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INTERGOVERNMENTAL COOPERATION AND THE MUNICIPAL INSURANCE CRISIS

TO ANDY LEAHY, ASSISTANT TO THE GOVERNOR OF THE
STATE OF ILLINOIS, 1972-1976, WHO TAUGHT
PEOPLE ABOUT GOVERNMENT AND GOVERNMENT ABOUT PEOPLE.

*Louis P. Vitullo**

*Scott J. Peters***

Under the Illinois Constitution of 1970, governmental units are authorized to enter into mutual agreements whereby their resources are pooled to provide services that might otherwise be prohibitively expensive for a single unit. Messrs. Vitullo and Peters suggest that intergovernmental cooperation can provide an effective solution for municipalities faced with the dual problems of expanding potential liability for damages and the corresponding difficulty in obtaining insurance. By uniting with other local governments, a municipality can obtain adequate insurance coverage while avoiding the large expense of a private insurance carrier.

Intergovernmental cooperation is based on the concept that the cost of public services can be reduced by achieving economies of scale so that there is maximum utilization of resources, facilities, and personnel.¹ Similar services provided by two or more governmental units are consolidated into one coordinated activity which transcends the boundaries of each individual unit. Some examples of intergovernmental cooperation are joint agreements in which one governmental unit provides services or facilities to another,² mutual assistance agreements,³ and organizations to combat particular problems within the delegating entities.⁴

This Article considers the use of intergovernmental cooperation as a solution to the current insurance crisis facing municipal governments. After

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1. ILLINOIS DEP'T OF LOCAL GOVERNMENTAL AFFAIRS & NORTHEASTERN ILLINOIS PLANNING COMMISSION, INTERGOVERNMENTAL COOPERATION IN ILLINOIS 10 (1976) [hereinafter cited as INTERGOVERNMENTAL COOPERATION].

2. The municipality of Pittsfield, Illinois agreed to provide 24-hour ambulance service to the majority of townships within Pike County. The Pittsfield police department administers the program. Pittsfield bills and collects all user fees. Each township pays a yearly fee for the service but all policy decisions are made by the mayor and city council of Pittsfield. *Id.* at 183-84. Another example is the agreement between the city and township of Robinson, Illinois, whereby the city provides personnel to equip the township's fire protection equipment. *Id.* at 192-93.

3. The agreement of the Battalion Seven Mutual Aid Association, consisting of the communities of Berkeley, Bellwood, Broadview, Hillside, Maywood, Melrose Park, and Westchester, provides that participating members shall share fire protection, rescue, and ambulance service during an emergency. Each member contributes equipment, a minimum of four firemen, and \$200 in annual dues for joint purchasing of necessary equipment. *Id.* at 189-90.

4. The city, park district, and school district of Naperville organized a defense fund to a suit by the Homebuilders Association of Greater Chicago that challenged a Naperville ordinance. The fund is used to finance a system of defense, including expert testimony and documentation. An advisory committee administers the funds and staffing needs are provided by the City of Naperville. *Id.* at 40-41.

briefly analyzing the historical bases of intergovernmental cooperation in Illinois, the cause of the municipal insurance crisis is then examined, with particular emphasis upon expanding municipal liability for tort, civil rights, and workers' compensation claims. As shown by two existing examples, self-insurance and risk pooling, intergovernmental cooperation can provide a workable remedy to the growing insurance problem.

BACKGROUND

The emergence of intergovernmental cooperation in Illinois reflects the changing forms and needs of local governments. In 1870, the framers of the Illinois Constitution maintained county and township governments based on geographical boundaries⁵ and revenues derived from an *ad valorem* property tax.⁶ Under this system, however, local governments were hindered in the performance of long-range projects because of the limited amount of debt that could be incurred.⁷

In addition, Dillon's Rule⁸ was a formidable obstacle to the solution of local government problems. Under the rule, municipal corporations could exercise only those powers which were: 1) expressly granted by the state legislature; 2) necessarily implied by, or incidental to, the express powers; or 3) indispensable to the attainment of the declared purpose of the corporation.⁹ Local governments were forced to seek legislative authority for every act that was desirable but not indispensable to the municipality. A further problem arose, however, in that a constitutional ban on special legislation

5. ILL. CONST. of 1870, art. X, §§ 1-13. For an excellent discussion of the history of townships and counties as the basic forms of local government, see Anderson & Lousin, *From Bone Gap to Chicago: A History of the Local Government Article of the 1970 Illinois Constitution*, 9 J. MAR. J. PRAC. & PROC. 697, 699-700 (1976) [hereinafter cited as Anderson & Lousin].

6. ILL. CONST. of 1870, art. IX, § 1. "[E]very person and corporation shall pay a tax in proportion to the value of his, her, or its property. . . ." *Id.* A sales tax was not levied in Illinois until 1933. Retailers' Occupation Tax Act, 1933 Ill. Laws 924 (current version at ILL. REV. STAT. ch. 120, §§ 440-453 (1979)), and an income tax was first imposed in 1969. Illinois Income Tax Act, P.A. 76-261, 1969 Ill. Laws 409 (current version at ILL. REV. STAT. ch. 120, §§ 1-101 to 17-1701 (1979)). Previously, governmental officials assumed that taxation of realty would best ensure that wealthier citizens assumed a greater tax burden. G. FISHER, *TAXES AND POLITICS: A STUDY OF ILLINOIS PUBLIC FINANCE* 127-29 (1969).

7. The amount of debt a local government could incur was limited to five percent of its assessed property value. ILL. CONST. of 1870, art. IX, § 12. See Anderson & Lousin, *supra* note 5, at 700.

8. As enunciated by Justice Dillon of the Iowa Supreme Court in *City of Clinton v. Cedar Rapids & Mo. R.R.*, 24 Iowa 455 (1868), "[t]he true view is this: Municipal corporations owe their origin to, and derive their powers and rights wholly from, the legislature." *Id.* at 475. *Accord*, *Barnes v. District of Columbia*, 91 U.S. 540 (1875). See Anderson & Lousin, *supra* note 5, at 703.

9. J. DILLON, *LAW OF MUNICIPAL CORPORATIONS* § 132, at 237 (5th ed. 1911). See *Ives v. City of Chicago*, 30 Ill. 2d 582, 584, 198 N.E.2d 518, 519 (1964) (expressly recognizing the validity of Dillon's Rule under the 1870 constitution); *County of Richland v. County of Lawrence*, 12 Ill. 1, 7 (1850) (legislature found to control fund belonging to public municipal corporation).

required the legislature to uniformly grant the same powers to all municipalities.¹⁰ Thus, while it might have been desirable to grant a certain power to Chicago, it might also have been equally undesirable to grant the same power to a smaller town. Further, the methods of avoiding the ban on special legislation were either cumbersome or ineffective.¹¹

The shift in the national economy toward industrialization created additional problems for Illinois' fragmented local governments.¹² The increasing demand for public services often exceeded the capacity of a single governmental unit. This led to the duplication and overlapping of functions by municipalities concerned with the same problem.¹³ To correct this inefficiency, the state legislature enacted several laws permitting intergovernmental cooperation,¹⁴ but Dillon's Rule and the ban on special legislation prevented any controlling law. Rather, the law in this area was scattered throughout the statutes. The effect was that local officials were unsure of the extent of their powers in light of the restrictive judicial approval of municipal powers. Thus, intergovernmental cooperation occurred only where there was clear statutory authority.¹⁵

By the time of the Sixth Illinois Constitutional Convention in 1970, it was clear that special authority was needed to solve modern problems facing local governments. Thus, the delegates to the Sixth Convention dramatically altered the powers of local governmental units. Dillon's Rule and legislative supremacy gave way to a system of home rule units¹⁶ and relative autonomy

10. "The General Assembly shall not pass local or special laws in any of the following enumerated cases . . . : for . . . regulating county and township affairs; . . . incorporating cities, towns or villages, or changing or amending the charter of any town, city or village. . . ." ILL. CONST. of 1870, art. IV, § 22.

11. As noted in Anderson & Lousin, *supra* note 5, at 703, one method of avoiding the constitutional ban in order to grant a power exclusively to Chicago was a constitutional amendment. The legislature could grant powers to Chicago alone, subject to referendum approval of a majority of the legal voters of the city. ILL. CONST. of 1870, art. IV, § 34. Due to several difficulties, this approach was eventually dropped from use. Anderson & Lousin, *supra* note 5, at 703.

The second method was by classifying areas of population. For example, a statute that began with "any municipality having a population of more than 500,000" would only cover Chicago. See, e.g., ILL. REV. STAT. ch. 24, § 1-4-5 (1979) (police officer of municipality with population greater than 500,000 can be indemnified for injuries caused in performance of duties). However, this method was flawed when the legislature desired that certain powers be granted to Chicago and smaller towns, but not medium-sized towns. Anderson & Lousin, *supra* note 5, at 703.

12. The fragmentation of Illinois' local governments system resulted in over 6,000 units of local government. INTERGOVERNMENTAL COOPERATION, *supra* note 1, at 2. See also Yackley, *Amid a Thicket of Governments*, 58 ILL. B.J. 348 (1970).

13. INTERGOVERNMENTAL COOPERATION, *supra* note 1, at 2-3.

14. Anderson & Lousin, *supra* note 5, at 792-93.

15. *Id.*

16. Home rule unit status was automatically conferred upon all municipalities having a population greater than 25,000 and upon any county having "a chief executive officer elected by the electors of the county . . ." ILL. CONST. art. VII, § 6(a). Further, any municipality with a population of less than or equal to 25,000 may elect by referendum to become a home rule unit. *Id.* Likewise, any home rule unit may elect "not to be a home rule unit." *Id.* § 6(b). See STATE OF ILL. COMM'N TO STUDY COUNTY PROBLEMS, 81st Gen. Assembly 10-13 (1978).

for localities regarding matters "pertaining to . . . [their] . . . government and affairs."¹⁷

Accordingly, to afford the broadest range of choice to local governments in solving common problems, a provision was included in the new constitution dealing exclusively with intergovernmental cooperation.¹⁸ Article VII, section 10 of the constitution provides a basic grant of power to a home rule unit or school district to cooperate with other governmental units and to transfer powers among themselves. It permits participating units to pool their efforts and encourages intergovernmental cooperation as a means of ensuring efficient and economical local government.¹⁹

The Intergovernmental Cooperation Clause of the new charter was specifically addressed by an Illinois court for the first time in *Connelly v. Clark County*,²⁰ where a county was operating a gravel pit for its own use in rebuilding roads and highways. While the appellate court held there was statutory authority for the county to operate the pit,²¹ it also found that the practice of selling gravel to other units of government without an ongoing agreement was prohibited by the new constitution.²² The court read the new constitution as permitting intergovernmental cooperation only when localities *jointly* perform a function or operate a facility. Isolated purchases, without a contractual obligation, were not within the scope of the Intergovernmental Cooperation Clause.²³ This holding demonstrated the need for clarification of the broad language of section 10.

17. ILL. CONST. art. VII, § 6(a).

18. The provision states in full:

INTERGOVERNMENTAL COOPERATION

(a) Units of local government and school districts may contract or otherwise associate among themselves, with the State, with other states and their units of local government and school districts, and with the United States to obtain or share services and to exercise, combine, or transfer any power or function, in any manner not prohibited by law or by ordinance. Units of local government and school districts may contract and otherwise associate with individuals, associations, and corporations in any manner not prohibited by law or by ordinance. Participating units of government may use their credit, revenues, and other resources to pay costs and to service debt related to intergovernmental activities.

(b) Officers and employees of units of local government and school districts may participate in intergovernmental activities authorized by their units of government without relinquishing their offices or positions.

(c) The State shall encourage intergovernmental cooperation and use its technical and financial resources to assist intergovernmental activities.

Id. § 10.

19. *Id.* See Anderson & Lousin, *supra* note 5, at 791-92. See generally Comment, *Intergovernmental Cooperation: Does the 1970 Illinois Constitution Give Units of Local Government the Green Light?*, 8 J. MAR. J. PRAC. & PROC. 295 (1975).

20. 16 Ill. App. 3d 947, 307 N.E.2d 128 (4th Dist. 1973).

21. *Id.* at 948-49, 307 N.E.2d at 129-30. See ILL. REV. STAT. ch. 121, § 5-601 (1979).

22. 16 Ill App. 3d at 951, 307 N.E.2d at 131.

23. *Id.*

As a result, the state legislature enacted the Intergovernmental Cooperation Act,²⁴ which clarified the policy favoring cooperation among units of local government. The Act explains the constitutional provision in two significant ways. First, a distinction is drawn between intergovernmental agreements and intergovernmental contracts. Pursuant to an intergovernmental agreement, the Act allows any power which may be exercised by a unit of local government to be exercised jointly with any other unit within or without the state.²⁵ In contrast, under an intergovernmental contract, municipalities may enter into contracts to provide a service that any party is authorized to perform.²⁶ One unit performs and pays for all administrative functions while the other unit merely purchases the services it uses. As an example, the *Connelly* court found that the county could not sell gravel to other units absent a partnership or joint venture agreement.²⁷ Under the Act, however, this arrangement used by the county would be considered a series of service contracts.

The second important clarification offered by the Act concerns insurance of the joint effort. Intergovernmental contracts may authorize the parties thereto to jointly self-insure and to use their funds to protect any other party to the contract against liability or loss in insurable areas.²⁸ For example, one municipality may contract with another to provide police service, partly in exchange for a reimbursement of retirement and disability pension liabilities resulting from the additional police protection. Yet, recent developments in municipal liability have elicited the need for intergovernmental cooperation agreements where insurance is the sole purpose.

THE MUNICIPAL INSURANCE CRISIS

Intergovernmental cooperation has a particularly useful and important application in the municipal insurance context. In the past it was generally recognized that municipal liability was highly restricted.²⁹ The need for insurance was much less critical and insurance underwriters could easily meet this need. The past two decades, however, have witnessed an explosive increase in municipal liability for tort, civil rights, and workers' compensation claims. As the limits of liability in these areas have become shifting and uncertain, municipal insurers have become reluctant or unwilling to underwrite many municipal activities. Without insurance, of course, most municipi-

24. P.A. 78-785, 1973 Ill. Laws 2382 (current version at ILL. REV. STAT. ch. 127, §§ 741-749 (1979)). See generally Note, *The Illinois Intergovernmental Cooperation Act*, 1974 U. ILL. L.F. 498.

25. ILL. REV. STAT. ch. 127, § 743 (1979).

26. *Id.* § 745.

27. 16 Ill. App. 3d at 949-51, 307 N.E.2d at 130-31.

28. ILL. REV. STAT. ch. 127, § 746 (1979).

29. See W. PROSSER, *HANDBOOK OF THE LAW OF TORTS* §§ 131-133, at 970-96 (4th ed. 1971); Comment, *Illinois Tort Claims Act: A New Approach to Municipal Tort Immunity in Illinois*, 61 Nw. U.L. Rev. 265 (1966); Comment, *Tort Claims Against the State of Illinois and Its Subdivisions*, 47 Nw. U.L. Rev. 914 (1953).

pal projects become too risky and must be abandoned, regardless of the government program's merit.

Expanding Local Governmental Liability and Its Impact

The increasing liability exposure of Illinois municipalities has its genesis, in part, in the 1959 Illinois Supreme Court decision, *Molitor v. Kaneland Community Unit District No. 302*.³⁰ *Molitor* and its progeny³¹ rendered local government units liable for the torts of their agents and employees, a clear break from common law principles that recognized complete sovereign immunity in such cases.³² In the wake of *Molitor* and the expansive municipal liability it sanctioned, the Illinois General Assembly in 1965 reinstated many of the pre-*Molitor* common law governmental immunities through the Local Governmental and Governmental Employees Tort Immunity Act.³³ Although designed to shield municipalities from liability in certain instances, the Act generally permits injured persons to recover damages from local governmental units when a unit or its agents caused the injury.³⁴

Even in those situations where a municipality or other local entity enjoys defenses or immunities under the Act, the protection provided by such defenses or immunities is often quite narrow. The most obvious limitation applies to local governmental employees' actions that exceed the Act's scope. In such cases, the statute provides no defense or immunity, leaving the local government liable for its employee's conduct. Examples of unprotected areas are willful misconduct³⁵ or nontort actions, such as breach of contract, workers' compensation, and occupational diseases.³⁶

30. 18 Ill. 2d 11, 163 N.E.2d 89 (1959), *cert. denied*, 362 U.S. 968 (1960), *modified on other grounds*, 24 Ill. 2d 467, 182 N.E.2d 145 (1962).

31. *See, e.g.*, *Kobylanski v. Chicago Bd. of Educ.*, 63 Ill. 2d 165, 347 N.E.2d 705 (1976); *Sullivan v. Midlothian Park Dist.*, 51 Ill. 2d 274, 281 N.E.2d 659 (1972); *Housewright v. City of LaHarpe*, 51 Ill. 2d 357, 282 N.E.2d 437 (1972); *Fanio v. John W. Breslin Co.*, 51 Ill. 2d 366, 282 N.E.2d 443 (1972).

32. *See, e.g.*, *Kinnare v. City of Chicago*, 171 Ill. 332, 49 N.E. 536 (1898) (immunity extended to school districts); *Town of Waltham v. Kemper*, 55 Ill. 346 (1870) (county and town immunity adopted). *See generally* Huff, *Tom Molitor and the Divine Right of Kings*, 37 CHI.-KENT L. REV. 44 (1960) (denouncing *Molitor* as judicial legislation); Comment, *Governmental Immunity in Illinois: The Molitor Decision and the Legislative Reaction*, 54 NW. U.L. REV. 588 (1959) (praising *Molitor* decision).

33. 1965 Ill. Laws 2983 (current version at ILL. REV. STAT. ch. 85, §§ 1-201 to 10-101 (1979)).

34. *See* *City of Chicago v. Vickers*, 8 Ill. App. 3d 902, 291 N.E.2d 315 (1st Dist. 1972) (sovereign immunity with respect to local municipalities replaced by Local Governmental and Governmental Employees Tort Immunity Act); Wangerin, *Actions and Remedies Against Governmental Units and Public Officers for Nonfeasance*, 11 LOY. CHI. L.J. 101 (1979).

35. *See* *Melbourne Corp. v. City of Chicago*, 76 Ill. App. 3d 595, 604, 394 N.E.2d 1291, 1298 (1st Dist. 1979) (plaintiff must allege malice to circumvent defense of Tort Immunity Act); *King v. City of Chicago*, 66 Ill. App. 3d 356, 384 N.E.2d 22 (1st Dist. 1978) (battery committed by police officers); *Nelson v. Nuccio*, 131 Ill. App. 2d 261, 268 N.E.2d 543 (1st Dist. 1971) (tortious conduct of police officer). *But see* *Mills v. County of Winnebago*, 104 Ill. App. 2d 366, 244 N.E.2d 65 (2d Dist. 1969) (plaintiff who was wounded by county deputy has cause of action against deputy individually for willful and wanton conduct but not against county that employed deputy).

36. ILL. REV. STAT. ch. 85, § 2-101 (1979).

Where the Act's immunities or defenses do apply, a local public entity may still face tort liability if it has secured liability insurance policies with respect to all defenses and immunities contained in the Act. In *Kobylanski v. Chicago Board of Education*,³⁷ the Illinois Supreme Court construed section 9-103(b) of the Act and held that purchasing insurance waived all tort immunity up to the amount of insurance coverage.³⁸ The *Kobylanski* case is significant because earlier decisions appeared to view such waivers more restrictively. For instance, in *Sullivan v. Midlothian Park District*,³⁹ the court held that purchasing public liability insurance waived tort immunity only for failure to maintain recreational areas.⁴⁰ Similarly, in *Housewright v. City of LaHarpe*⁴¹ and *Fanio v. John W. Breslin Co.*,⁴² the court held that acquiring insurance waived certain notice and timely filing requirements under the Act.⁴³ In view of *Kobylanski* and these other cases it appears that obtaining liability insurance from a private carrier waives all tort immunity to the extent of the insurance policy's coverage.⁴⁴

In addition, a recent Illinois Appellate Court decision has extended the waiver concept to include waiver of immunity from punitive damages. In *Holda v. County of Kane*,⁴⁵ the plaintiff claimed that Kane County officials' negligent operation of Kane County Jail resulted in his severe beating at the hands of other inmates. The Second District Appellate Court concluded that the county's procurement of liability insurance constituted a waiver of the

37. 63 Ill. 2d 165, 347 N.E.2d 705 (1976).

38. *Id.* at 173-74, 347 N.E.2d at 709.

39. 51 Ill. 2d 274, 281 N.E.2d 659 (1972).

40. *Id.* at 281-82, 281 N.E.2d at 663.

41. 51 Ill. 2d 357, 282 N.E.2d 437 (1972).

42. 51 Ill. 2d 366, 282 N.E.2d 443 (1972).

43. In *Housewright*, the Illinois Supreme Court held that under section 9-103(b) of the Local Governmental and Governmental Employees Tort Immunity Act, ILL. REV. STAT. ch. 85, §§ 1-101 to 10-101 (1979), public entities that purchase insurance waive the statutory right to written notice of an injury as a prerequisite to a suit. 51 Ill. 2d at 366, 282 N.E.2d at 442. On the same day, the court held in *Fanio* that the six-month notice and one-year limitation for suits against a local public entity were waived by the entity's purchase of insurance to cover liability. 51 Ill. 2d at 370, 282 N.E.2d at 445.

44. One commentator has argued that the acquisition of liability insurance should result in the waiver of only certain provisions of the Tort Immunity Act. He reasons that there are three policy considerations underlying the establishment of the Act: (1) protection of public funds; (2) protection of public employees in the exercise of their discretion; and (3) the separation of powers doctrine. Because the acquisition of insurance relates only to the protection of public funds, only statutory immunities based on the protection of those funds should be waived. Judge, *Tort Immunity Act: Only Certain Immunities are Waived by Public Entity's Purchase of Insurance*, 63 ILL. B.J. 386 (1975). The Illinois Supreme Court, however, has not accepted this analysis. See *Lansing v. County of McLean*, 69 Ill. 2d 562, 372 N.E.2d 822 (1978) (county waiver immunity up to limits of public liability policy); *Kobylanski v. Chicago Bd. of Educ.*, 63 Ill. 2d 165, 347 N.E.2d 705 (1976) (school board waiver immunity up to limits of liability insurance policy).

45. 88 Ill. App. 3d 522, 410 N.E.2d 552 (2d Dist. 1980).

Act's immunity from punitive damages under section 2-102.⁴⁶ The *Holda* decision represents potentially vast liability because punitive damages often greatly exceed compensatory damages.

Compounding local governmental units' liability problems are recent developments in the civil rights field. According to the United States Supreme Court decision in *Monroe v. Pape*,⁴⁷ municipal corporations were considered beyond the scope of the Civil Rights Act of 1871 because they were not "persons."⁴⁸ Later federal cases extended this civil rights immunity to local public entities other than municipal corporations, such as states,⁴⁹ state agencies,⁵⁰ municipal agencies⁵¹ and townships.⁵²

In 1978, however, the Supreme Court abrogated the municipal immunity doctrine in *Monell v. New York City Department of Social Services*.⁵³ The *Monell* Court concluded that the *Monroe* decision erroneously viewed section 1983 as applying only to natural persons when the statute was meant to include both legal and natural persons.⁵⁴ By holding that municipalities and other local governmental entities are persons under section 1983, the *Monell* decision effectively eliminated a municipality's insulation from monetary, declaratory, or injunctive relief when the basis of the claim is conduct that "implements or executes" a policy or regulation adopted by the governmental entity.⁵⁵ This conduct includes actions that constitute "governmen-

46. *Id.* at 530, 410 N.E.2d at 558.

47. 365 U.S. 167 (1961). The plaintiffs alleged that the invasion and subsequent search of their home by Chicago police officers without a warrant and the detention of Monroe at a police station without a warrant or arraignment was a violation of their civil rights under 42 U.S.C. § 1983. 365 U.S. at 169.

48. *Id.* at 191. Section 1983 provides:

Every person who, under color of any statute, ordinance, regulation, custom, or usage, of any state or Territory, subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be held liable to the party injured in an action at law or suit in equity or other proper proceeding for redress.

42 U.S.C. § 1983 (1976) (emphasis added).

49. *See, e.g.*, *Cherame v. Tucker*, 493 F.2d 586 (5th Cir.) (states not "persons" for § 1983 purposes), *cert. denied*, 419 U.S. 868 (1974).

50. *See, e.g.*, *Sykes v. California*, 497 F.2d 197 (9th Cir. 1974) (department of motor vehicles).

51. *See, e.g.*, *Garrett v. City of Hamtramch*, 503 F.2d 1236 (6th Cir. 1974) (city planning commission); *United Farmworkers of Fla. Hous. Project, Inc. v. City of Delray Beach*, 493 F.2d 799 (5th Cir. 1974) (county planning board).

52. *See, e.g.*, *Pressman v. Chester Township*, 307 F. Supp. 1084 (E.D. Pa. 1969).

53. 436 U.S. 658 (1978). The plaintiffs were pregnant employees who claimed that officials from the Department of Social Service and the Board of Education had forced them to take unpaid leaves of absence before they were medically advised to do so. *Id.* at 660-62.

54. The Supreme Court re-examined the legislative history of the Civil Rights Act of 1871 and the legislative intent to hold governmental units liable for damages for constitutional violations resulting from governmental policy or custom. *Id.* at 664-89.

55. *Id.* at 690.

tal custom,"⁵⁶ even if such customs are not approved officially. But the status of good faith conduct⁵⁷ was left open by *Monell*, leaving municipalities free to assert a qualified immunity defense.

The good faith question, however, was recently resolved in *Owen v. City of Independence*.⁵⁸ In *Owen*, the Supreme Court considered the plaintiff's claim for damages based upon the release of investigative reports to the news media and plaintiff's discharge from his position as Chief of the Independence, Missouri Police Department.⁵⁹ The city argued that because the City Council members acted in good faith in releasing information concerning Owen, the city and its council members were entitled to immunity from civil rights claims. The *Owen* Court rejected this argument, concluding that a municipality may not assert good faith as a defense in section 1983 actions.⁶⁰ In a related decision, *Gomez v. Toledo*,⁶¹ the Supreme Court pronounced that the burden of pleading good faith rests upon the defendant and that this defense is available to a public official only if the official "has an objectively reasonable basis for [his] belief [and] . . . the official himself is acting sincerely and with a belief that he is doing right."⁶² The effect of *Monell*, *Owen* and *Gomez*, of course, is that the liability of local governmental units for the conduct of their officials, employees, and agents has greatly increased.

It should be noted, however, that the Supreme Court recently determined that Congress did not intend that punitive damages be awarded against a municipality in an action brought under section 1983. In *City of Newport v. Fact Concerts, Inc.*,⁶³ the plaintiffs sought compensatory and punitive damages against the mayor and city council of Newport, Rhode Island, for attempting to prevent a jazz-rock group from performing at a local state park. The Court reversed the district court's award of punitive damages, concluding that legislative history showed that municipalities were immune

56. In *Adickes v. S.H. Kress & Co.*, 398 U.S. 144 (1970), Justice Harlan described the term "governmental custom" as a practice "not authorized by written law . . . [but] . . . so permanent and well settled as to constitute a 'custom or usage' with the force of law." *Id.* at 167-68.

57. Often, public officials have been protected from personal liability when good faith actions taken pursuant to official duties resulted in constitutional violations. *See, e.g.*, *Sala v. County of Suffolk*, 604 F.2d 207 (2d Cir. 1979) (county strip search policy enacted in good faith); *Ohland v. City of Montpelier*, 467 F. Supp. 324 (D. Vt. 1979) (good faith discharge of public employee).

58. 455 U.S. 622 (1980).

59. The statement alleged that Owen had misappropriated police department property, that narcotics had "mysteriously" disappeared from his office, that traffic tickets had been manipulated, and that suspects had been released under unusual circumstances. Brief for Petitioner at 3, *Owen v. City of Independence*, 445 U.S. 622 (1980).

60. The Court felt that Congress intended to incorporate into the statute only those common law immunities existing at the time when the statute was enacted; thus, the Court refused to acknowledge the good faith defense when interpreting the statute. 455 U.S. at 644.

61. 446 U.S. 635 (1980).

62. *Id.* at 641 (quoting *Wood v. Strickland*, 420 U.S. 308, 321 (1975)).

63. 101 S. Ct. 2748 (1981).

from such damages in section 1983 actions.⁶⁴ This decision represents a significant limitation on the expanding liability of municipal officials.

While tort and civil rights immunities and defenses available to local public entities and their officials are diminishing, yet another key source of liability appears to be increasing—workers' compensation.⁶⁵ As a result of expanded coverage, the cost to municipalities of workers' compensation has increased dramatically,⁶⁶ just as it has in the private sector. For example, a survey of Illinois municipalities shows that workers' compensation insurance premiums rose 90.5% between July 1, 1975 and July 1, 1979.⁶⁷ Moreover, in light of recent changes in the Workers' Compensation Act that hold municipalities liable to injured volunteer firemen, police, and civil defense members or trainees based upon the average weekly wages earned by such employees in their regular employment,⁶⁸ it is likely that insurance premiums will continue to rise.

Diminishing defenses and immunities, together with expanding liability bases, necessarily spell greater insurance costs because municipalities and other local public entities must maintain adequate insurance coverage. When one considers the devastating impact of a substantial civil rights judgment, or a multitude of workers' compensation claims upon a small unit of local government, the need for adequate insurance coverage becomes apparent.

The funds available to pay a judgment are a function of the tax base of the unit.⁶⁹ The larger the tax base, the easier it is for the governing body to meet the costs imposed by the judgment. Thus, a small municipality may not be able to pay a large judgment because it lacks a sufficiently broad tax base. Unlike private defendants, however, judgments against a local government may not be executed through attachment or sale of a local governmental unit's assets,⁷⁰ an obvious result in light of the practical difficulties inherent

64. *Id.* at 2750-52.

65. See Witt, *Risk Management: Claims By and Against City Employees*, 42B NIMLO MUN. L. REV. 280, 289 (1979).

66. See Parrish, *Workmen's Compensation Law in Illinois: Some Economic Consequences of Recent Changes*, 27 DEPAUL L. REV. 715, 723 (1978).

67. Interview with James Mochal, Gallagher & Basset Insurance Agency, in Chicago, Ill. (Aug. 28, 1981).

68. Act of September 15, 1980, P.A. 81-1482, § 10, 1980 Ill. Laws 1723 (amending ILL. REV. STAT. ch. 48, § 138.10 (1979)).

69. See ILL. REV. STAT. ch. 85, § 9-107 (1979), which provides:

A local public entity may levy or have levied on its behalf taxes annually upon all taxable property within its territory at a rate that will produce a sum which will be sufficient to pay the cost of settlements or judgments . . . to pay the costs of protecting itself or its employees against liability . . . , to pay the costs of and principal and interest on bonds issued under Section 9-105, to pay tort judgments or settlements . . . to the extent necessary to discharge such obligations.

Id.

70. See, e.g., ILL. REV. STAT. ch. 34, § 604 (1979), which provides: "Execution shall not, in any case, issue against the lands or other property of a county . . ." See also *Midland Elec. Coal Corp. v. County of Knox*, 1 Ill. 2d 200, 224, 115 N.E.2d 275, 287-88 (1953).

in attaching or selling a bridge or city street. Instead, a judgment may be enforced through a mandamus action requiring compliance with the provisions of section 9-104 of the Local Governmental and Governmental Employees Tort Immunity Act.⁷¹ Section 9-104 provides that a judgment may be paid in the year rendered, in the ensuing fiscal year, or in yearly installments up to a maximum of ten equal annual installments plus interest. The terms are determined by the hardship that payment of the judgment would cause the municipality.⁷² An additional tax may be levied,⁷³ and bonds may also be issued, in an amount in excess of the general statutory debt limit of the local governmental unit to satisfy the judgment.⁷⁴

A large judgment against, or settlement by, a local public entity requires the unit to expend its general revenue funds and reduces funds that would otherwise be available for governmental services. As previously discussed, local governments are already pressed by dwindling revenues and escalating costs; huge judgments only serve to create more costs and divert more revenues. Furthermore, bonds issued to pay a judgment are included in determining whether a municipality has authority to issue more bonds for other purposes.⁷⁵ Thus, once compelled to increase its indebtedness up to or in excess of the statutory limit by issuing bonds to pay a judgment, a municipality can no longer issue additional bonds or incur additional indebtedness for other services and projects.⁷⁶

Quite clearly, absent insurance, a substantial judgment or series of judgments could monetarily and functionally cripple a municipality by forcing it to forego or reduce services in vital areas. Yet insurance is unavailable to some municipalities⁷⁷ and for many others it has become prohibitively expensive. Due to the expanding liability of local governments and concomitant disappearing defenses,⁷⁸ insurers are facing greater underwriting costs and

71. ILL. REV. STAT. ch. 85, § 9-104 (1979).

72. *Id.*

73. *Id.* § 9-107.

74. *Id.* § 9-105.

75. Bonds necessary to discharge a tort settlement or judgment against a governmental unit may be issued for an amount, including existing indebtedness, in excess of any statutory debt limitations. *Id.*

76. See Act of August 11, 1979, P.A. 81-165, § 18, 1979 Ill. Laws 952 (amending ILL. REV. STAT. ch. 85, § 851 (1979)), which provides:

[N]o county having a population of less than 500,000 and no township, school district or other municipal corporation having a population of less than 300,000 shall become indebted in any manner or for any purpose, to an amount, including existing indebtedness, in the aggregate exceeding 2.875% on the value of the taxable property therein. . . .

However, this limitation does not apply to indebtedness incurred to pay firemen's and policemen's salaries and indebtedness of sanitary districts. ILL. REV. STAT. ch. 85, § 851.15 (1979).

77. See STATE OF ILL. COMM'N TO STUDY COUNTY PROBLEMS, 81st Gen. Assembly, at 18 (1978). See also Miles, *Report of the National Institute of Municipal Law Officers Committee on Inter-Municipal Cooperation*, 41 NIMLO MUN. L. REV. 192, 194, 197 (1978); INSTITUTE FOR LOCAL SELF GOVERNMENT, PUBLIC AGENCY LIABILITY 36-39 (1978) (California municipalities).

78. See note 29 and accompanying text *supra*.

will not significantly lower municipal premiums in the near future. Thus, local governments currently are facing an insurance crisis.

INTERGOVERNMENTAL COOPERATION AS A REMEDY

Solutions to the municipal insurance crisis can be achieved through several forms of aggressive risk management. The most basic risk management technique is to modify or abandon risk-prone activities. This is often accomplished by educating employees of dangerous work habits and improving the safety of the work environment. With increasing costs and shrinking revenues, many municipalities have made more affirmative efforts toward controlling the source of their risks.⁷⁹

Another risk management approach is self-insurance. Self-insurance involves maintenance of an adequate fund or reserve by the local government to meet claims as they arise as well as streamlined claims processing.⁸⁰ Cook County, for example, no longer carries private sector insurance and, therefore, has assumed the risk for any damages caused by its employees or officers. Thus, if a county official has an accident while negligently driving a county vehicle on official business, Cook County assumes the cost of liability and draws upon its reserve fund. To process such claims without the services provided by an insurance company, Cook County employs several persons for the sole purpose of reviewing claims against the county. In addition, several assistant state's attorneys devote the majority of their time to defending the County against tort claimants. Through its self-insurance plan Cook County now meets all its insurance-related obligations with its own resources, thereby saving the cost of high insurance premiums demanded by private carriers.

Self-insurance is not practical, however, for small municipalities that lack adequate funds and employees over which to spread large risks. Substantial or numerous judgments would rapidly exhaust the minimal insurance funds small local governmental units could afford to maintain and would consume far too much employee time that could be spent performing other governmental duties. Moreover, the relatively small number of employees in such units prevents specialized training in claims processing or defense. In short, self-insurance is a benefit derived from economies of scale that normally result only from large operations.

Nonetheless, small municipalities have realized substantial savings by entering into intergovernmental cooperation agreements through which governmental units aggregate and share workers' compensation, tort, or other

79. For a discussion of the favorable results obtained from a risk management program implemented in one city, see Wooderson & Hoffpauir, *Risk Management in a Southern City: The Growth of the Concept in the City of Lafayette, Louisiana*, 11 *URBAN LAW* 396, 401 (1979).

80. See Pfennigstorf, *Governmental Risk Management in Public Policy and Legislation: Problems and Options*, 1977 *AM. B. FOUNDATION RESEARCH J.* 255, 281-85.

liability exposures. Under such agreements⁸¹ a risk management agency is created to serve each participating local governmental unit, referred to as a member. As a precondition to membership, prospective members must make initial pool contributions that are analogous in some respects to capital contributions in partnerships. Initial contributions represent estimated loss experiences calculated by underwriters relying on the prospective members' past loss histories. When a member's loss experience exceeds its initial contribution, supplemental pool contributions are required. Once funded and organized, the risk management agency hires its own professional staff, including risk managers, claims adjusters, and counsel.

The agency is governed by a board of directors, with each agency member entitled to one vote and represented by one director on the board. The directors, in turn, adopt by-laws and select a chairman to head the agency. The number of members can vary during the agency's life, with new members added upon a two-thirds vote of approval by the board. Provision is usually made in the agency's by-laws for expulsion of members under certain circumstances, such as failing to make payments due the agency, refusing to undertake loss reduction programs, refusing to allow the agency reasonable access to relevant municipal records, or failing to cooperate fully and completely with claims adjusters. Members can, of course, withdraw from the agency, but they remain liable for their pro rata contributions to the agency's reserve pool for the year in which they withdraw.

The type of losses covered by the agency's reserve pool are determined by the board. Thus, an agency may offer protection and services for such areas as property, casualty, and civil rights, or limit its coverage to a single exposure such as workers' compensation. After an adjuster decides a claim is within the agency's coverage, he estimates the amount the agency is willing to pay. Members have the right to object and raise what is referred to as an optional defense if they consider the estimate excessive. However, if a member chooses to defend the claim and the resulting judgment exceeds the previously rejected estimate, the *member*—not the agency—pays the difference between the judgment and the estimate.

Unknown to many small municipalities, risk management agencies have served their cost-cutting purpose rather well. For example, one insurance cooperative, dubbed IRMA (Intergovernmental Risk Management Agency),⁸² provides coverage for property, workers' compensation, and gen-

81. Twenty-one Illinois municipalities entered into a cooperative insurance agreement in 1980. Relevant portions of the contract and by-laws of the South Towns Agency for Risk Management (STARM), a representative cooperative, are reproduced in the appendix to this article so that the reader may refer to an actual application of the general principles discussed in this section.

82. The twenty-two Illinois municipalities that comprise IRMA are mainly western and northwestern suburbs of Chicago. IRMA evolved from a 1976 seminar where 69 northern Illinois cities met to discuss municipal insurance problems. A committee's study of the matter led to the establishment of IRMA in January, 1979. See Aavang, *IRMA: The Nation's Largest Municipal Insurance Co-op*, ILLINOIS ISSUES, Aug. 1980, at 13-15.

eral liability exposures. Over its three and one-half year existence each IRMA member has enjoyed combined premium and loss savings of 38% to 40% compared to their previous payments and losses under private insurance plans.⁸³ Moreover, through IRMA, participating municipalities now have extensive loss prevention and risk management programs, uniform claims handling, and receive interest on invested pool contributions.⁸⁴ Another Illinois risk management agency, STARM (South Towns Agency for Risk Management),⁸⁵ provides coverage only for workers' compensation losses. Like IRMA participants, STARM members have also realized substantial reductions in combined premium and loss experience, averaging about 35% per member organization.⁸⁶

Although the effectiveness of these agencies is well established, their existence and operations have yet to be challenged in the Illinois court system. Some uncertainty remains as to whether they will be sanctioned. In the event such an operation is challenged, three important issues may arise. The first is whether these agreements, by requiring each agency member to aggregate and share its liability with other participating units, would be considered reciprocal pools and therefore subject to the rules and regulations of the Illinois Insurance Code⁸⁷ and the Illinois Department of Insurance. If so, an agency's cost would rise significantly and its activities would be curtailed greatly. If not, they would retain their current cost efficiency and management flexibility.⁸⁸

Though somewhat functionally similar to reciprocal pools, risk management agencies differ in one critical respect—their statutory authority. Reciprocal pools, which allow participants to combine reserves held to fund potential judgments,⁸⁹ are authorized by the Insurance Code itself and can

83. *Id.* at 13.

84. *Id.* at 14.

85. See note 81 *supra*.

86. Interview with James Mochal, Gallagher & Bassett Insurance Agency, in Chicago, Ill. (Aug. 28, 1981).

87. ILL. REV. STAT. ch. 73, §§ 613-1065.724. (1979 & Supp. 1981).

88. Legislation was recently introduced in the Illinois House of Representatives to specifically amend the Insurance Code so that intergovernmental risk management agencies would be regulated by the Department of Insurance. H.R. 553, 82d Ill. Gen. Assembly, 1st Sess. (1981). However, the bill died in the City and Villages Committee in the 1981 Spring Session.

89. One authority describes reciprocal pools as:

that system whereby individuals, partnerships, or corporations engaged in a similar line of business undertake to indemnify each other against a certain kind or kinds of losses by means of a mutual exchange of insurance contracts, usually through the medium of a common attorney in fact appointed for that purpose by each of the underwriters under agreements whereby each member separately becomes both an insured and an insurer with several liability only.

2 G. COUCH, INSURANCE § 18:11 (2d ed. 1959). See *W.R. & Co. v. Harding*, 348 Ill. 454, 181 N.E. 331 (1932) (analysis of reciprocal insurance pools in a tax context); *Mosteiko v. National Inter-Insurers Corp.*, 229 Ill. App. 153 (3d Dist. 1923) (analysis of reciprocal insurance pools in context of broker's liability).

only exist pursuant to that code.⁹⁰ Risk management agencies, on the other hand, find their authorization in the Illinois Constitution's strong endorsement of intergovernmental cooperation⁹¹ and the Intergovernmental Cooperation Act's express sanction of such insurance arrangements in particular.⁹² As discussed earlier, Illinois courts have followed these constitutional and statutory mandates by liberally interpreting their scope and purpose.⁹³ It seems logical that courts will follow the same pattern when reviewing the status of risk management agencies because of their express statutory approval and the important, if not critical, municipal insurance need they fill.

A second issue may arise with respect to implementing such intergovernmental insurance cooperatives. Municipalities must anticipate long term financial obligations to participate in shared risk agencies, but annual appropriations normally will not provide the necessary fiscal commitment. In addition, the Illinois Municipal Code expressly prohibits municipalities from obligating unappropriated funds.⁹⁴ Thus, municipalities appear unable to form risk management agencies because they cannot appropriate sufficient current funds and cannot obligate any future unappropriated funds.

This funding dilemma, however, was squarely addressed in a 1974 Illinois Attorney General opinion.⁹⁵ The question was whether a municipality that was contracting for additional police services could obligate itself on a long term basis to reimburse the municipality providing the services for possible future disability and retirement pension claims. The authority for the police contract was the Intergovernmental Cooperation Act and article VII, section 10, of the 1970 Illinois Constitution. The Attorney General concluded that the Act, in effect, repealed or amended the provision of the Municipal Code that prevented the obligation of unappropriated funds. Because the two statutes were in direct conflict, the later legislation was found to prevail.⁹⁶ Although no subsequent attorney general or court opinions have examined the unappropriated funds question, the 1974 attorney general opinion should be followed because of its persuasive emphasis upon Illinois' established public policy favoring intergovernmental cooperation.

Finally, there may be a question of whether the establishment of a risk pool by municipalities constitutes a waiver of immunity under the provisions of the Tort Immunity Act.⁹⁷ Although this issue was not squarely addressed, an Illinois appellate court has held that self-insurance does not constitute such a waiver. In *Beckus v. Chicago Board of Education*,⁹⁸ the plaintiff

90. ILL. REV. STAT. ch. 73, §§ 673-697 (1979).

91. See notes 16-19 and accompanying text *supra*.

92. See notes 24-28 and accompanying text *supra*.

93. See notes 38-46 and accompanying text *supra*.

94. ILL. REV. STAT. ch. 24, § 8-1-7 (1979). See *Chicago Patrolman's Ass'n v. City of Chicago*, 56 Ill. 2d 503, 309 N.E.2d 3, *cert. denied*, 419 U.S. 839 (1974).

95. 1974 OP. ATT'Y GEN. No. S-696.

96. *Id.*

97. See notes 37-44 and accompanying text *supra*.

98. 78 Ill. App. 3d 558, 397 N.E.2d 175 (1st Dist. 1979).

sought recovery for injuries sustained in a school playground accident.⁹⁹ The court held that the Board of Education's self-insurance program, which called for self-insurance up to one million dollars,¹⁰⁰ did not waive the Board's immunity up to that limit.¹⁰¹ By analogy, a risk pool is nothing more than a combination of self-insurers. Therefore, in light of *Beckus*, risk pooling should not constitute a waiver of immunity.

In sum, the growing liability of municipalities has caused an insurance crisis for small local public entities. Although insurance is often prohibitively expensive, frequently it is not available at any cost. Self-insurance fills the gap for those governmental entities large enough to undertake it, supplemented by risk reduction or control programs where possible. For small governments, risk management agencies provide the same services at inexpensive rates through intergovernmental cooperation. Indeed, such agencies have proved highly successful. If the legality of a risk management agency is challenged, the agency will probably prevail because of its strong constitutional and statutory foundation.

CONCLUSION

Declining revenues and spiraling costs compel more efficient management practices by local public entities. A key tool in the struggle with these twin problems is intergovernmental cooperation, which encourages greater utilization of existing resources by exploiting advantages created through economies of scale. Though still in its infancy, intergovernmental cooperation has been well received by the courts because of its useful public purpose and its strong constitutional and statutory underpinnings.

The expanding liability exposure of small local governments has brought forth a relatively new form of intergovernmental cooperation, the risk management agency. As with other intergovernmental cooperative activities, such agencies have promoted less expensive and more professional management practices, resulting in substantial savings and better insurance coverage for participating municipalities. Although some doubt exists as to the applicability of insurance regulations, and the agencies' power to use unappropriated funds, such questions should be resolved in favor of the risk management agencies. The insurance crisis alleviated by these agencies more than justifies the minimal legal risks that may attend them.

99. *Id.* at 559, 397 N.E.2d at 176.

100. The appellate court noted that the Board of Education invited bids for liability insurance coverage for a lesser amount but that it was unsuccessful in obtaining such coverage. *Id.* at 561, 397 N.E.2d at 178.

101. As the court noted:

The purpose of section 9-103(b) of the [Tort Immunity] Act is to require that when a local public entity is immune from suit, its insurance carrier cannot avoid liability by invoking the entity's immunity. . . . In this case, the insurance carrier's policy did not cover plaintiff's claim, and plaintiff's claim is also barred against defendant pursuant to the Tort Immunity Act.

Id. (citations omitted).

APPENDIX

**CONTRACT AND BY-LAWS
SOUTH TOWNS AGENCY FOR RISK MANAGEMENT***

ARTICLE I. Definitions and Purpose.**Purpose:**

The South Towns Agency For Risk Management (STARM) is a cooperative agency voluntarily established by contracting units of local government as defined in the Illinois Constitution of 1970 pursuant to Article VII, Section 10 of the 1970 Constitution of the State of Illinois and Chapter 127, Section 746 of the Illinois Revised Statutes for the purpose of seeking the prevention or lessening of casualty losses to municipal properties and injuries to persons or property which might result in claims being made against such units. Initially, the AGENCY will create a joint Risk Management Pool for workers' compensation claims.

It is the intent of the MEMBERS of this AGENCY to create an entity which will administer a Joint Risk Management Pool and utilize such funds contributed by the MEMBERS to defend and protect, in accordance with these By-Laws, any MEMBER of the AGENCY against stated liability or loss. Such By-Laws shall constitute the substance of a contract among the MEMBERS.

All funds contained within the Risk Management Pool are funds directly derived from its MEMBERS who are local governments within the State of Illinois. It is the intent of the parties in entering into this agreement that the creation of this AGENCY shall not waive, on behalf of any local public entity or public employees as defined in the Local Governmental and Governmental Employees Tort Immunity Act, any defenses or immunities therein provided. This intent shall be more fully implemented as the scope of risk management undertaken by them through a joint municipal self-insurance program using governmental funds shall increase beyond workers' compensation claims. Specifically, the MEMBERS of this AGENCY intend to effect no waiver of immunities through their contribution of public funds retained within the Risk Management Pool and not used to purchase excess or stop loss insurance policies. Such contributions being reserves to protect against uninsured risks in accordance with Chapter 127, Section 746, are not intended to constitute the issuance of a policy for insurance coverage, (by an insurance company authorized by the Department of Insurance to write such coverage in Illinois), as provided in Chapter 58, Section 9-103 of the Illinois Revised Statutes.

ARTICLE II. Powers and Duties.

The powers of the AGENCY to perform and accomplish the purposes set forth above shall, within the budgetary limits and procedures set forth in these By-Laws, be the following:

- (a) To employ agents, employees and independent contractors,
-
- (c) To carry out educational and other programs relating to risk reductions,
- (d) To cause the creation of, see to the collection of funds for, and administer a risk management pool,
-
- (g) To provide risk management services including the defense of and settlement of claims,
-

ARTICLE III. Participation.

.....

New MEMBERS shall be admitted only by a two-thirds (2/3) vote of the entire membership of the Board of Directors and subject to the payment of such sums and under such conditions as the Board shall in each case or from time-to-time establish.

*Prepared by: Stewart H. Diamond, Ancel, Glink, Diamond & Murphy, P.C., Chicago, Illinois.

ARTICLE IV. Commencement of Agency and Term.

Units of local government, . . . wanting to join the AGENCY, shall pass an ordinance authorizing unconditional membership in STARM in accordance with the terms of this agreement. Such municipalities shall forward to the South Suburban Mayors and Managers Association (SSMMA) the full amount of their first year's initial pool contribution. . . . That sum is .9023% of the manual rate which would apply for all officers and employees of the prospective MEMBERS entitled to workers' compensation coverage as last furnished to Arthur J. Gallagher & Company.

ARTICLE V. Board of Directors.

(a) There is hereby established a Board of Directors of the AGENCY. Each MEMBER unit of local government shall by majority vote of its corporate authorities elect one (1) person to represent that body on the Board of Directors for a term of one (1) year. The MEMBER may also select an alternative representative to serve when the initial representative is unable to carry out his duties. The person and alternate selected need not be an elected official of the MEMBER. At its first meeting of each fiscal year, the Board of Directors shall elect one (1) of its members to serve as Chairman of the Board until the conclusion of the fiscal year. . . .

(b) The Board of Directors shall determine the general policy of the AGENCY which policy shall be followed by all AGENCY officers, agents, employees and independent contractors employed by the AGENCY. It shall have the responsibility for (1) Hiring of AGENCY officers, agents, non-clerical employees and independent contractors, (2) Setting of compensation for all persons, firms and corporations employed by the AGENCY, (3) Setting of fidelity bonding requirements for employees or other persons, (4) Approval of amendments to the By-Laws, (5) Approval of the acceptance of new MEMBERS, (6) Approval of the annual budget of the AGENCY, (7) Approval of educational and other programs relating to risk reduction, (8) Approval of reasonable and necessary loss reduction and prevention procedures which shall be followed by all MEMBERS, (9) Approval of annual and supplementary payments to the Risk Management Pool for each MEMBER. The Board of Directors shall establish such rules and regulations regarding the payout of funds from the Risk Management Pool as shall from time-to-time seem appropriate.

(g) A greater vote than a majority of a quorum shall be required to approve the following matters:

(ii) The admission of a new MEMBER and the expulsion of a MEMBER shall require the affirmative two-thirds (2/3) vote of the entire membership of the Board of Directors,

(iv) The amendment of these By-Laws to cause the termination of this agreement sooner than five (5) years after its commencement, a reduction or elimination in the scope of loss protection set out in Article IX to be furnished by the self-insurance pool derived from payments from the MEMBERS, the amendment of these By-Laws to cause a modification of more or less than 25% as the high or low range of the pool contribution factor, as defined within Article VIII(d), and the expansion of the scope of coverage of the AGENCY beyond that from time-to-time contained within Article IX, shall require the recommendation of a majority vote of the Board of Directors plus the approval of such amendment by affirmative two-third (2/3) vote of the MEMBERS evidenced by resolutions of the respective corporate authorities.

In the case of the expansion of the scope of coverage of the AGENCY, in addition to the greater than majority vote set out above, it shall also be required that the new Joint Risk Management Pool to be created for the purpose of funding the expanded coverage shall be in at least an amount certain which amount shall be specified in the resolutions passed by the corporate authorities of the MEMBERS. Provided, however, that the corporate authorities of any MEMBER which votes against an expansion of the scope of coverage of the AGENCY beyond the area of Workers'

Compensation shall be given a single opportunity to entirely withdraw from the AGENCY before the effective date of the expansion. Such opportunity to withdraw may only be exercised if the expansion in the scope of the coverage of the AGENCY actually takes place. The corporate authorities of MEMBERS which vote against such an expansion shall be given a period of at least thirty (30) days following the date upon which all requisites for expansion had taken place in which to elect whether to remain in the group or withdraw. . . .

ARTICLE VIII. Finances and Risk Management Pool.

(c) Each MEMBER of the AGENCY shall make such annual payments to the Risk Management Pool as are approved by an affirmative two-thirds (2/3) vote of the entire membership of the Board of Directors. In determining such payments, the Board shall utilize at least the following factors: manual rates, the joint experience of the MEMBERS, audited employment records, the modification factor set forth in Article VIII(f), anticipated administrative costs and the cost of excess and aggregate insurance.

(e) Each MEMBER of the AGENCY shall make supplementary payments to the Risk Management Pool as are approved by the Board of Directors, providing, however, that such additional sums shall be assessed in the same proportion as annual payments for the year in question except as such proportions may be modified by the Board of Directors after an audit. The forwarding of such annual and supplementary payments within a time specified in notices to the MEMBERS giving them not less than forty-five (45) days to make such payments, shall be of the essence of this contract. Except as such payments may be required as a result of an audit, supplementary payment shall only be required by the Board of Directors in a situation in which there is a reasonable concern that the sum remaining from the annual payment will not be sufficient to meet the responsibilities of the AGENCY established in these By-Laws. MEMBERS shall be responsible for supplementary payments during the entire life of the AGENCY and any later period when claims or expenses need be paid which are attributable to the year of membership when the event out of which the expense or claim occurred.

(f) In subsequent years, the Board of Directors may require the annual or supplementary payments to be made on a monthly or quarterly basis. The Board of Directors may, beginning with the third fiscal year of the AGENCY, establish debits or credits in the pool contribution payment for those MEMBERS with above average or below average loss or claim records. Such increase or decrease above or below the payment which would otherwise be required without the experience modification shall not effect such unmodified amount by more than plus or minus 25%.

ARTICLE X. Excess Insurance.

The AGENCY will purchase excess insurance from a company approved by the Department of Insurance to write such coverage in Illinois. The amount of such excess insurance shall initially be a limit of \$5,000,000.00 in excess of the AGENCY's deductible of \$250,000.00 per occurrence.

In addition to the stated excess insurance coverage, the AGENCY will obtain aggregate stop loss insurance such that in the event that the AGENCY should in any single year expend a maximum aggregate sum set from time-to-time by the Board of Directors for the payment of claims, the stop loss protection would pay additional claims above that amount to certain maximum annual amount. The Board of Directors shall determine the commencement level of the aggregate stop loss protection and its limit based upon the current assets and risk history of the AGENCY.

For the first year of the AGENCY's existence, the sequence of the obligations of the MEMBER, the AGENCY and the excess insurer for a workers' compensation claim resulting in

liability within the scope of the self-insurance, catastrophe excess insurance and stop loss insurance to be provided is as follows:

The AGENCY shall pay any claim under the worker's compensation statute of the State in accordance with the scope of loss protection set forth in ARTICLE IX. The next level of responsibility shall be that assumed by the excess insurer. In the event that a series of losses should exceed the amount of coverage provided by the Risk Management Pool, the excess insurance and the stop loss coverage for any one year, then the payment of such uncovered valid loss shall be the obligation of the individual MEMBER or MEMBERS against whom the claim was made and perfected by judgment or settlement. In subsequent years, the Board of Directors in establishing the funding level of the AGENCY shall determine whether, as is the case in the first year, the Joint Risk Management Pool will be congruent with the level of the commencement of excess and aggregate insurance coverages.

ARTICLE XI. Obligations of Members.

The obligations of MEMBERS of the AGENCY shall be, as follows:

(a) To appropriate or budget for, where necessary to levy for and to promptly pay all initial, annual and supplementary or other payments to the Risk Management Pool at such times and in such amounts as shall be established by the Board of Directors within the scope of this agreement. Any delinquent payments shall be paid with a penalty which shall be equivalent to the prime rate of interest on the date of delinquency or the highest interest rate allowed by statute to be paid by an Illinois non-home rule municipality whichever is greater.

(b) To select a person to serve on the Board of Directors and to select an alternate representative.

(c) To allow the AGENCY reasonable access to all facilities of the MEMBER and all records including but not limited to employment and financial records which relate to the purpose or powers of the AGENCY.

(d) To allow attorneys employed by the AGENCY to represent the MEMBER in investigation, settlement discussions and all levels of litigation arising out of any claim made against the MEMBER within the scope of loss protection furnished by the AGENCY.

(e) To furnish full cooperation with the AGENCY's attorneys, claims adjusters, the Risk Manager and any agent, employee, officer or independent contractor of the AGENCY relating to the purpose and powers of the AGENCY.

(f) To follow in its operations all loss reduction and prevention procedures established by the AGENCY within its purpose and powers.

(g) To report to the AGENCY as promptly as possible all incidents which could result in the AGENCY being required to pay a claim.

....

ARTICLE XIV. Optional Defense by Municipality.

The Board of Directors will promulgate rules and procedures to allow MEMBERS the reasonable opportunity to prevent the AGENCY from settling cases or claims in a manner contrary to the wishes of the MEMBER. Such rules and procedures may, among other matters, include the following items:

- (1) An amount of the settlement at which the MEMBER may exercise this privilege,
- (2) The notice of settlement, if any, and the time and manner within which the decision of the MEMBER to object to the settlement shall be transmitted to the AGENCY,
- (3) Who shall bear costs of the defense of the claim or case which occur after the MEMBER has prevented the settlement from taking place.

The rules and procedures shall provide that where the MEMBER has exercised its privilege to prevent the settlement of the case or claim, it shall be responsible for any later judgment or settlement which disposes of the case above the amount of the settlement which had previously been reached between the claimant and the AGENCY.

....

ARTICLE XVI. Expulsion of Members.

By the affirmative vote of two-thirds (2/3) of the entire membership of the Board of Directors, any MEMBER may be expelled. Such expulsion, which shall take effect at the beginning of the next fiscal year, may be carried out for one or more of the following reasons:

- (a) Failure to make any payments due to the AGENCY,
- (b) Failure to undertake or continue loss reduction and prevention procedures adopted by the AGENCY,
- (c) Failure to allow the AGENCY reasonable access to all facilities of the MEMBER and all records which relate to the purpose or powers of the AGENCY,
- (d) Failure to furnish full cooperation with the AGENCY's attorneys, claims adjusters, the Risk Manager and any agent, employee, officer or independent contractor of the AGENCY relating to the purpose and powers of the AGENCY,
- (e) Failure to carry out any obligation of a MEMBER which impairs the ability of the AGENCY, to carry out its purpose or powers.

No MEMBER may be expelled except after notice from the AGENCY of the alleged failure along with a reasonable opportunity of not less than thirty (30) days to cure the alleged failure. . . .

ARTICLE XVII. Termination of the Agency.

If, at the conclusion of the fifth year, the AGENCY is not continued by the entry of some or all then current MEMBERS into a new Contract and By-Laws agreement, all withdrawing MEMBERS shall remain fully obligated for their portion of any claim against the assets of the Risk Management Pool which was created during the term of the membership of the withdrawing MEMBERS along with any other fulfilled obligation, including but not limited to calls for supplementary payments for years of their membership which may be called for in subsequent years. In the event that the AGENCY is not continued beyond its initial five-year term, the Board of Directors shall continue to meet on such a schedule as shall be necessary to carry out the winding up of the affairs of the AGENCY. If the AGENCY shall continue in operation, the withdrawing MEMBERS shall continue to hold membership on the Board of Directors but they shall only vote on matters affecting their limited continuing interest in the AGENCY. Those MEMBERS continuing to participate in the existence of the AGENCY at the end of the five-year term shall determine whether any funds of the AGENCY should be distributed to withdrawing MEMBERS.

DATED: _____, 19 ____.

ACCEPTED:

Mayor

Municipal Clerk

