurance Program on all properties for which the City received disaster aid for flood damage. NFIP is a federal program administered by FEMA to provide flood insurance in high risk areas that the commercial insurance market is unwilling to cover. Coverage limits and premium rates are set by NFIP, although consumers purchase the policies through commercial agents. The maximum coverage available through this program is \$500,000 for a building and \$500,000 for its contents.

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<sup>5</sup> In 2011, the Risk Manager purchased five policies directly, totaling less than \$40,000 in premiums. In the recent past, the Risk Manager purchased larger policies directly from wholesalers, including a master property policy for all City-owned property.

<sup>6</sup> 42 U.S.C. §5121-5206.

<sup>7</sup> 44 C.F.R. §206.252-253.

In 2011, the City purchased individual flood insurance policies for 80 properties from NFIP, with new policies added on an ongoing basis as repairs were completed on storm-damaged properties. Not every City-owned property was insured; the City did not purchase individual flood policies for properties that were vacant or that had not been repaired from prior damage. In 2011, the City's flood policies provided a total of \$62 million in building and contents coverage with a combined \$1.1 million deductible.

## B. General Property Insurance

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FEMA regulations call for past recipients of disaster assistance to procure property insurance coverage for the full amount of the FEMA assistance they were eligible to receive in past disasters. The coverage available to the City through NFIP, capped at \$500,000 per building and limited to flood damage, provides only a portion of the coverage contemplated by FEMA rules. The City is therefore required to purchase additional property insurance through the commercial marketplace to satisfy FEMA's requirements.

The City satisfied the FEMA requirement for additional insurance by purchasing a master property policy at a cost of about \$1.5 million per year. The master policy insured most City-owned properties, which the City valued at a total of \$763 million in 2011. This insurance covered multiple hazards, including fire, vandalism, wind, and flood, but provided only limited coverage for catastrophic events like hurricanes. The total amount of recovery under the policy from a single occurrence was capped at \$50 million, far less than the total \$763 million in insured value for the property. The maximum total payout for damages caused by catastrophic events was even lower, with recovery capped at \$30 million for earthquakes, floods, and named storms. In addition to lower recovery limits, coverage for catastrophic events was also limited by high deductibles; rather than the \$50,000 deductible for most hazards, flood damage and damage caused by a named storm, including wind damage, were each subject to a separate \$10 million deductible.

The City's combined coverage from NFIP and the master property policy falls far short of insuring against the full extent of potential damage caused by a hurricane or other disaster. The limitations on the City's coverage reflect the unavailability of insurance against such high magnitude risks and underscore the importance of maintaining eligibility for federal disaster assistance, as discussed below.

## STAFFORD ACT CERTIFICATION

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Although FEMA regulations are intended to require individuals and communities to purchase insurance coverage for disaster risk rather than rely on federal assistance, the rules acknowledge that in high-risk areas some types of commercial insurance may not be available or may be available only at extraordinary cost. The regulations state that the FEMA Regional Administrator "shall not require greater types and extent of insurance than are certified . . . as reasonable by the appropriate State insurance commissioner."<sup>8</sup> Greatly increased insurance costs and unavailability of certain types of insurance on the commercial market following Hurricanes Katrina and Rita led the Louisiana

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<sup>8</sup> 42 U.S.C. §5154(a)(2). In: Letter to President George Bush, August 10, 2007; "RE: Stafford Act Certifications in Louisiana."

Commissioner of Insurance to invoke this clause to modify insurance requirements for certain government and non-profit organizations. In 2007 his office produced a letter that set the standards these organizations were required to meet in order to be certified as having “reasonable” insurance coverage and therefore eligible for future disaster aid. The letter was updated in 2010 with minor revisions.<sup>9</sup>

The Commissioner’s certification process applies to property and flood insurance, the main coverage types relevant to hurricanes and tropical storms. After reviewing data on median insurance expenditures for different types of government and non-profit organizations in coastal states, he defined a “reasonable” level for each type based on the cost of the insurance premiums. For local governments, including the City of New Orleans, the Commissioner determined that the reasonable outlay for insurance premiums was 0.33 percent of the annual operating budget. The mandated outlay amount must be spent on flood coverage through the NFIP program and on commercial property coverage (including wind but not flood) up to replacement cost for the covered property. Any remaining funds must be used for flood coverage in excess of NFIP limits. Local governments must be reviewed by the Department of Insurance and receive a certification of compliance with these requirements. They must remain in compliance to be eligible for future disaster assistance.

The Department of Insurance, in coordination with the Governor’s Office of Homeland Security and Emergency Preparedness (GOHSEP), reviewed the City’s flood insurance and master property insurance policy in 2007 and certified that the City met the defined expenditure standard. In effect, the letter from the Commissioner of Insurance stated that as long as the City maintained sufficient qualifying insurance expenditures, it would be eligible for federal aid in the case of a subsequent disaster. The City’s compliance has not been officially reviewed or re-certified since 2007, but the Risk Manager continues to use the standard set by the Commissioner to guide the acquisition of property and flood insurance. Based on the City’s 2011 operating budget of \$488 million, the 0.33% standard required the City to spend \$1.6 million on qualifying property and flood insurance. According to the Risk Manager, the City met this standard in 2011.

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<sup>9</sup> Letter to President George Bush, August 10, 2007; “RE: Stafford Act Certifications in Louisiana.” Letter to President Barack Obama, July 20, 2010; “RE: Revised Criteria – Stafford Act Certifications in Louisiana.”

### III. FINDINGS

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#### THE CITY'S INSURANCE POLICIES

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**FINDING 1. THE STATEMENT OF VALUES FOR THE CITY'S 2011 MASTER PROPERTY POLICY WAS OUT OF DATE.**

The largest portion of the City's property and casualty program costs was allocated toward the master all-risk property policy, which covered most City-owned properties at a cost of about \$1.5 million.<sup>10</sup> The properties insured under this policy in 2011 were listed on a statement of values, which included descriptions and values for 316 properties at 208 distinct addresses.<sup>11</sup> The total insured value of all properties on the 2011 list was \$763 million.

The statement of values was maintained by the Risk Manager, who coordinated with other departments to track changes and make updates. This list formed the basis of the master property policy, as it defined which properties were covered and the value of each. Insurers relied on this statement of values to model risks, estimate potential exposure and losses, and determine the City's premium cost.

The 2011 statement of values the City provided to insurers had not been fully updated to reflect changes following Hurricane Katrina. Although values had been revised for properties that were repaired after Katrina, the list still included pre-storm values for damaged properties that had not been repaired. For example, the Municipal Auditorium continued to carry a listed value of \$50 million despite massive flood and wind damage. The World Trade Center building had a listed value of \$33.9 million, despite being partially gutted and in a state of general disrepair.

Although the amount spent on property insurance is prescribed by the Commissioner of Insurance, the actual coverage provided for that cost can vary. Maintaining an accurate statement of values with current information on each property is important in order to maximize the value of the City's property insurance. In the event of a loss, payment from the insurer is based on the *lower* of the actual amount of loss or the stated value of the property. For this reason, overstated property values, which may increase the premium, do not provide any increased protection from loss. By the same token, understated property values limit the policy's effectiveness in mitigating risks such as fire, leaving the City vulnerable to non-covered losses.

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<sup>10</sup> The master property policy was purchased in layers, with several different insurers each providing partial coverage up to the total coverage amount. This let the City purchase the desired coverage level while allowing multiple insurance companies to spread the risk. The City's 2011 policy was divided into seven layers, with Lexington, Ironshore, Lloyd's, and Maxum Specialty insurance companies providing parts of the overall policy. AMWins, a wholesale insurance broker, coordinated the policy so that despite the layered arrangement, there was one overall set of terms and conditions that defined the coverage, exclusions, limits, and deductibles.

<sup>11</sup> Multiple buildings at the same address were listed separately in the statement of values.

**FINDING 2: THE STATEMENT OF VALUES FOR THE CITY'S 2011 MASTER PROPERTY POLICY CONTAINED ERRORS AND DEFICIENCIES.**

A representative of the wholesale insurance broker who coordinated coverage under the City's master property policy told evaluators that shortcomings in the City's 2011 statement of values made it difficult for insurance companies to calculate premiums. The insurance premiums were developed by entering information from the list into a computer model that estimated potential losses. The wholesaler stated that missing or incomplete information in the City's list disrupted the model, leading to increased loss assumptions and higher premium cost. In his estimation, improving the accuracy, completeness, and detail in the statement of values would be the easiest, most cost-effective way for the City to increase the value of the master property policy.

The City's list commonly lacked such basic elements as the addresses or zip codes of properties and contained information for certain properties that was entered in a format unreadable by the model. Many properties were classified as "address unknown," because the City did not properly format the list. For example, a community center was classified as "address unknown," because the file included the note "Phase I" in the address field rather than the description field. Other addresses were rejected because the word "Saint" was abbreviated "St." or because unnecessary periods and spaces were added. According to a memo from the wholesaler to the City's Risk Manager, almost 20% of the insured value was classified as "address unknown" due to a combination of uncorrected errors and improper formatting.

In addition, over half of the insured value was classified as "unknown construction type," due to the same types of miscommunications, errors, and missing data. For example, City Hall was classified as unknown construction type, because the line on the City spreadsheet that should have listed construction type instead said "AAA sprinkler." The construction type entry for the New Orleans Museum of Art stated "1910, 1970, 1993" (the dates of construction and renovation) instead of describing the building.

In addition to containing basic errors in data entry, organization, and formatting, the City's statement of values did not include much of the necessary information. A typical statement of values lists the address, building value, contents value, construction date, building type, number of stories, and construction materials, as well as information about risk abatement systems like sprinklers, hurricane bracing and building elevation. Vague, incomplete information undermined the City's list, with entries such as the World Trade Center, which listed construction type simply as "concrete." More complete information would lower the uncertainty reflected in the risk models, which would likely lower the City's loss assumptions and premium.

A representative of the producer of record told evaluators that the City received a template from the wholesale broker in 2010 showing what information was needed and how to organize it, but it is clear from 2011 policy documents that the necessary steps to correct and complete the list were not taken.<sup>12</sup>

**FINDING 3: THE CITY PURCHASED SEPARATE PROPERTY INSURANCE FOR THE MAHALIA JACKSON THEATER, ADDING SIGNIFICANT COST WITH NO APPARENT RATIONALE.**

Almost all City-owned properties were covered under the master property policy in 2011, but the City purchased a separate policy to provide \$35 million in coverage for the Mahalia Jackson Theater for the Performing Arts at a cost of nearly \$100,000 per year. The wholesale broker who coordinates the City's property insurance told evaluators that including the theater in the master property policy would cost significantly less than maintaining the separate policy.

The \$35 million individual policy for the theater stands in stark contrast to the master policy, which provided just \$30 million in City-wide coverage for flooding or a named storm. Rolling the theater into the master policy would therefore represent a decrease in coverage for the building in the event of a disaster. Nonetheless, the decision to spend more to provide a much higher level of property insurance for one building than for all other City-owned properties should be based on a sound risk management rationale.

Both the City's producer of record and the wholesale broker told evaluators that they asked the City's Risk Manager to explain the City's rationale for insuring the theater separately but had not received a clear explanation. The City might have a sound rationale for the decision, but when evaluators asked the Risk Manager for an explanation, she said only that the decision was made by the previous mayor's administration.

**FINDING 4: THE CITY PURCHASED LIABILITY INSURANCE ON A VACANT PARCEL OF LAND WITH NO APPARENT JUSTIFICATION.**

As discussed in the introduction, the City did not, with limited exceptions, purchase insurance to cover the risk of legal liability for injuries caused by City employees or conditions at City-owned properties. The City self-insured for liability risk at almost all City-owned properties, with the striking exception of Lincoln Beach, a vacant parcel of land along Lake Pontchartrain. In 2011, the City paid about \$5,000 to purchase liability insurance for this single property.

The City's Risk Manager told evaluators that her predecessor initiated the coverage because the land was "an attractive nuisance," with a "high probability for a wrongful death suit," and that "access to the land was through a railroad track," and the "land had no supervision." These factors do not provide a convincing rationale for singling out this parcel as a unique liability risk. The decision to insure one City property but not others that may pose high risks did not appear to be based on a well-reasoned risk management strategy.

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<sup>12</sup> Documents from the 2012 policy renewal clearly show that the statement of values still had not been significantly updated or improved by that time.

## THE PRODUCER OF RECORD CONTRACT

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In the insurance industry, brokers and agents are typically compensated either through commissions based on a percentage of insurance premiums, or through fee-for-service agreements. Commissions are common for small insurance policies for which a 10 to 20 percent commission paid to the agent is commensurate with the amount of paperwork, time, and service provided. As the size of the premium increases, however, the amount of effort and service provided by the agent does not increase proportionally. For larger insurance policies, a fee-for-service arrangement will therefore provide a better value for the customer.

Commission-based compensation adds a disproportionate cost to larger insurance policies and has other disadvantages: (1) commissions are tied to premiums, giving the agent a disincentive to find the lowest cost insurance; (2) commissions are embedded in premiums and may not be easily discernible; and (3) commissions are paid regardless of whether the agent provides ongoing service.

On October 1, 2009, the City contracted with an insurance agency, H & G Insurance, Inc. (H & G)<sup>13</sup>, to act as the City's producer of record for property and casualty insurance under a one-year contract. The 2009 contract was extended into 2011, at which time, with the City's approval, H & G assigned its interest in the contract to BRK Insurance Group, LLC (BRK).<sup>14</sup> Under this contract, the producer of record consulted with the Risk Manager to determine insurance needs, solicited quotes from insurance underwriters or wholesaler brokers, met with the Risk Manager to select policies, placed coverage, and renewed existing policies. All services were provided on an on-request basis, and the City was not required to place all insurance policies through the producer.

The City's producer of record contract called for the producer to be paid a maximum fee of \$80,000 annually and specified that property insurance policies would be written "net-of-commission," meaning that the premiums charged to the City could not include any commissions paid to the producer.<sup>15</sup> The City's Risk Manager told evaluators that the producer of record contract included fee-based compensation because paying commissions on those policies would cost more than a reasonable fee-for-service. She noted that the City's master property insurance policy alone cost nearly \$1.5 million in 2011, and that a 10 percent commission on those premiums alone would add up to \$145,000, far more than the \$80,000 maximum fee.

The producer of record actually received far more than the \$80,000 maximum fee in 2011; although all other policies were net-of-commission, the contract specified that the producer could receive commissions for placing NFIP flood policies. The Risk Manager explained that the City allowed these commissions because the federal government establishes the terms of the NFIP flood insurance and

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<sup>13</sup> H&G's application listed The Kennedy Financial Group as a disadvantaged business (DBE) partner, and committed to 50% DBE participation on the contract.

<sup>14</sup> The same individuals providing services under the H & G contract continued to provide the services after the contract assignment.

<sup>15</sup> For instances in which an insurance underwriter would not agree to write a policy net-of-commission, the contract allowed the producer to credit those commissions toward the maximum fee or return them to the City.

does not allow these policies to be written net-of-commission. The producer of record placed the City's NFIP policies through Fidelity National Property and Casualty Insurance Company and received a 20% commission. In 2011, the producer placed NFIP flood insurance policies for the City totaling about \$300,000 in premium cost, of which about \$60,000 was paid to the producer in commissions. As a result, the producer was paid about \$140,000 under the contract in 2011.

**FINDING 5: THE CITY DID NOT MANAGE THE PRODUCER OF RECORD CONTRACT TO MAXIMIZE THE VALUE OF THE PRODUCER'S SERVICES OR ENSURE THAT THE AMOUNT OF EFFORT OR VALUE OF DELIVERABLES WAS COMMENSURATE WITH THE FEES.**

The contract called for the producer to be paid up to a maximum of \$80,000 based on invoices for services provided. The contract included the following payment provision:

As a prerequisite to payment, the Contractor shall submit to the City monthly invoices detailing the services provided in connection with this Agreement.

In practice, the producer and the City ignored the payment provision cited above and treated the \$80,000 maximum price as a flat fee. Each monthly invoice was for \$6,666.67 and simply stated "Broker Fee" with no explanation or detail. Lacking any documentation of the services provided or hours worked, the Risk Manager could only guess at how much time and effort was actually required of the contractor. In an interview with evaluators, she speculated that obtaining price quotes for the master property policy likely required significant effort from October through December each year, but other policies were generally renewed from year to year and required little work. In 2011, BRK received \$80,000 in fees and about \$60,000 in commissions, but the City had no assurance that this \$140,000 compensation bore a reasonable relationship to the services provided.

In addition to eroding accountability, the flat fee had the disadvantage of eliminating incentives that could have benefited the City. The contractor received the same compensation regardless of the amount of work done and therefore had no financial incentive to devote more than the minimum level of effort required. This payment arrangement was not designed to motivate the producer to devote extra time and energy to such tasks as ensuring that underwriters were given complete and accurate information and attempting to generate more competition for the City's insurance. The City missed an opportunity to maximize the value of the contract by not establishing clear expectations for service and tying payments to services performed or deliverables provided.

A BRK principal told evaluators that the firm used a wholesale broker to place the City's all-risk master property coverage. The wholesale broker, rather than BRK, therefore performed some of the services called for in the contract, such as soliciting quotations from insurance companies, and received commissions for the placements. These commissions added to the City's cost of insurance but were essentially hidden in the premiums.<sup>16</sup> The contract itself was silent with respect to wholesale broker fees and did not require this additional cost to be disclosed. The wholesale commissions made it even

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<sup>16</sup> A BRK representative told evaluators that he negotiated a commission rate with the wholesale insurance broker, AmWINS Brokerage of Georgia, LLC, and recalled that the rate agreed upon was 4%. A 4% commission on the master property policy would add approximately \$60,000 to the cost of the producer of record contract.

more difficult for the City to determine whether it was paying a reasonable amount for the services provided under the producer of record contract.

A lack of standards or measures to assess the contractor's work compounded the unfavorable compensation structure of the contract. The contract included a general list of services to be provided but did not indicate how the contractor would be evaluated. No performance standards were defined, and no reporting mechanisms were included. According to one of the BRK principals, the City did not perform any evaluation of the firm's work in the two plus years they have served as producer of record. The lack of performance standards, evaluations, and reports of work performed compromised the City's ability to ensure that its goals were met and that resources were spent efficiently.

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### THE 2011 REQUEST FOR QUALIFICATIONS

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In January 2011, the City released Request for Qualifications (RFQ) No. 2340-01019 to award a new contract for a property and casualty insurance producer of record. The services sought were considered professional services, which are procured pursuant to the request for proposals process spelled out in Executive Order MJL 10-05.

**FINDING 6: THE SELECTION PROCESS DID NOT GENERATE PRICE COMPETITION FOR A NEW PRODUCER OF RECORD CONTRACT.**

The standard solicitation document for professional service contracting called for in Executive Order MJL 10-05 is a Request for Proposals (RFP). The executive order contemplates instances in which the City may release a Request for Qualifications (RFQ) to screen potential respondents on the basis of their professional qualifications prior to receiving proposals. However, the Executive Order calls for an RFQ to be followed by an RFP, which seeks competitive price proposals, rather than as the final step before awarding a contract.

Because the solicitation documents for the insurance producer of record were styled as a Request for Qualifications rather than a Request for Proposals, cost was not included as a factor in selecting a proposal. The Risk Manager explained to Evaluators that the RFQ was written based on the understanding that state law did not permit the City to award a fee-based contract to an insurance producer. This understanding stemmed from a bulletin issued by the Louisiana Commissioner of Insurance in August 2010, cautioning insurance producers and customers that fee-based, non-commission producer agreements violated state insurance laws and that a producer could not agree to rebate commissions to a customer. The Risk Manager assumed that the producer's compensation would have to be based on commissions, and therefore fee was not included as a factor in the selection process.

The City received seven proposals in response to the RFQ and evaluated the competing insurance agencies solely on the basis of criteria other than cost.<sup>17</sup> The City did not have the benefit of comparing proposed prices and therefore could not weigh cost along with other factors to select the agency offering the overall best value. The five-member selection committee chose the incumbent contractor, BRK, as the highest ranked proposer and began to negotiate the terms of a new producer of record contract.

In the time between the RFQ release and the selection of BRK, state law was changed to permit fee-based contracts. In response to the Commissioner's 2010 bulletin, and at the urging of local governments including the City of New Orleans, the Louisiana Legislature in 2011 enacted La. R.S. 22:1567, which specifically authorized entities meeting certain qualifications (including the City) to use fee-based contracts in lieu of paying commissions to property and casualty insurance producers. NFIP flood insurance falls under the purview of the statute and is eligible for fee-based contracting. Similarly, federal law does not prohibit insurance producers from rebating premiums for NFIP flood policies, which is common practice in other states, including Florida and California.

In September 2011, the Risk Manager told evaluators that the City was negotiating a new contract with BRK in which compensation for the all-risk property policies would be fee-based. Although changing the basis of compensation from a commission-based contract to a fee-based contract would produce significant cost savings, the City cannot be assured that the terms it negotiates with BRK on a sole-source basis would be as favorable as the terms available if the City solicited new proposals including fee information. There is no substitute for fair and open competition to maximize the value realized from spending public funds. Based on concerns about the compensation structure and selection process, evaluators requested that the City delay execution of a contract pending the release of this report.

**FINDING 7: THE SELECTION COMMITTEE DID NOT EXPLAIN THE REASONS FOR THE PROPOSAL RATINGS, OBSCURING THE DECISION MAKING PROCESS.**

The RFP process is intended to give public officials discretion to consider the qualifications of proposed personnel and other factors in addition to price when choosing a contractor to perform a professional service. The qualitative factors, such as relevant experience and performance history, should be well-defined and closely related to the contract requirements. The evaluation process should be rational and well-documented so that a competing vendor or a citizen can understand what factors were considered and how the selected proposal was chosen.

Executive Order MJL 10-05 requires the selection committee to evaluate proposals and document its process in writing, in accordance with the following provision:

The members on the Selection Committee shall first evaluate the proposals on the basis of criteria other than price. The members on the Selection Committee shall either

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<sup>17</sup> Responding firms were: Aparicio Walker & Seeling Inc. (AW&S), BRK Insurance Group LLC (BRK), Fontenelle & Goodreau Insurance LLC (F&G), Fulton Johnson Newman & Pittmann Insurance Agency Inc. (FJN&P), HUB International (HUB), McGriff Seibels & Williams Inc. (MS&W), and Swanson & Associates Inc. (S&A).

complete the numerical grading and provide a written explanation stating the reasons for the rating for each criteria, or if using the wholly qualitative evaluation criteria, the members shall provide a rating of a proposal as highly advantageous, advantageous, not advantageous, or unacceptable and state the reasons for the rating for each criteria.

The City’s producer of record RFQ used the following qualitative criteria and numerical grading scheme to evaluate proposals:

**Figure 1: Weighted Evaluation Criteria for RFQ No. 2340-01019.**

Evaluation Criteria	Maximum Score
Specialized experience and technical competence	45
Performance history, including, without limitation, competency, responsiveness, cost control, access to the insurance marketplace, work quality and the ability to meet schedules and deadlines	40
Willingness to promote full and equal business opportunities in accordance with the City’s State-Local Disadvantaged Business Enterprise Program	10
Maintenance of an office, residence, or domicile in Orleans Parish, to the extent permitted by law	5

Each of the five members of the selection committee prepared a written score sheet assigning a numerical score to each of the seven proposals for each of the four evaluation criteria. A composite scoring sheet was prepared showing the overall score assigned by each committee member to each proposal and totaling the members’ scores to produce a total numerical score. The proposals were then ranked by numerical score, with BRK achieving the highest score. Because no price proposals were solicited, the committee could not weigh the evaluation scores against price to determine the best value. BRK was therefore selected for the contract based on its numerical evaluation score.

The selection committee did not follow the Executive Order MJL 10-05 instructions to provide a written explanation stating the reasons for the numerical score assigned for each criterion. Four of the five members provided only numerical scores with no written comments. One member offered uninformative comments, none exceeding three words, which provided no meaningful explanation for the differences in the numerical scores. These comments were limited to: “can do work,” “can do services,” “can undertake work,” “capable,” “good history,” “good,” and “history.”

The scores assigned for maintaining an office in Orleans Parish and participating in the DBE program were related to specific information provided by proposers, but scores for the two primary criteria, qualifications and performance history, were not clearly related to objective differences among proposals. We calculated an average score for each proposal based solely on these two criteria, which accounts for 85% of the overall proposal score. The results, shown in Figure 2, indicate that the committee did not identify major differences among the proposers with respect to qualifications or performance history.

**Figure 2: Selection Committee Scores and Ranking Based on Qualifications and Performance History**

Firm	Rank (Based on criteria for experience and performance history)	Average score for specialized experience and technical competence (45 pts maximum)	Average score for performance history (40 pts maximum)	Combined average score for experience and performance history
BRK	1	41	36.6	77.6
FJN&P	2	41	34	75
MS&W	3	40	35	75
S&A	4	38	33	71
HUB	5	40	31	71
AW&S	6	39	31	70
F&G	7	36	33	69

Four out of the seven proposals received equal scores or were within one point of the others on the most heavily weighted criterion, specialized expertise and technical competence. The range of scores on performance history is also relatively narrow. These scores suggest that the committee had difficulty making meaningful distinctions among the firms.

The RFQ specifically evaluated access to the insurance marketplace as part of a firm’s performance history and asked respondents to describe their access to standard and excess markets. Responses to this question varied among proposers but were generally vague and hard to differentiate. For example, BRK, the top-ranked firm, provided no concrete examples or specific experiences, citing only “access to all standard markets and numerous regional and specialty markets.” Further, it indicated that it would “access non-admitted markets by utilizing the services of major excess and surplus brokers.” Market access is a valid consideration in selecting an insurance producer, but the selection committee would need substantive evidence of their ability to access markets rather than vague assertions to evaluate this factor properly.

The committee may have gathered additional information by contacting references or otherwise verifying the quality of services provided by firms, but the City provided no records to document such activities. With no written explanations from the selection committee, there is no way to determine whether and how non-quantifiable factors were considered, or if information not found in the proposal documents was used to score proposals. Without documenting the evaluation rationale, the available information does not meet the Executive Order’s intent of creating a transparent selection process.

## IV. CONCLUSION AND RECOMMENDATIONS

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### CONCLUSION

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The City's property and casualty program is an important component of the City's overall risk management efforts. It accounted for about \$2.5 million in expenditures in 2011, including payments to the producer of record and insurance premiums. The following recommendations address the findings in this report and suggest avenues for improvement in the management of the property and casualty program and the procurement of producer of record services.

### RECOMMENDATIONS

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**RECOMMENDATION 1: THE CITY SHOULD REQUEST A REVIEW OF ITS PROPERTY AND FLOOD INSURANCE PROGRAM TO VERIFY THE CITY'S CONTINUING ELIGIBILITY FOR STAFFORD ACT WAIVER CERTIFICATION.**

Ensuring eligibility for FEMA assistance in the event of a disaster is vital to the City's interests. The City's insurance coverage was reviewed in 2007, and the Commissioner of Insurance verified that it met the criteria for Stafford Act waiver certification, which is essential to maintaining eligibility for FEMA assistance. The City is not required to undergo another eligibility review unless a disaster occurs, but the Governor's Office of Homeland Security and Emergency Preparedness (GOHSEP) is willing to assist local governments with a voluntary review upon request.<sup>18</sup> The City would submit budget documents, insurance expenditures, and policy terms, and GOHSEP would verify that the City is currently in compliance with waiver requirements. The Risk Manager has exercised care to maintain the required levels of coverage, but obtaining a periodic review would provide another layer of assurance.

**CITY RESPONSE:** *"The Risk Manager develops a FEMA Insurance Obligations and Waiver Worksheet annually (a copy of the 2011 Worksheet is attached), which confirms that the City remains in compliance with the waiver requirements and no other certification is needed. We have confirmed this practice and our compliance with the Governor's Office of Homeland Security. Therefore, there is no need for the City to request recertification of the waiver from the Commissioner of Insurance at this time. However, we will continue to maintain dialogue with both the Governor's Office of Homeland Security and Commissioner of Insurance to evaluate whether updating this certification at some point in the future is advisable."*

**OIG COMMENT:** *The importance of the City's continuing eligibility for a Stafford Act waiver can be measured by the amount of federal aid received after Hurricane Katrina. Although not required, we believe that it would be prudent and responsible of the City to obtain periodic outside reviews of its eligibility.*

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<sup>18</sup> GOHSEP partners with the Department of Insurance for reviews and is the primary point of contact.

**RECOMMENDATION 2: THE CITY SHOULD UNDERTAKE THE NECESSARY STEPS TO DEVELOP AN UP-TO-DATE AND ACCURATE STATEMENT OF VALUES FOR ITS MASTER PROPERTY INSURANCE COVERAGE. (ADDRESSES FINDINGS 1 AND 2)**

At \$1.5 million, the City's master all-risk property insurance policy accounted for most of the cost of the property and casualty program in 2011. Although the City's primary objective for the master property policy appears to be maintaining Stafford Act certification compliance, the policy also provides coverage for less catastrophic risks. For example, building-specific incidents like fires are covered by the policy. To maximize the benefits of the policy, the City should consider not only the policy's role in compliance in the event of a citywide catastrophe, but also the coverage value the policy presents for other risks.

The statement of property values used to purchase the master policy has not been fully updated following Hurricane Katrina. By using overstated or understated values, the City may pay more than necessary for some properties or risk incurring uninsured losses. In addition to inaccurate valuations, the wholesale insurance broker who handled the placement of that policy indicated that deficiencies in the statement of values made it difficult for insurance companies to calculate premiums. Missing or incomplete information in the City's list disrupted the model used by insurers to price risk, leading to increased loss assumptions and higher premium cost.

Developing a more complete and accurate statement of values involves two separate and distinct tasks. The first task is to correct errors, fill in missing information, and fix formatting problems; this can be achieved in a relatively short time without specialized expertise. The wholesale broker has provided the City with a template and instructions on how to enter information that will make it accessible to the insurers' computer models.

The second task is to develop much more complete and detailed building information to improve the statement of values, and to assess the current values for properties.

An improved statement of values is a worthwhile investment that has the potential to improve the quality of coverage, gaining better value for the City's \$1.5 million annual premium.

*CITY RESPONSE: "... [D]evelopment of a comprehensive Statement of Values is currently underway and is a two-step, collaborative effort between the Risk Management Unit, Property Management, Capital Projects and Information Technology and Innovation (ITI). The first step involves identifying and electronically cataloging all properties including land, buildings, leases and servitudes owned by the City of New Orleans should be completed by August 2012. The second step involves a full assessment and/or appraisal of value for each property owned by the City, and has an expected date of completion of December 2013."*

**RECOMMENDATION 3: THE CITY SHOULD DEVELOP A RISK MANAGEMENT PLAN FOR THE PROPERTY AND CASUALTY PROGRAM. (ADDRESSES FINDINGS 3 AND 4)**

The City's property and casualty program appears to be aimed primarily at maintaining coverage required to qualify for the Stafford Act waiver certification. Ensuring eligibility for FEMA assistance is a vital objective, but the City would benefit from developing a coherent plan for managing property and casualty risks.

The Government Finance Officers Association (GFOA) recommends that governments develop a comprehensive risk management program that identifies, reduces, or minimizes risk to its property, interests, and employees. Developing such a comprehensive program is a substantial undertaking, but the City can begin by establishing standards to guide decisions about the types and levels of property and casualty insurance needed to protect the City. These standards should be based on an analysis of the frequency and magnitude of losses incurred and the cost of insuring against these losses.

This report found that the City maintained a separate property insurance policy on the Mahalia Jackson Theater and a liability policy for Lincoln Beach that appeared inconsistent with the City's overall approach to managing property and casualty risks. Establishing a risk management plan will give the City a logical framework for determining whether these and other insurance policies should be maintained.

*CITY RESPONSE: "The City will form an internal working group to develop a risk management plan for the property and casualty program that will include the risk philosophy and risk tolerance of the City. The working group will look to GFOA and other comparable institutions for guidance and standards to assess for use by the City."*

**RECOMMENDATION 4: THE CITY SHOULD DEVELOP A NEW REQUEST FOR PROPOSALS FOR A PRODUCER OF RECORD CONTRACT. (ADDRESSES FINDINGS 5, 6, AND 7)**

The City honored evaluators' request for delay and has not yet awarded a new contract based on the January 2011 RFQ. BRK is continuing to provide producer of record services under an extension of the 2009 contract, and the City's primary property and casualty insurance, the master all-risk property policy, has been placed for 2012. At this juncture, the City can either extend BRK's 2009 contract again or complete the negotiations with BRK to establish the terms of a new contract for 2012. Regardless of which option the City chooses for the current year, we recommend that the City develop an RFP for the award of a new contract for the upcoming year.

This report found that the 2011 RFQ did not generate price competition and that the selection committee did not document a coherent rationale for their numerical scores for qualifications or performance history. These deficiencies compromised competition and did not ensure that the selection process obtained the best value for the City. The following recommendations would help avoid these problems with a new RFP.

**PART (A): THE RFP SHOULD SOLICIT COMPETITIVE PRICES FOR A FEE-BASED CONTRACT.**

It is in the City's interest to pursue a purely fee-based contract, with no commissions. Commissions based on insurance premium rates make it difficult to discern the true cost of services and drive up costs.

A new fee-based contract should be structured according to a fee-for-service model. Rather than paying a set amount regardless of the work done, a fee-for-service contract would base payment on the level of effort for specific tasks or for specified deliverables. This compensation method provides an incentive to devote effort to the contract and holds the contractor accountable for specified tasks or deliverables.

In implementing this model, the RFP should ask respondents to propose one or more hourly billing rates and estimates of hours to be worked at each rate. The contract should include a key personnel clause to ensure that the individuals performing the work meet the qualifications stated in the proposal. In order to receive payment, the contractor should be required to submit itemized invoices, detailing the work hours, services performed, and individuals performing the work, or to produce agreed-upon deliverables. The contract may cap the maximum compensation either for specific tasks or for all services provided.

**PART (B): THE RFP SHOULD INCLUDE CLEAR STANDARDS THAT WILL BE APPLIED TO EVALUATE QUALIFICATIONS.**

The rationale for using an RFP process is to identify significant differences among proposers and allow decision makers to select the response that presents the best overall value rather than simply the lowest cost. In some cases, it makes sense to pay a higher price for a vendor based on a clearly demonstrated track record or qualifications. With respect to the producer of record contract, the producer's fee is far less than the cost of insurance, so the producer's ability to obtain more favorable terms from insurers should be a primary consideration. For this reason, the City should identify and evaluate objective evidence of ability to access the relevant insurance markets.

In the 2011 RFQ process, scores for proposers' qualifications and performance history did not vary considerably, indicating that the committee did not find significant differences among them. There is no sound reason to base a contract award on a slightly higher numerical score if proposers are, for all practical purposes, equally qualified. If a well-reasoned comparison of proposals produces no meaningful distinction between two or more competing vendors, the prudent decision is to choose the vendor offering the best price.

**PART (C): THE SELECTION COMMITTEE SHOULD ADHERE TO THE INSTRUCTIONS IN EXECUTIVE ORDER MJL 10-05 BY PROVIDING WRITTEN EXPLANATIONS OF NUMERICAL SCORES.**

This report found that the numerical scores assigned to proposals were not clearly supported by explanations of their relation to qualifications or performance history. Numeric ratings give the illusion of mathematical precision but often provide little insight into the reasoning behind the numbers.

When numbers are not clearly tied to measurable standards, they appear arbitrary and susceptible to manipulation and favoritism.

The Mayor's Executive Order, based on the American Bar Association's Model Procurement Code, communicated the importance of written explanations to demonstrate sound reasoning in the evaluation process. The City should ensure that selection committees follow the instructions in the Executive Order and include meaningful written explanations that allow vendors and citizens to understand the proposal rankings.

*CITY RESPONSE: "The City will develop a new RFP for a Producer of Record contract. The RFP will be released on or about April 25, 2012."*

**RECOMMENDATION 5: THE CITY SHOULD IMPROVE OVERSIGHT OF THE PRODUCER OF RECORD AND SHOULD INCLUDE CLEAR PERFORMANCE STANDARDS IN THE CONTRACT. (ADDRESSES FINDING 5)**

The City should be more active in evaluating and managing the producer of record contract. Evaluations of the contractor should be performed on an annual basis and corrective action taken as necessary to remedy any issues. The contractor should be required to comply with the terms of the current contract by submitting detailed monthly invoices describing the services performed.

The new contract should include clear performance standards and defined reporting mechanisms to track performance. A well constructed and managed contract is fundamental to ensuring that the City receives high quality services at a good value.

*CITY RESPONSE: "The City will include performance standards in the RFP and these items will become a part of the contract upon execution."*

## V. OFFICIAL RESPONSE TO THE INTERNAL REVIEW DRAFT

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The Office of Inspector General provides an internal review draft to any person or entity that is the subject of report findings or recommendations. Any written response submitted by a subject within 30 days after receiving the draft will be included in the final public report.

The OIG provided an internal review draft of this report to the City's Risk Management Division, City Attorney's Office, and Chief Administrative Office on February 22, 2012. Prior to finalizing the public report evaluators met with City personnel to discuss the report findings and recommendations. The City's response is included in its entirety in this section.

This public report reflects corrections and other changes made to the review draft based on the responses received from the report subjects.

*For OIG comment on City's response to Finding 3, see page 35.*

CHIEF ADMINISTRATIVE OFFICE  
CITY OF NEW ORLEANS

MITCHELL J. LANDRIEU  
MAYOR

ANDREW D. KOPPLIN  
FIRST DEPUTY MAYOR & CAO

April 12, 2012

Mr. Edouard Quatrevaux *Q 4/12/12*  
Inspector General  
Office of the Inspector General  
525 St. Charles Avenue  
New Orleans, Louisiana 70130

**Re: OIG Report on City Property and Casualty Insurance Program**

Dear Mr. Quatrevaux:

We thank you and your staff for this review of the City's property and casualty insurance program and for meeting with us for an in-depth discussion of your findings and recommendations.

Following are our responses to the specific findings in your report.

Finding #1: THE STATEMENT OF VALUES FOR THE CITY'S 2011 MASTER PROPERTY POLICY WAS OUT OF DATE.

The City is currently updating its Statement of Values to reflect changes to those properties damaged as a result of Hurricane Katrina. Some properties have been repaired or renovated, while others still require substantial improvements. Development of a updated, comprehensive Statement of Values is a two-step, collaborative effort between the Risk Management Unit, Property Management, Capital Projects and Information Technology and Innovation (ITI).

The first step involves identifying and electronically cataloging all properties including land, buildings, leases and servitudes owned by the City of New Orleans. ITI has committed resources from its Service and Innovation Team and Geographic Information System Team to assist in this effort. As of the date of this response, the City has identified and electronically cataloged 80% of its assets and this step should be completed by August 2012.

The second step is a full assessment and/or appraisal of value for each property owned by the City, which is time consuming as well as expensive. Accordingly, the City is developing a plan to best utilize its limited resources to effectively and efficiently complete this task and to prioritize the most important structures from a risk management perspective. In addition to resources from departments mentioned above, the City expects to call on its current contractors and the Assessor to assist in this effort. Expected date of completion is December 2013.

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PHONE 504.658.8600 | FAX 504.658.8648

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**Finding #2: THE STATEMENT OF VALUES FOR THE CITY'S 2011 MASTER PROPERTY POLICY CONTAINED ERRORS AND DEFICIENCIES.**

As stated above, the City is currently working on a comprehensive Statement of Values, which should address the errors and deficiencies. As additional information on City properties is gathered through this undertaking, we will update our Statement of Values. We will also standardize the format to ensure it includes the required information needed for a broker to most effectively market the City's master property program. Further, once the updated, comprehensive Statement of Values is developed we will increase oversight to make sure that errors do not reoccur.

**Finding #3: THE CITY PURCHASED SEPARATE PROPERTY INSURANCE FOR THE MAHALIA JACKSON THEATER, ADDING SIGNIFICANT COST WITH NO APPARENT RATIONALE.**

The City as owner of the Mahalia Jackson Theater entered into an operating agreement with Arts Center Enterprises – New Orleans, LLC (ACE) for the management of the facility. Pursuant to this operating agreement, the City is contractually obligated to maintain insurance and to promptly repair, replace, restore and reconstruct the Theater and return it to substantially the same form it existed prior to any casualty. That provision was an essential requirement articulated by the management company in order for the City to enter into the private-public partnership with them to manage the facility.

Because of this contractual requirement, the City determined that purchasing a stand-alone policy was the best way to meet its obligation. If the Theater were part of the city's master policy, then this contractual requirement would force the City to prioritize the repair of the Theater ahead of other, more critical, city infrastructure, which the City believes would not be in the City's best interests.

While we understand that the City's producer of record and wholesale broker may not have understood the City's goals with regard to this decision, we did provide this information as the basis of a sound rationale to the Office of Inspector General prior to the conclusion of this review and therefore disagree with the inclusion of this finding in this report.

**Finding #4: THE CITY PURCHASED LIABILITY INSURANCE ON A VACANT PARCEL OF LAND WITH NO APPARENT JUSTIFICATION.**

The Risk Manager continued to renew these policies covering vacant land known as Lincoln Beach based on the legal opinion of the previous Interim Risk Manager. The policies covering this parcel of land will expire on April 16, 2012. The Risk Manager has been authorized to non-renew these policies as of April 16, 2012.

**Finding #5: THE CITY DID NOT MANAGE THE PRODUCER OF RECORD CONTRACT TO MAXIMIZE THE VALUE OF THE PRODUCER'S SERVICES OR ENSURE THAT THE AMOUNT OF EFFORT OR VALUE OF DELIVERABLES WAS COMMENSURATE WITH THE FEES.**

Effective March 1, 2012 the Producer of Record monthly invoice will provide detailed information such as the service provided, the hours worked, and the monthly fee based on the annual contract amount. The current contract does not delineate or reference the commission between the broker and the wholesaler. The City did work with the broker in negotiating the lowest commission from the wholesale broker to secure the optimal cost savings to the City.

**Finding #6: THE SELECTION PROCESS DID NOT GENERATE PRICE COMPETITION FOR A NEW PRODUCER OF RECORD CONTRACT.**

The RFQ was issued January 2011 at which time the City was following an Advisory Letter issued by the Louisiana Commissioner of Insurance in August 2010 that explicitly prohibited a Producer of Record from waiving commission in exchange for charging a reduced fee as well as prohibiting insurance companies from providing quotes or issuing an insurance policy that is written "net of commission". As a result, the City was prohibited from producing an RFP that would generate price competition and to have followed the recommendation of the OIG in this regard would have put us in conflict with the state's chief regulator of the insurance industry. Such an RFP would have required us to willfully ignore the Commissioner's direction. Therefore, this finding about price competition should have been directed not at the City of New Orleans but to the Commissioner of Insurance and should have urged the Commissioner to withdraw his Advisory Letter.

Because the City strongly disagreed with the Commissioner of Insurance's guidance, we joined with other municipalities to pass legislation, House Bill 137, which took effect in August 2011 and allowed a Producer of Record to negotiate fees in lieu of commissions with a property and casualty insurer or a policyholder, giving cities like New Orleans the opportunity to save significant amounts.

Following passage of this legislation and after conferring with the Office of Inspector General regarding how to address the original RFP which was precluded from generating price competition, the City determined that the best course of action for the City was to extend its existing fee for service contract rather than award a new contract pursuant to that RFP process. The City is now, in 2012, about to issue a new RFP for a producer of record that includes the opportunity for price competition afforded by this important legislation that the City helped pass.

**Finding #7: THE SELECTION COMMITTEE DID NOT EXPLAIN THE REASONS FOR THE PROPOSAL RATINGS OBSCURING THE DECISION MAKING PROCESS.**

During the last two years, about 100 selection committee meetings have been held to select vendors to do business with the City. All of these meetings have been held in public, with many vendors and taxpayers in attendance. The discussion among committee members has often been extensive, and in some cases, lasted over more than one meeting. The decision of the selection committee can be summarized by the scores of the members, but the overall decision-making process encompasses all of the discussion between and among committee members. The City agrees that more detailed written explanations of the committee's decision making process would

be beneficial, and we are developing guidance for better capturing the group's rationale for its final selection decision.

The particular RFP discussed in this report did attract a number of well-qualified proposers and, as this report notes, it was hard to differentiate clear and obvious differences between the proposals. The selection committee met on more than one occasion, always in public, to review the strengths and weaknesses of the proposals. Mayor Landrieu's Executive Order created this open, transparent, public process where professional-minded discussion led to a judgment as to which proposal best suited the City, and the City remains committed to refining further an already much-improved process.

**Recommendation #1: THE CITY SHOULD REQUEST A REVIEW OF ITS PROPERTY AND FLOOD INSURANCE PROGRAM TO VERIFY THE CITY'S CONTINUING ELIGIBILITY FOR STAFFORD ACT WAIVER CERTIFICATION.**

In 2007 the City ("Applicant") received a Stafford Act Waiver from the Louisiana Commissioner of Insurance. On July 20, 2010 the Louisiana Commissioner of Insurance (copy attached) wrote to President Barack H. Obama: "If an Applicant obtains such coverage, satisfies the criteria contained herein, and receives, or has already received, a confirmation of the certification of a Stafford Act waiver request from me by separate letter, the reduction of eligible damages for a future disaster by the amount of damages eligible on the same property in a past disaster that is described in 44 C.F.R. 206.253(b)(2) (referred to by FEMA as the "5903 reduction") will not apply." He further wrote: "Applicants are advised that any certification made by me in response to their application for Stafford Act waiver will remain in full force and effect as long as the Applicant continues to obtain and maintain the insurance coverage consistent with the percent of budget criteria contained in this letter." The Risk Manager develops a FEMA Insurance Obligations and Waiver Worksheet annually (a copy of the 2011 Worksheet is attached), which confirms that the City remains in compliance with the waiver requirements and no other certification is needed. We have confirmed this practice and our compliance with the Governor's Office of Homeland Security. Therefore, there is no need for the City to request recertification of the waiver from the Commissioner of Insurance at this time. However, we will continue to maintain dialogue with both the Governor's Office of Homeland Security and Commissioner of Insurance to evaluate whether updating this certification at some point in the future is advisable.

**Recommendation #2: THE CITY SHOULD UNDERTAKE THE NECESSARY STEPS TO DEVELOP AN UP-TO-DATE AND ACCURATE STATEMENT OF VALUES FOR ITS MASTER PROPERTY INSURANCE COVERAGE.**

As noted under Finding 1, development of a comprehensive Statement of Values is currently underway and is a two-step, collaborative effort between the Risk Management Unit, Property Management, Capital Projects and Information Technology and Innovation (ITI). The first step involves identifying and electronically cataloging all properties including land, buildings, leases and servitudes owned by the City of New Orleans should be completed by August 2012. The second step involves a full assessment and/or appraisal of value for each property owned by the City, and has an expected date of completion of December 2013.

Recommendation #3: THE CITY SHOULD DEVELOP A RISK MANAGEMENT PLAN FOR THE PROPERTY AND CASUALTY PROGRAM.

The City will form an internal working group to develop a risk management plan for the property and casualty program that will include the risk philosophy and risk tolerance of the City. The working group will look to GFOA and other comparable institutions for guidance and standards to assess for use by the City.

Recommendation #4: THE CITY SHOULD DEVELOP A NEW REQUEST FOR PROPOSALS FOR A PRODUCER OF RECORD CONTRACT.

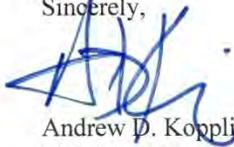
The City will develop a new RFP for a Producer of Record contract. The RFP will be released on or about April 25, 2012.

Recommendation #5: THE CITY SHOULD IMPROVE OVERSIGHT OF THE PRODUCER OF RECORD AND SHOULD INCLUDE CLEAR PERFORMANCE STANDARDS IN THE CONTRACT.

The City will include performance standards in the RFP and these items will become a part of the contract upon execution.

Thank you again for your partnership in helping us improve transparency and efficiency within the City of New Orleans.

Sincerely,



Andrew D. Kopplin  
First Deputy Mayor / Chief Administrative Officer  
City of New Orleans

Attachments

CITY OF NEW ORLEANS

2011 FEMA Insurance Obligations and Waiver Worksheet

Current Operating Budget	<b>\$488,558,029</b>		
Last Certified Financial Statement	\$511,762,000	The greater is used to calculate waiver requirements	
Assistance Expected			
Buildings & Contents		Category E	
<b>Current Insurance Coverage</b>			
Lexington	\$50,000,000	Excess of \$10,000,000 SIR	
NFIP Policies		Excess of Various Deductibles	
<b>Current Insurance Premiums</b>			
Lexington & Other Layers	\$1,527,750.00	Wind Deductible	\$10,000,000 SIR
NFIP	\$303,460.00		
<b>TOTAL PREMIUM</b>	<b>\$1,831,210.00</b>		
<b><u>Waiver Requirements</u></b>			
Type of Entity	Governmental		
Waiver %	0.33%	Of Operating Expense	
<b><u>Waiver Expenditure Requirements</u></b>	<b>\$1,612,241.00</b>		



LOUISIANA DEPARTMENT OF INSURANCE  
JAMES J. DONELON  
COMMISSIONER

July 20, 2010

President Barack H. Obama  
The White House  
1600 Pennsylvania Avenue NW  
Washington, DC 20500

RE: Revised Criteria - Stafford Act Certifications for Louisiana

Dear Mr. President:

This letter will supplement and restate my August 10, 2007 letter to former President George W. Bush concerning the criteria and methodology being used in Louisiana with respect to waiver requests submitted to me, as Commissioner of Insurance for the State of Louisiana, pursuant to the Robert T. Stafford Disaster Relief and Emergency Assistance Act, 42 U.S.C. § 5121, *et seq.* ("Stafford Act"). The Stafford Act authorizes you, as President, to provide disaster assistance through grants to state and local governments as well as certain eligible non-profit organizations (hereinafter referred to as "Applicants") damaged by Presidentially-declared major disasters. As a condition to receive the eligible disaster assistance, the Stafford Act requires the Applicant obtain and maintain "such types and extent of insurance...as may be reasonably available, adequate, and necessary, to protect against future loss to such property." 42 U.S.C. § 5154(a)(1).

However, the Stafford Act specifically provides that "[I]n making a determination with respect to availability, adequacy, and necessity under Paragraph (1), the President shall not require greater types and extent of insurance than are certified to him as reasonable by the appropriate State insurance commissioner responsible for regulation of such insurance." 42 U.S.C. § 5154(a)(2).

In my August 10, 2007 letter, I provided the criteria under which requests made to me for Stafford Act certifications would be considered for local governments and non-profit entities eligible for federal assistance as a result of damages sustained in Hurricane Katrina and/or Hurricane Rita. The purpose of this letter is to advise you, and all Applicants, of revisions that apply to applications for Stafford Act assistance for damages from Hurricane Katrina and/or Hurricane Rita and from any subsequent Presidentially-declared major disasters including, but not limited to, Hurricane Gustav and/or Hurricane Ike.

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Some of the modifications contained herein are the result of communications with representatives of the U.S. Department of Homeland Security, both at the Louisiana Transitional Recovery Office and in Washington DC (hereafter, "FEMA"). Among the issues discussed with FEMA were: (a) how my Stafford Act certification affects the treatment of an eligible Applicant's deductible in the event of a second disaster and (b) how my certification impacts the potential second-disaster recovery of an Applicant who has satisfied the Stafford Act by obtaining coverage through a blanket policy, insurance pool arrangement, layered arrangement or some combination of those options. In advance of my sending this letter, a letter was written to FEMA on August 21, 2009, informing it of my belief and understanding that a Stafford Act certification would impact each of those issues favorably for an eligible Applicant suffering subsequent disaster losses. (A copy of that August 21, 2009 letter is attached.) FEMA did not refute or contradict my position in its response thereto. Therefore, the following will include details concerning how my certification will affect an eligible Applicant's Stafford Act assistance in the unfortunate circumstance of a second disaster loss.

The aftermath of the unprecedented and devastating natural disasters of Hurricane Katrina and Hurricane Rita in 2005 and Hurricane Gustav and Hurricane Ike in 2008 remains significant. Local governments, as well as certain eligible non-profit organizations in the State of Louisiana, continue to struggle to carry out their missions to provide necessary and desirable public, educational, and charitable services. The availability and cost benefit of property and commercial flood insurance remains a serious concern for all of these entities.

Under the authority granted to me by the Stafford Act as the Commissioner of Insurance for the State of Louisiana, I hereby certify that commercial insurance coverage for the perils of flood and wind is not reasonably available to Applicants in order for Applicants to procure property insurance coverage for the full amount of their eligible disaster assistance to be received under the Stafford Act for damages sustained as a result of Presidentially-declared major disasters such as Hurricanes Katrina, Rita, Gustav and/or Ike. Under current insurance market conditions, the premium cost of flood insurance in excess of the coverage provided by the National Flood Insurance Program ("NFIP") and of wind coverage would require these Applicants to expend a substantially higher percentage of their annual budgets for property insurance than the median amount expended by similar entities and organizations regionally. In addition, many Applicants with large risks have been unable to obtain quotes for higher layers of excess flood insurance. To require Applicants to purchase coverage to the full extent of the eligible disaster assistance, if such coverage were even available at all, would impose such excessive expense on Applicants as to substantially impair their ability to carry out their missions to provide necessary and essential public, educational, and charitable services.

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Further, I hereby certify that insurers providing commercial property insurance coverage in the areas affected by Presidentially-declared major disasters such as Hurricanes Katrina, Rita, Gustav or Ike are often requiring policyholders to accept deductibles significantly higher in amount than those which were required prior to those storms. Under these circumstances, the insurance coverage is not reasonably available for amounts within these increased policy deductibles.

If an Applicant cannot reasonably obtain and maintain full property insurance coverage as typically required for their disaster assistance, an Applicant can and should obtain and maintain such property insurance coverage as can be purchased by a reasonable expenditure from its current annual operating budget. Such reasonable expenditure shall include the following:

A. An Applicant shall procure NFIP flood insurance coverage for building and contents for at least every facility that sustained flood damages in Hurricanes Katrina, Rita, Gustav and/or Ike and in any subsequent Presidentially-declared natural disaster. The amount of this coverage shall be the maximum amount available from the NFIP. The amount of premium dollars spent by an Applicant on NFIP flood insurance coverage and excess flood coverage should be included in the calculation of the percentage of budget amount described in the following paragraph.

B. An Applicant shall allocate a reasonable proportion of its current annual operating budget to the purchase of property insurance, including protection for wind and flood, for each of its properties that are the subject of Stafford Act public assistance grants. The reasonable percentage for each type of organization is set forth below. These percentages have been modified from those stated in the August 10, 2007 letter to President George W. Bush. These percentages are now based on the median that organizations of these types are spending as a percent of budget for property insurance premiums, as compared to the sixtieth percentile used in the August 10, 2007 letter. Further, statistics from coastal states were used, as compared to the national statistics previously used, in an effort to apply regionally relevant data.

On an annual basis, the Applicant shall procure property insurance coverage that, coupled with the premium dollars spent on NFIP and excess flood coverage, totals a premium equal to the specified percent of the Applicant's annual operating budget (exclusive of capital outlay) according to the prior year's certified audited financial statement or the same percentage of the Applicant's annual operating budget for the current year of post-disaster operations:

	ORGANIZATION	PERCENTAGE OF BUDGET
1.	Local Governmental	0.33%
2.	Elementary and Secondary Education	0.29%
3.	Post-Secondary Education	0.17%
4.	Health Care	0.26%
5.	Non-Profit Association	2.91%
6.	Non-Profit Trust	1.41%
7.	Non-Profit Religious	2.61%

C. An Applicant shall comply with the following requirements regarding the expenditure of the designated percentage of its current annual operating budget for the purchase of property insurance coverage:

1. Procure NFIP coverage as described above;
2. Procure property coverage, including wind and other perils (exclusive of flood), up to the replacement cost; and
3. With remaining funds, procure excess flood coverage.

To the extent that an Applicant purchases coverage through a blanket insurance policy, insurance pool arrangement, layered policy arrangement or some combination of those options (hereafter, "blanket-type policy"), any such coverage must be scheduled in order to meet the waiver requirement. If an Applicant obtains such coverage, satisfies the criteria contained herein, and receives, or has already received, a confirmation of the certification of a Stafford Act waiver request from me by separate letter, the reduction of eligible damages for a future disaster by the amount of damages eligible on the same property in a past disaster that is described in 44 C.F.R. §206.253(b)(2) (referred to by FEMA as the "5903 reduction") will not apply. The elimination of the 5903 reduction as a result of my certification for blanket-type policies has been confirmed in the attached August 21, 2009 correspondence to FEMA, and FEMA has not refuted it.

I have certified herein that coverage within the increased deductibles being required by insurers is not reasonably available. To be eligible for a certification, an Applicant shall not have a deductible for property insurance coverage that exceeds 15%. Further, this property insurance coverage should not include a combined deductible with any business interruption coverage. If an Applicant obtains coverage that satisfies the criteria contained herein (whether of a blanket-type policy or not) and receives, or has already received, a confirmation of the certification of a Stafford Act

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waiver request from me by separate letter, that certification shall have the effect of making the amount of the Applicant's deductible an element of the eligible Stafford Act assistance in the event of a subsequent disaster. In other words, a Stafford Act certification issued by me to an Applicant will eliminate any reduction of the Stafford Act grant assistance available to the Applicant in a subsequent disaster based on the amount of the Applicant's deductible. The inclusion of the deductible as eligible for subsequent disaster assistance as a result of my certification has been confirmed in the attached August 21, 2009 correspondence to FEMA and FEMA has not refuted it.

The premium cost of business interruption insurance (i.e., time element) coverage shall be separate from and shall not be included in the calculation of the premium to comply with the percentage provided above for the purchase of property insurance. Likewise, the premium costs for other lines of insurance (i.e., workers' compensation, general liability, automobile liability, etc.) shall not be included in the calculation of the premium to comply with the property insurance percentage unless it can be shown that this expense is being incurred so as to meet a requirement of a FEMA public assistance grant.

D. The Applicant shall provide documentation demonstrating compliance with the criteria established herein as part of the application process. Applications are to be addressed to Disaster Recovery Division, Governor's Office of Homeland Security and Emergency Preparedness ("GOHSEP"), 415 North 15th St., Baton Rouge, LA 70802. An application checklist is published at [www.louisianapa.com](http://www.louisianapa.com). Telephone inquiries may be made to the Public Assistance Division at 225-338-6782 or by fax to 225-338-3259. All Applicants requesting Stafford Act certifications with respect to multiple properties or multiple project worksheets shall be required to complete and return a spreadsheet containing information concerning the type and amount of coverage obtained. The spreadsheet form will be provided by GOHSEP upon the Applicant's request and the completed form will be made part of the Applicant's application.

This certification is intended to apply retroactively with respect to all Applicants that have already obtained Stafford Act waiver certifications from me, provided those Applicants have continued to obtain and maintain compliance with the percent of budget criteria contained in my August 10, 2007 letter to President George W. Bush or the percent of budget criteria contained herein. If an Applicant has already purchased property insurance on any or all of its property that is the subject of a FEMA public assistance grant and has not previously obtained a certification from me, and has exceeded the new percentage of budget requirements set forth herein, this certification shall not authorize the Applicant to reduce the existing property insurance coverage already purchased. That Applicant may, however, submit an application requesting a Stafford Act waiver certification for consideration with respect to increased deductibles that may have been incurred (consistent with the 15% upper limit stated herein).

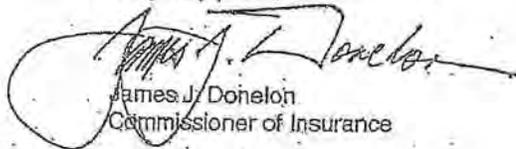
President Obama  
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Applicants are advised that any certification made by me in response to their application for Stafford Act waiver will remain in full force and effect as long as the Applicant continues to obtain and maintain the insurance coverage consistent with the percent of budget criteria contained in this letter. Applicants are advised, again, that until modified, amended or altered by me, the criteria contained herein applies to Stafford Act assistance requests for damages resulting from Hurricanes Katrina, Rita, Gustav and/or Ike as well as any subsequent Presidentially-declared major disaster.

I issue this certification based on percentage of budget due to the substantial quantity of Stafford Act public assistance grants that have been filed, and will be filed, by qualifying entities. This certification and the requirements enumerated herein shall remain in effect until otherwise modified, altered, or amended by me. I will review this certification and requirements periodically and advise you of any modifications, alterations, or amendments accordingly as I deem appropriate.

With best wishes and kindest personal regards, I remain

Very truly yours,



James J. Dohegan  
Commissioner of Insurance

cc: Hon. Bobby Jindal, Governor  
Janet Napolitano, Secretary U.S. Dept. of Homeland Security  
James Walke, Director, Disaster Assistance, FEMA  
Tony Russell, Administrator, Region VI, FEMA  
Michael Karl, Acting Director, Louisiana Transitional Recovery Office, FEMA  
Tracey Phillips, FEMA  
K. Mike Winner, FEMA  
Mark Cooper, Director, GOHSEP  
Mark S. Riley, Dep. Director, Chief of Staff, GOHSEP  
Mark DeBosier, Dep. Director-Disaster Recovery Division, GOHSEP  
Al Ater, Chief Dep. Commissioner, LDI  
Ed O'Brien, Deputy Commissioner, LDI  
Warren E. Byrd, Esq., Executive Counsel, LDI  
Ben Moss, LDI  
W. Shelby McKenzie, Esq.  
Margaret L. Tooke, Esq.

## COMMENT ON THE CITY OF NEW ORLEANS RESPONSE

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The City argues that Finding 3 should have been excluded because the Administration satisfactorily explained the need for the Mahalia Jackson Theater's property insurance policy during the exit conference. Although we accept that the explanation provided is satisfactory, the finding was included in this report because the Risk Manager was unable to provide an explanation and the rationale was provided only after our draft report was provided to the City.