

City of
Gainesville

Inter-Office Communication

December 8, 2005

TO: Honorable Mayor and Members of the City Commission

FROM: 
Brent Godshalk, City Auditor

SUBJECT: Arthur J. Gallagher & Co. Insurance Broker Update

On August 8, 2005, the City Commission directed the City Auditor to review Arthur J. Gallagher's (Gallagher) records related to their return of approximately \$1.3 million to the City of Gainesville (the City). The City Commission also directed the City Auditor to report back to the City Commission regarding how much the City had been overcharged and what the appropriate level of interest due from Gallagher would be.

After receiving this referral, the City Auditor's Office worked with the City Attorney's Office to establish a legal agreement with Gallagher allowing the City to immediately deposit the \$1.3 million check received without hindering the City's ability to seek additional compensation, including interest, from Gallagher. This was accomplished and the check was deposited into the City's bank account on August 22, 2005.

At the same time, staff of the City Auditor's Office traveled to Gallagher's offices in Clearwater, Florida and reviewed documentation related to insurance products brokered by Gallagher for the City from 1991 through 2005. A key portion of our review was verifying the overcharges identified by Gallagher against 3rd party documentation Gallagher received from insurance providers. Based on our review, we identified adjustments to the approximate \$1.3 million previously received from Gallagher totaling approximately \$19,000 to the City's benefit. Gallagher was very cooperative in providing access to the records necessary for us to complete this phase of our review and has agreed with these adjustments.

We then prepared an interest calculation model identifying the City's lost opportunity costs associated with the excess commissions paid by the City during the 14 year period under review. The model mirrored the methodology utilized by the City of Lakeland Internal Audit Department previously agreed to by Gallagher. However, we used the City of Gainesville's annual operating yield on investments, averaging 5.4% from 1995 through 2005, for each fiscal year during the period and applied these rates to the excess commissions retained by Gallagher. Lakeland used the Florida State Board of Administration pooled interest rate for the respective fiscal years, averaging 4.2% from 1995 through 2005, since this is where Lakeland invests short-term cash balances. Our analysis identified a total interest amount due of approximately \$600,000.

After discussing this analysis with the City Manager and City Attorney, Gallagher was provided a detailed summary of our analysis identifying total additional monies due from Gallagher to the City as of September 30, 2005 in the amount of \$611,555. Gallagher responded to our analysis by submitting a proposal requesting the City utilize the Florida State Board of Administration pooled interest rate for the respective fiscal years. Gallagher's proposal identified total additional monies due from Gallagher to the City as of September 30, 2005 in the amount of \$411,299.

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Discussions have continued with Gallagher to try to reach final agreement on the total amount due the City. In the interest of reaching an amicable resolution on this issue, the City Auditor, City Manager and City Attorney presented a proposal to average the two sets of interest rates, resulting in an amount due from Gallagher of \$514,272, including accrued interest through December 2005. The City Manager and City Attorney will continue negotiations with Gallagher and present a recommended settlement to the City Commission for approval at a future meeting. The City Auditor's Office is turning our focus to completing the portion of the City Commission referral related to our review of the City's system of internal control surrounding the placement and monitoring of insurance coverage. We intend to issue our resulting final audit report to the City Commission's Audit and Finance Committee after providing the City Manager an opportunity to provide a written response to our recommendations for improvement.

Please feel free to contact me if you have any questions or comments regarding this update or any other issues.

CC: Charter Officers