

WORKERS COMP: Court ruling favors gig economy companies - **PAGE 10**

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Internet of things generates
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RISK MANAGEMENT

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VIEW FROM THE TOP

BILL SCALDAFERRI

Bill Scaldaferrri was appointed CEO for Allianz Global Corporate & Specialty in North America in July 2016 and is responsible for AGCS business in the U.S. and Canada. He previously ran AGCS's alternative risk transfer group and managed specialty lines on a global basis for AGCS, serving as chief underwriting officer for that business. In this issue, he discusses innovation, technology and other matters. **PAGE 16**



OFF BEAT

Grumpy Cat copyright win has this feline's owner feeling purr-fectly content. **PAGE 42**



Mitigation efforts speed storm recovery

BY GLORIA GONZALEZ

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The costliest year for natural disasters on record is placing new attention on the importance of mitigating future disaster risks, with compelling data highlighting how investments in predisaster mitigation can save money in the long term.

The insurance sector has a particularly critical role to play in disaster mitigation efforts, including by incentivizing the building of new infrastructure to more resilient standards or retrofitting existing infrastructure to withstand catastrophic perils, experts say.

The National Institute of Building Sciences found that the cost benefits of investing in disaster mitigation were even higher than previously estimated, with every dollar invested saving the United States \$6 in future costs compared with the \$4 return in avoided losses cited in a 2005 study. The report, released in January, examined 23 years of federally funded mitigation grants provided by the Federal Emergency Management Agency, the U.S. Economic Development Administration and the U.S. Department of Housing and Urban Development.

"I have to say bravo to NIBS for putting a punctuation point on the value of miti-

"It's going to take longer for businesses in those states (with weaker building codes) to open their doors and for homeowners to get back to normal just because there's going to be more damage without those mitigation measures."

Chris Hackett,
Property Casualty Insurers
Association of America in Chicago



gation," said Julie Rochman, president and CEO of the Insurance Institute for Business & Home Safety in Tampa, Florida. "I would still argue that there's probably more savings there but will accept 6-to-1."

However, President Donald Trump signed an executive order in August revoking the establishment of a federal flood risk management standard that would have prompted federal agencies to consider current and future risk when taxpayer dollars were used to build or rebuild near floodplains.

"It's kind of a shame for two reasons," Ms. Rochman said. "Number one, elevating in flood-prone areas is always good. It's not a political issue. It's just common sense and engineering. Two, it was the federal government trying to lead by example."

Even in the absence of a federal initiative, state and local governments can enhance their focus on disaster mitigation by implementing stronger building codes,

experts say.

Building codes in Florida, for example, have reduced the risk of damage caused by hurricanes and tropical storms, experts say. IBHS conducted a study following Hurricane Charley in 2004 that showed a 40% reduction in the frequency and a 60% reduction in the severity of hurricane-related damage to homes built to stronger building code standards. More recently, Hurricane Irma tested the stronger statewide building code, with most of its damage affecting older infrastructure that had not been retrofitted, according to experts.

Florida was the second-highest scoring state in an IBHS study that rated the effectiveness of states in adopting and enforcing building codes, following only Virginia. In contrast, Texas received one of the lowest scores in the 2015 study because it does not require mandatory adoption and enforcement of its residential building code throughout the state, although homeowners must meet wind-

storm building code standards to obtain windstorm and hail insurance from state insurer Texas Windstorm Insurance Association.

"It's those states that haven't adopted the most modern building codes that will take longer to recover," said Chris Hackett, senior director of policy at the Property Casualty Insurers Association of America in Chicago. "It's going to take longer for businesses in those states to open their doors and for homeowners to get back to normal just because there's going to be more property damage without those mitigation measures."

FM Global estimated its policyholders that implemented physical risk improvements to protect facilities from flood reduced their overall loss exposure by \$820 million during Hurricane Harvey, said Brion Callori, senior vice president and manager of engineering and research at the Johnston, Rhode Island-based insurer.

AFTER MARIA, ATTENTION TURNS TO FORTIFYING PUERTO RICO'S BUILDING CODES

As Puerto Rico continues to recover from Hurricane Maria, insurance experts are likely to turn their attention to the state of the U.S. territory's building codes.

Hurricane Maria, a Category 4 storm with 155-mph winds, struck Puerto Rico on Sept. 20, killing at least 64 people, destroying thousands of homes and leaving thousands of people without electricity or

water for months.

In 2011, Puerto Rico adopted a uniform building code that required structures to be built to withstand winds of up to 140 mph. Many buildings were built under a prior code requiring protection against 125-mph winds.

Duncan Ellis, U.S. property practice leader for Marsh L.L.C. in New York, said while Puerto Rico is still in a recovery

phrase, he expects there to be changes in the territory's building code.

"I would be surprised if the building codes were not changed in some way, shape or form," he said. "Where we probably saw the biggest change in building codes was in Florida post-Hurricane Andrew. There was a significant change in Florida's building codes, which I think has paid off in spades."

Mr. Ellis said that policies will typically have increased cost of construction coverage where a policy will cover the costs to rebuild property or real property pursuant to the new building codes.

"But if the building codes are changed, you're not allowed to do what you had before, then the policy will cover what one calls upgrades," he said.

Rob Lenihan

Insurers have a critical role to play in incentivizing mitigation, offering discounts for commercial property owners who take specific mitigation measures such as ensuring their properties are built to the most modern building code or using materials such as wind-resistant windows, Mr. Hackett said.

“Many companies will take that into account when developing a premium for a particular commercial risk,” he said.

“With disaster mitigation, I think insurers are taking a look at the risk and realizing they can afford to charge lower premiums,” said Peter Roldan, a San Francisco-based partner representing policyholders at law firm Emergent L.L.P.

Insurance companies are recommending the installation of floodgates in some flood-prone locations and are prepared to give premium credits that over five to 10 years can pay back the cost of that investment and prevent the recurrence of flood damage at the location, especially if these floodgates are built to their specifications, said Robert DeRosa, Houston-based senior managing director and head of Crystal & Company’s property practice.

“I really think that any activity from a mitigation perspective that’s explained directly to the carrier and explained the

right way is going to be incentivized,” he said. “When you have locations where you know you’re going to get hit by a hurricane or flood — it’s not a matter of if, it’s a matter of when, and what are you doing to prevent that instead of just relying on your insurance company to provide coverage in the event of a loss?”

Advocates of disaster mitigation hope the lessons taught by the 2017 disasters are not lost, with the billions in damage caused by Hurricane Harvey showing what can happen if development is allowed in vulnerable areas with little to no thought about mitigating these risks.

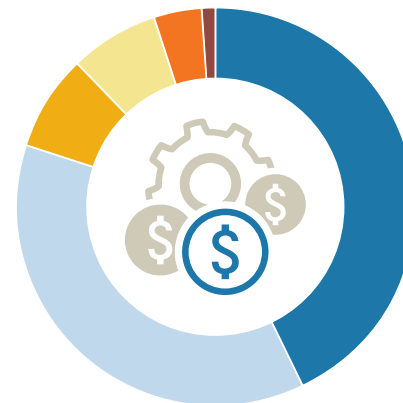
“It’s important to not become complacent because we had a long stretch in Florida where we did not have significant hurricane activity. But then the 2017 season happened, and the risks and dangers associated with hurricanes became a reality again,” Mr. Hackett said.

“I think we’ve proven that once people have a loss, the message gets out, at least in the commercial arena,” Mr. Callori said. “The bigger question is how do you extrapolate that to convince people who haven’t had the loss yet but are exposed to take action?”

But as climate change instigates more frequent and intense storms, the answer

BENEFITS OF MITIGATION

The National Oceanic and Atmospheric Administration declared 2017 the costliest year on record for weather and climate disasters, with total costs of about **\$306 billion**, eclipsing the record losses in 2005 by **\$100 billion**. But mitigation represents a sound financial investment that can reduce these costs, with benefits beyond the property lines of the mitigated buildings and the lives of occupants, including freeing up resources that would otherwise be spent on insurance claims and administrative fees, according to a new study.



The total cost of 23 years of federal mitigation grants was **\$27.4 billion**, while the benefits shown below added up to **\$157.9 billion**:

- **43%** Casualties and PTSD: **\$68.1 billion**
- **37%** Property: **\$58.1 billion**
- **8%** Additional living expenses and direct business interruption: **\$12.9 billion**
- **7%** Insurance: **\$10.5 billion**
- **4%** Indirect business interruption: **\$6.3 billion**
- **1%** Loss of service: **\$2.0 billion**

Source: Natural Hazard Mitigation Saves: 2017 Interim Report

in some areas will not be mitigation, but a prohibition on future development because of the difficulty in mitigating against an evolving danger, some experts say.

For example, a property could be built or retrofitted to be 3 to 5 feet above the current floodplain, but with rising sea levels, that level may not be sufficient in 15 to 20 years, said Craig Poulton, CEO

of Salt Lake City-based Poulton Associates Inc., the underwriting manager and administrator of private flood insurer Natural Catastrophe Insurance Program.

“The best form of mitigation is don’t build there,” he said. “Building in exposed areas without taking extreme measures to raise the structure out of the floodplain is just foolish.”

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Self-driving cars put insurers to the test

BY MATTHEW LERNER

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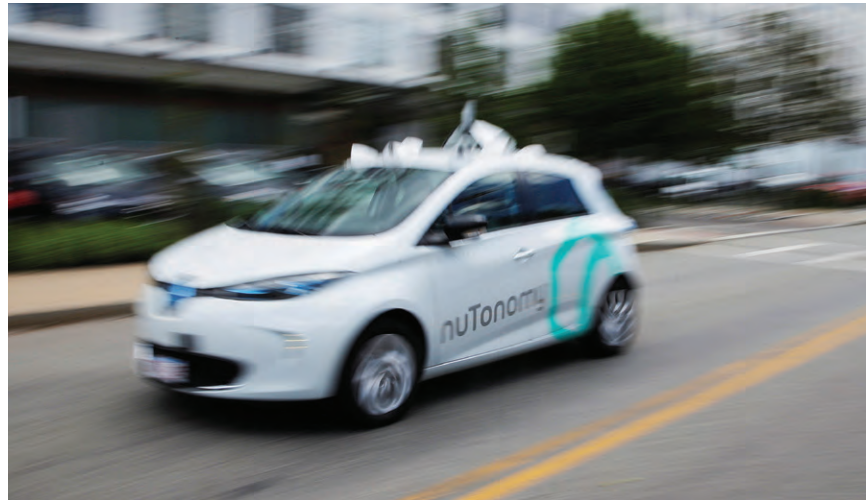
Progress in the race among established and new car manufacturers to field autonomous vehicles is challenging insurers trying to keep pace with developments in transportation.

From dealing with unfamiliar vendors and stakeholders to questions of liability and coverage, the insurance sector must navigate myriad fronts in their efforts to offer appropriate products and coverages for the next generation of automobiles.

According to California Department of Motor Vehicles autonomous vehicle disengagement reports for 2017 — which describe disconnections either from technical failure or drivers taking control — Waymo, the Mountain View, California-based autonomous driving development unit of Google parent Alphabet Inc., logged the most miles of autonomous vehicle testing in the state at 352,545, followed by General Motors Cruise Automation L.L.C., a unit of Detroit-based General Motors Co., at 131,675 miles.

Italian-American auto manufacturer Fiat Chrysler Automobiles N.V. will be supplying Waymo with “thousands” of Chrysler Pacifica hybrid minivans beginning in late 2018 for a planned autonomous ride-hailing service slated to begin in Phoenix this year, according to a statement from the automaker. The new vehicles will result from a collaboration between Waymo and FCA engineers to design self-driving vehicles built on a mass production platform. FCA declined to provide further information. Waymo did not return a request for comment.

Meanwhile, GM has filed a safety petition, part of a regulatory filing required of



REUTERS

A self-driving car being developed by nuTonomy, a company creating software for autonomous vehicles, is guided down a street near the firm’s offices in Boston.

new vehicles, with the U.S. Department of Transportation for its fourth-generation self-driving Cruise AV, which has no steering wheel, pedals or manual controls, to be on the road in 2019, according to a statement from the automaker.

“We’re now getting an idea about how quickly autonomous vehicles will roll out. It looks like we’ll see deployments in a few cities this year or next,” said Paul Carroll, CEO and editor-in-chief at Insurance Thought Leadership Inc. in New York. “But we still don’t know a lot of things. How soon will we move from Level 4 — autonomy within a heavily mapped, limited area — to full autonomy?”

Autonomous vehicles initially will likely have both a limited geographical footprint and set of driving condition tolerances within which they can operate, said Hilary N. Rowen, senior counsel with Clyde & Co in San Francisco and an observer to

the Uniform Law Commission Drafting Committee on Highly Automated Vehicles for the American Bar Association Tort Trial & Insurance Practice Section.

Such limitations for these early vehicles make them better candidates for fleet application than for personal use, she said.

In its 2018 Self-Driving Safety Report, GM said it had “combined the best of Detroit, Silicon Valley and our teams around the world” in the development of its program. This development model, which involves new types of players, raises questions for the insurance industry.

“Historically, we saw two stakeholders participating in the mobility segment: original equipment manufacturers and component suppliers,” said Jose Heftye, sharing economy and autonomous mobility practice leader for Marsh L.L.C. in San Francisco. “Now there is a third stakeholder, the on-demand platforms,” which could

AUTONOMOUS AUDIENCE

- ▲ **77%** of U.S. drivers said autonomous features had a positive influence on their decision to purchase their current vehicle.
- ▲ **28%** percent of U.S. adults said they would not buy, rent, share or travel in a vehicle with autonomous features.
- ▲ Adults in the U.S. expect it will be **2051** before driverless vehicles represent the majority of vehicles on road.
- ▲ **42%** of adults in the U.S. said they would be comfortable sharing the road with driverless vehicles
- ▲ **81%** of U.S. respondents said owners or riders of driverless vehicles in the future should have car insurance.
- ▲ **64%** of U.S. respondents said people who use subscription or on-demand driverless services should have their own auto insurance.

Source: AIG: The Future of Mobility and Shifting Risk

include logistics firms and others, he said.

Suppliers may not be aware of their exposures, said Robert W. Peterson, professor at Santa Clara University School of Law in California. “An OEM held primarily responsible for a loss can pass that loss up the chain to the responsible supplier.”

Innovative technology used to develop the vehicles raises further questions.

In the absence of a court interpretation, Ms. Rowen said, it’s unclear whether a vehicle’s automated driving system — the hardware and software that controls the car in autonomous mode — can be a covered entity under an auto insurance policy.

“The system is not itself ... an insured under an auto policy,” Ms. Rowen said.

“It is still early to determine where the liability risks would fall, and many of these questions are top of mind for insurers,” Lex Baugh, CEO of North America general insurance for American International Group Inc. in New York, said in an email. “The law as it relates to products liability and software embedded in products will evolve as we gain experience with the new technologies.”

Insurance policies for autonomous vehicles may need to be a combination of personal liability, commercial liability and product liability, Mr. Heftye said, to reflect the needs of policyholders who may use the vehicles for personal use and for ride-share or commercial purposes.

“As our mobility behavior changes, we have to think about risk and exposure differently,” Mr. Baugh said. “The shift is upending our conventional wisdom about liability and the way that we predict the cost of risk; however, we know the risk will not disappear. It will shift, largely from human to machine, which will blur the lines between personal and commercial risks,” Mr. Baugh said.

CALIFORNIA OFFERS OPTIONS FOR PROTOTYPE COVERAGE

While insurers grapple with how to insure autonomous vehicles when they hit the public roads, California, the state that hosts many of the autonomous vehicle prototypes, has established insurance requirements for the testing of the vehicles.

One of the options it allows is the posting of a \$5 million surety bond.

“The California Department of Motor Vehicles has promulgated a regulation dealing with the testing of autonomous vehicles and they have specific insurance requirements which must be satisfied by the designer of the vehicle, either through the purchase of commercial auto insurance or

through the posting of a fairly substantial bond,” said Hilary N. Rowen, senior counsel with Clyde & Co in San Francisco.

Ms. Rowen is also an observer to the Uniform Law Commission Drafting Committee on Highly Automated Vehicles for the American Bar Association Tort Trial & Insurance Practice Section.

“For testing purposes, it is very specific from a regulatory environment what type of insurance policy you need,” said

Jose Heftye, sharing economy and autonomous mobility practice leader for Marsh L.L.C. in San Francisco.

At first, “The challenge was to develop insurance programs and the right capac-

ity for vehicles testing on public roads, which at the beginning was very, very difficult,” Mr. Heftye said. “It is now fairly straightforward to get that type of coverage,” which is still based on auto liability together with different components. Mr. Heftye was unable to provide further details due to nondisclosure agreements.

Many companies have evidently met the burden. The list of 17 manufacturers that filed the State of California Autonomous Vehicle Disengagement Reports for 2017 stretches from Baidu USA L.L.C. to Zoox Inc. and includes well-known names such as BMW A.G., Ford Motor Co., GM Cruise L.L.C. and Mercedes-Benz.

Matthew Lerner



Family leave law confuses employers 25 years later

BY ROB LENIHAN

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The Family and Medical Leave Act celebrated a milestone birthday in February, but employers still struggle to comply with the 25-year-old law.

Employers often get tripped up on core elements of the law, including notifying employees of their rights to take FMLA leave — in some instances, without them even officially requesting it — and the documentation they can ask employees for to support any leave requests, legal experts say.

The FMLA — signed into law by President Bill Clinton on Feb. 5, 1993 — allows eligible employees to take up to 12 work weeks of unpaid leave during any 12-month period to attend to a serious health condition of the employee, parent, spouse or child, or for pregnancy or care of a newborn child, or for adoption or foster care of a child.

Employers are obligated to provide FMLA leave if workers report to a site with 50 or more employees within a 75-mile radius.

Jeff Nowak, Chicago-based co-chair of the labor and employment practice group for Franczek Radelet P.C., said the FMLA “has withstood the test of time to providing job-protected time to people who need it when they are severely injured, or their family members are injured or ill.”

“It is critical employers carefully administer the FMLA and become acutely aware of its rules, because those rules often trip employers up, thereby creating liability,” he said.

New York attorney Eric M. Nelson said the impact of the FMLA has been enormous, noting that at least three states, including New York, now have paid leave laws, New York City in November 2017 expanded its paid leave law, and “the concept now of paid family leave is on the president’s agenda.”

“In my experience, employers aren’t as well versed as they should be in when they must allow or can deny leave,” Mr. Nelson said. “They’re also often unsure what they can ask for in the way of notice from employees seeking leave, and what they can require from employees in the way of documentation to support a request for leave.”



Mr. Nelson added that best practices for employers include making sure their human resources personnel have both training and available resources regarding what is required of the company in connection with the employee’s request for, and the company’s rights regarding, leave.

Matthew Gomes, a partner with Weinberg, Wheeler, Hudgins, Gunn & Dial L.L.C. in Atlanta, said when a human resources manager or supervisor learns of an employee with a potentially serious health condition, “the employee doesn’t have to say, ‘I would like to take FMLA leave.’”

“You may have an affirmative duty to inform the employee of his or her rights under the FMLA,” Mr. Gomes said. “There have been a number of FMLA claims that have arisen in that circumstance because the employee says, ‘you the employer should have let me know that I could’ve taken FMLA leave and by not doing that you denied my FMLA rights as a result.’”

Stacie Caraway, employment law attorney with Miller & Martin P.L.L.C. in Chattanooga, Tennessee, describes FMLA documentation as “an employer’s FMLA prenup defining your FMLA marriage.”

“The big takeaway is to make sure your FMLA leave policy and your process for reviewing and approving FMLA leave paperwork has been vetted by legal,” Ms. Caraway

said. “Employers have to think about what does the paperwork actually say. If there’s something on the FMLA leave paperwork that doesn’t make any sense or is asking you to approve leave on an ‘as needed’ basis, you have a seven-day period to get corrected paperwork once you tell the employee in writing that there’s a problem, and if they don’t correct it you can deny the leave.”

Barbara Hoey, a partner with Kelley Drye & Warren L.L.P. in New York, said employers “have a legal right to push back if the initial documentation is not sufficient, and the reason I have clients do that is once you’ve certified it, you’re stuck. You’ve done it, you’ve certified it, and now your rights are much more limited.”

Maria Rodriguez, partner and Western region head of the employment group with DLA Piper in Los Angeles, advised that the “employer’s policy needs to be clear, it needs to be distributed to all employees, and it needs to model the FMLA and any related state laws.”

“Intermittent leave of absence may qualify as FMLA or the equivalent law, so managers need to be trained to work with human resources so that when employees are taking time off on some sort of a regular or consistent basis, they need to be trained to make sure those employees are working with HR,” she said.

“You see a lot of abuse where people have this condition that flares up on Monday mornings and Friday afternoons,” Mr. Gomes said.

Debbie Friedman, member of Cozen O’Connor in Philadelphia, warned against automatically firing an employee if he or she does not return immediately to work after the 12-week leave has ended.

“This law can’t be viewed in a vacuum,” she said. “An employer has to carefully evaluate whether an employee is entitled to additional time off under state or local laws or ordinances or pursuant to company policies on leaves of absences.”

PRIVACY VIOLATED IN FMLA CASE

Some employers have gotten themselves into legal trouble with the Family and Medical Leave Act.

In January 2015, the 6th U.S. Circuit Court of Appeals in Cincinnati ruled in *Terry Tilley v. Kalamazoo County Road Commission*; *Kalamazoo County Road Commission Board of Commissioners* that a commission employee was entitled to FMLA coverage, even though the commission was not obligated to provide the coverage, because of a misleading statement in its employee manual.

While the 6th Circuit agreed with the district court that the commission did not have the required 50-employee/75-mile threshold that normally required it to provide FMLA coverage, the commission’s employee manual stated that employees covered under the FMLA “are full-time employees who have worked for the road commission and accumulated 1,250 work hours in the previous 12 months.”

“Make sure your employee handbook is up to date,” said Lindsay Freedman, an associate with the Thatcher Law Firm L.L.C. in Greenbelt, Maryland. “And that you have a section on what an employee should do when they request leave. Make sure your policies are clear.”

Some smaller companies may be using a handbook that has not been updated or that has not been reviewed by an attorney, he said.

“Maybe they got some stock language online that doesn’t pass muster with the law,” he said.

Meanwhile, an employee’s privacy became an issue in an FMLA case last year.

In January 2017, a court ruled an employer violated the FMLA when an employee’s request, which included his personal medical information, was revealed to co-workers who teased him about it.

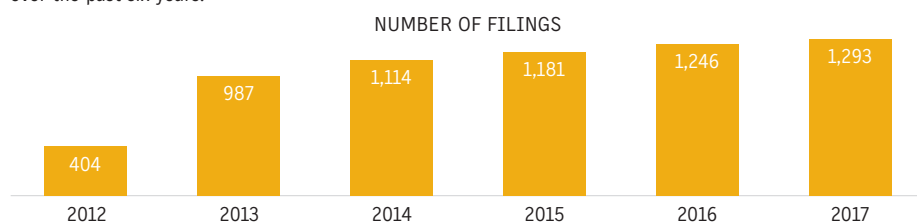
In *Scott Holtrey v. Collier County Board of County Commissioners*, the U.S. District Court in Fort Myers, Florida, found that the “enforcing labor regulation makes clear that confidentiality of medical information is a right provided and protected under the FMLA.”

The court also refused to dismiss Mr. Holtrey’s retaliation claim, stating his allegations of co-workers’ repeated and frequent jokes and obscene gestures about his condition “suffice to state an adverse employment action.”

Rob Lenihan

RIISING TIDE OF FMLA CASES

The number of civil cases alleging violations of the Family and Medical Leave Act has risen significantly over the past six years.



U.S. District Courts: FMLA civil cases commenced during 12-month periods ending Dec. 31, 2012, to Dec. 31, 2017. Data collection for FMLA category began on Oct. 1, 2011.

Source: Administrative Office of the U.S. Courts

Drug shift solves one problem, raises another

BY LOUISE ESOLA

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The workers compensation industry is leaning on anti-inflammatory drugs as it seeks to move away from opioids as a prescription for pain for injured workers.

But some medical experts are concerned that this shift could also lead to overprescribing, overutilization and serious side effects such as gastrointestinal bleeding and liver and heart problems.

Known in the marketplace as non-steroidal anti-inflammatory drugs, this class of pain relievers aims to reduce inflammation, a common cause of musculoskeletal pain. NSAIDs, as they are dubbed, come in prescription strengths with generic names such as celecoxib, etodolac and diflunisal. They are also sold in over-the-counter varieties under common household names that include Advil, Aleve and Motrin or generic names such as ibuprofen and even aspirin.

"We are shifting toward (NSAIDs), and there are side effects we are concerned with," said Reema Hammoud, Southfield, Michigan-based director of clinical pharmacy for Sedgwick Claims Management Services Inc.

"We are on guard," Nikki Wilson, Omaha, Nebraska-based pharmacy product manager for Coventry Workers Comp Services, said of the industry's trend toward nonopioid pain medications.

"We know there needs to be a lot of education on the front end" of prescribing anti-inflammatory drugs, she added.

Most in the medical community have recently put NSAIDs in another category: safer than opioids.

The California closed drug formulary for injured workers launched on Jan. 1 has moved all opioids into the "nonexempt" category, meaning a utilization review is required beyond a four-day supply. Yet the formulary allows most pain-relieving anti-inflammatory drugs, classifying



ANTI-INFLAMMATORY DRUG CONSUMERS

- Of 1,326 ibuprofen users, **87%** took them over the counter, with **9.5%** taking them in conjunction with prescription non-steroidal anti-inflammatory drugs, or NSAIDs.
- **61%** did not recognize that what they were taking was an NSAID.
- Of those prescribed one pill, **64%** did not know they were not supposed to take more.

Source: "Exceeding the daily dosing limit of nonsteroidal anti-inflammatory drugs among ibuprofen users." Pharmacoepidemiol Drug Safety, 2018 issue.

the drugs as "exempt" from a utilization review, meaning doctors can generally prescribe them for pain without regulatory oversight.

The formulary lists 28 NSAIDs, with four that are nonexempt and come with restrictions for prescribing to injured workers, according to the drug list.

"Most state formularies and treatment guidelines recommend NSAIDs first," said Dr. Brigitte Nelson, Scottsdale, Arizona-based senior vice president of workers compensation clinical management at Express Scripts Holding Co. "Yet they are

not innocuous drugs."

Those managing workers comp claims and injured workers' prescriptions say a close examination of side effects has some putting the brakes on NSAIDs, or at least treading cautiously.

"The side effects are not fatal if you know what you are doing," Ms. Wilson said.

The U.S. Food and Drug Administration's list of 19 side effects includes heart attack, stroke, high blood pressure, kidney and liver failure and stomach ulcers.

The longer NSAIDs are taken, the higher the risk of developing or worsening such conditions, according to the FDA.

For example, a person with a heart condition should take the "lowest dose possible," said Ms. Wilson, who added, "or not at all." In some cases, she said, the patient is "left with opioids" as a safer option for treating pain.

"You have to look at all the patient factors and evaluate that patient to prevent these side effects," said Ms. Hammoud, adding that some risks can be mitigated with other medications, such as protective agents for the gastrointestinal tract. "There

are ways to prescribe them where they are not dangerous."

Most prescribers are aware of what to do and how to prescribe, but the patients themselves can raise the risk by being uninformed, Dr. Nelson said.

"Prescribers are careful, but consumers are not," said Dr. Nelson, who said some of the risk in comp — and the delay of recovery and exacerbation of health problems that come with side effects — can be out of the industry's hands because they don't know the patients are mixing medications.

Undisclosed NSAID drug combinations increase the risk exponentially, experts say. That's when an injured worker suffering from pain takes both a prescription formula and an over-the-counter NSAID, unaware that mixing the two can put a patient on the fast track to more serious side effects.

"I think one of the things that we've discovered is that people know what they are taking, they know what the product is called, but they don't know what it is or what's in it," said David Kaufman, a Boston University epidemiologist and researcher who in 2017 conducted a study of 1,326 ibuprofen users, including some who also took prescription formulas in conjunction with what they purchased over the counter. "If they don't know it's an NSAID and they don't know they shouldn't take more than one NSAID at a time, then they get into trouble."

Mr. Kaufman had patients keep a seven-day diary on medications and, upon inspection, found that "most did not recognize all products taken as NSAIDs."

"We can prevent so much by educating our patients and letting them know that these are chemicals and we have to be careful," said Ms. Hammoud.

"Especially with long-term use, we don't want to see anybody taking anything long term. Everything comes with side effects," she said.

'PILL FOR EVERY ILL' MENTALITY DRIVES HUNT FOR PAINKILLERS

The shift from opioids to anti-inflammatory drugs for pain has much to do with patient expectations, the medical community's rush to prescribe and the drug industry's push to fix problems with a pill, according to experts.

Dr. Robert Goldberg, chief medical officer and senior vice president of Healthsystems L.L.C., a Tampa, Florida-based national workers compensation pharmacy and ancillary benefits management provider, calls the pick between opioids and non-steroidal anti-inflammatory drugs a "false choice."

"Right now, the conversation has been dominated by pharma," he said. "Pill for every ill — we have been hearing that for 30 years."

Another issue is that most patients seeing a doctor expect a prescription, said Nikki Wilson, Omaha, Nebraska-based pharmacy product director for Coventry Workers Comp Services.

"The psychology of why we prescribe is patients' expectation and demand," she said. "The mentality has been give them a prescription and get them out the door."

The U.S. Food and Drug Administration

found in a 2004 study that 42% of those seeking a doctor's care expect a prescription; 63% of those individuals are seeking a refill.

Workers compensation is trying to change that, said Dr. Brigitte Nelson, Scottsdale, Arizona-based senior vice president of workers compensation clinical management at Express Scripts Holding Co. "All of the treatment guidelines for managing pain are emphasizing nonpharmacological therapies," she said.

"Pain control should always start with

nonpharmacological forms of treatment," said Dr. Goldberg, who puts self-care, ice, heat, exercise and other alternative, physical therapies at the top of the list.

"The onus is on the patients — they have to participate in their own care," said Sylvia Sacalis, Tampa-based pharmacist and vice president of clinical services for Healthsystems. "They need to take part in some of these modalities. A pill is easier, but there are other modalities they have to be willing to try. It's a mind shift — they have to get their mind there."

Louise Esola

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Gig economy workers in comp gray area

BY JOYCE FAMAKINWA
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The gig economy continues to grow, but gig workers hoping for workers compensation coverage face an uncertain future.

Their employment status, or lack thereof, and therefore their eligibility for workers comp benefits is often determined by how tightly the gig company controls their schedules and other aspects of their work, according to legal experts.

In the California federal court case *Lawson v. Grubhub Inc. et al.*, a judge ruled last month in favor of Chicago-based Grubhub Inc., an online and mobile food ordering company that allows users to receive deliveries from local restaurants.

Raef Lawson, a former Grubhub delivery driver, alleged that he was an employee and should be compensated for unreimbursed expenses, while Grubhub argued that Mr. Lawson was an independent contractor. The judge ruled that since Grubhub did not control how Mr. Lawson made deliveries, his transportation, his appearance or his schedule, he was correctly classified by the gig economy company as an independent contractor.

The level of control companies place upon workers is a huge factor when it comes to determining if gig economy workers are considered employees instead of independent contractors, according to legal experts.

"The law requires you to look at whether these workers are controlled or not controlled by these companies," said Simona Agnolucci, a San Francisco-based partner at Kecker, Van Nest & Peters L.L.P. "You look at things like who sets their schedule, who tells them what to do, and one important consideration is that many gig economy workers do what's called 'multi-apping.' They log in and out of various platforms during a single workday. So they might give a Lyft ride, then pick up a Caviar delivery, and then make a trip for Postmates. Employees don't work that way. You don't walk into McDonald's, make a burger and then take off your uniform and go next door to Burger King, fill a few orders for them and go back to McDonald's."

Mr. Lawson's attorney plans to appeal the court's decision.

"The California Supreme Court is considering adopting a stricter test for employee classification, under which



REUTERS

Grubhub Inc., which debuted on the New York Stock Exchange in 2014, was at the center of a case over whether its drivers are employees or contractors.

we would have won under the court's reasoning, so we are going to ask the court to wait while the Supreme Court issues its decision in that case (*Dynamex Operations West v. Superior Court*)," Mr. Lawson's attorney, Shannon Liss-Riordan, San Francisco-based partner at Lichten & Liss-Riordan P.C., said in an email.

The company is pleased with the court's decision and is prepared to defend it if an appeal occurs, according to an emailed statement from Grubhub's attorney, Michele L. Maryott, a partner with Gibson, Dunn & Crutcher L.L.P. in Irvine, California.

While the case centers on wage and hour issues, some experts say it is significant for the gig economy and the misclassification question, which could determine whether workers can receive comp benefits.

"Regarding the impact on workers comp and employee status, the two are really tied together very closely," said Richard Meneghello, a Portland,

Oregon-based partner at Fisher & Phillips L.L.P. "If the judge were to have decided that Lawson were an employee and not an independent contractor, then Lawson would have been entitled to workers comp benefits. The ruling is significant in that it forecloses the opportunity for other Grubhub drivers to make a similar argument and to essentially ask the court to put them in the category of employees that should be deserving of workers comp benefits."

But the decision is limited in its scope, according to other experts.

Although the decision is "helpful" to gig employers, the legal standard for independent contractor status under wage laws and workers compensation statutes are often very different, said Cheryl Wilke, a Miami-based partner at Hinshaw & Culbertson L.L.P.

"It is anticipated that individuals will continue to pursue employment status under state workers compensation laws which favor coverage," she said.

The comp industry has not engaged with the gig economy in any meaningful way and is mostly taking a wait-and-see approach, experts say.

"What I'm seeing, looking at the industry as a whole, is that everyone knows that this is an issue and they are having dialogues internally within the industry and at their companies, but they are waiting to see," said Christina Goldschmidt, New York-based vice president of customer experience design at digital experience agency Cake & Arrow who has researched and written about the gig economy and commercial insurance. "It's a gray area, and it's going to be either an opportunity or a larger risk that emerges, but right now they have yet to figure that out. People are trying to propose ideas that would be a win-win."

Last year, Uber Technologies Inc. began taking steps to provide a version of workers comp coverage to its drivers. In some states, Uber drivers have access to an insurance program for workers injured on the job that would help pay medical bills and replace their normal earnings. The coverage would cost drivers less than 4 cents per mile.

Uber's program is unique, and gig economy companies may be hesitant to provide coverage for workers because it would place them in the category of employer, experts say.

"I would think that in order to do this, companies would want some sort of bargain with state and federal regulators," said Mr. Meneghello. "In other words, we are willing to do this to provide a greater safety net to workers in the gig economy, but we don't want to get burned for it. We don't want you to turn around and say, aha, as a result of you doing this thing ... we are going to rule in these other cases that these people are employees and not contractors."

POSTMATES PAID PREMIUMS, BUT CASES STILL RARE

Grubhub Inc. is not the only gig economy company to grab headlines when it comes to the employees vs. independent contractors debate.

In 2016, the Washington state Department of Labor & Industries ordered San Francisco-based food delivery service Postmates Inc. to retroactively pay workers compensation premiums for more than 3,000 of its couriers in the state. Postmates considers its workers who deliver food from restaurants and grocery stores independent contractors, but the department determined that the company should pay \$323,027 in audited workers comp premiums for those workers.

"Part of the reason we haven't seen more of this is that

there is a good deal of anxiety about whether to fight out a particular case in a particular jurisdiction," Michael C. Duff, a Laramie-based professor at the University of Wyoming's College of Law, said in explaining why more cases along these lines haven't been filed.

"Any case that would go to a jury is particularly problematic," he said. "If a case makes it to a jury ... then you would be likely to see a settlement."

"If I was Uber or Grubhub or Lyft, I would be very nervous every time a case makes its way to trial," Mr. Duff added. "Employers don't want cases to go to trial. They want them dismissed at the summary judgment stage."

Joyce Famakinwa

THE GIG ECONOMY AND INSURANCE

The gig economy is made up of companies and workers who engage with each other through short-term contracts and freelance work based on an online platform. Cake & Arrow, a New York-based digital customer experience agency, surveyed gig economy workers about insurance in a recent report.

18%
Have insurance

89%
Are unaware of insurance policies that cover them

56%
Have considered buying insurance

44%
Have not considered buying insurance

55%
Said their work was not a safety risk

Source: Cake & Arrow, Insurance in the Age of the Gig Economy, 2017

Safety standard reflects global supply chains

BY GLORIA GONZALEZ

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A building collapse in Bangladesh that killed more than 1,000 workers in the garment industry in April 2013 helped propel the development of an occupational health and safety management systems standard that aims to improve the safety of workplaces across the globe, experts say.

The Savar, Bangladesh, building collapse isn't the only example of the dangers of lax standards, but the tragedy demonstrated the workplace safety risks inherent in global supply chains and heightened efforts to develop the ISO 45001 standard — the first global standard for occupational health and safety management systems.

"That particular incident drove and pushed people to move faster in getting this standard developed," said Derek Eversdyke, director of facility safety products at safety signs and labels designer and manufacturer Clarion Safety Systems L.L.C. in Milford, Pennsylvania.

The International Organization for Standardization developed the standard over a 4½-year period, and it was approved in January by about 93% of the ISO membership — beyond the two-thirds majority needed for publication — and is scheduled for publication on March 12.

"It is clear to the world that this is going to be a big game-changer," said Mr. Eversdyke, a member of the U.S. technical advisory group on ISO 45001.

A key component was getting buy-in for the standard from more than 60 countries as global supply chains extend beyond the United States and Europe, experts say.

"It's hard to get that level of consensus given the different needs that we all have from our different countries," said Victor Toy, chair of the U.S. technical advisory group on ISO 45001 administered by the American Society of Safety Engineers and a San Francisco-based principal with consultancy Insyst OH&S. "That's a great signal."

The standard will provide a framework for occupational health and safety goals, facili-



REUTERS

The 2013 collapse of a building in Savar, Bangladesh, housing garment factories led to increased efforts to develop a global safety standard, which will be published this month.

tating the identification of workplace safety risks and solutions and metrics for measuring the success of safety initiatives to reduce the nearly 2.8 million workplace fatalities across the globe, according to the ISO.

"It's forcing you to look at all the risks you have as a company, find out what those opportunities are, and then decide as a team which of those opportunities you're going to include in your plan for the year," said Randy Parnow, corporate safety manager at industrial supply company Fastenal Co. in Winona, Minnesota.

The ISO 45001 standard is designed to build on and integrate with previous standards such as ISO 14001, which governs environmental management, and ISO 9001, which governs quality management, among other standards.

"What I like about (the standard) is that it can work with the other programs," Mr. Parnow said. "I like that you can use it to bring the environment and safety together in one plan. I like that it ensures that you have employee involvement, because a lot of times companies will try to set up a safety program and without employees involved, if they have no ownership, they don't care. When they're involved in the process, then they care."

"This standard is putting language in place that really shows what that top senior management commitment to safety looks like," said Larry Poague, senior loss control consultant with Lockton Cos. L.L.C. in Kansas City, Missouri.

The ISO 45001 standard also encourages a more proactive approach to risk identification, assessment and mitigation, experts say.

"The most obvious risks are those that people identify from lagging indicators such as injuries and illnesses," Mr. Toy said. "The challenge for that is that we're looking backwards at what has happened rather than focusing on true risks. This really is a risk management standard."

"I think the difference is being proactive

versus being reactive," Mr. Eversdyke said.

The United States also has a standard called ANSI Z10 for occupational health and safety management systems, while OHSAS 18001 was the de facto international standard, Mr. Toy said.

"Since this is a system that is now a global one, rather than having to adopt individual country standards on how you manage occupational health and safety, it's really going to make it easier for organizations to do business across country lines, whether or not you have operations or you have suppliers in other countries that you do business with," Mr. Toy said.

"At least from the safety community, we're seeing a positive push to bring labor standards up and outside of our country and into the global supply chain," Mr. Poague said.

Many organizations currently using the 18001 standard have pledged to certify to the ISO 45001 within the three-year transition period, Mr. Toy said, adding that he thinks the potential for adoption of 45001, given its global nature, could be even wider than 18001.

"I think you're going to see a big migration from 18001 to the 45001 because it's just a better system," said Edwin Foulke, an Atlanta-based partner at Fisher & Phillips L.L.P., a former OSHA assistant secretary of labor and a member of ASSE's technical advisory group.

"Companies that get into this are going to significantly improve their safety programs, and that's going to translate into less workers comp costs and the total costs associated with injured employees," Mr. Foulke said.

SAFETY AWARENESS

- ✦ Most contractors in the construction industry — 88% — are at least aware of the U.S. Occupational Safety and Health Administration's safety and health program management guidelines, and 54% have made changes to their programs based on them, according to a report by Silver Spring, Maryland-based CPWR-The Center for Construction Research and Training and New York-based Dodge Data & Analytics published in December.
- ✦ However, 93% of larger companies — those with 100 or more employees — are aware of the guidelines compared with 79% of smaller companies, defined as those with fewer than 50 employees. The smallest companies, with fewer than 20 employees, are the only ones where less than half of those who are aware of these guidelines have made changes based on them, according to the report.

OSHA GUIDELINES HELP SMALLER FIRMS CREATE EFFECTIVE SAFETY PROGRAMS

While the soon-to-be-published ISO 45001 safety standard aims to help large and multinational employers implement workplace safety systems, the U.S. Occupational Safety and Health Administration's safety and health program guidelines help small to midsize employers implement effective programs.

OSHA released its long-awaited update to its 1989 guidelines in October 2016, with a key change being the addition of a section specifically addressing

multiemployer workplaces. The guidelines now include seven core elements — up from six — for a safety and health program: management leadership, worker participation, hazard identification and assessment, hazard prevention and control, education and training, program evaluation and improvement, and communication and coordination for host employers, contractors and staffing agencies.

Although the OSHA guidelines talk about some of the same topics as the ISO 45001

standard set for publication on March 12, they do not go into the same level of detail as the private-sector standard, experts say.

"If you're a small company in particular and you don't have the resources to do anything else, that helps you," said Edwin Foulke, an Atlanta-based partner at Fisher & Phillips L.L.P., a former OSHA assistant secretary of labor and a member of the American Society of Safety Engineers' technical advisory group on 45001. "But you're going to see more and more

companies go into 45001."

"The OSHA program is particularly good for small businesses that are looking for a simple system," said Victor Toy, chair of the ASSE's technical advisory group and San Francisco-based principal with consultancy Insyst OH&S. "Those who are a little more advanced seek to adopt (ANSI Z10) or 45001 because they have a higher level of integration and concepts related to managing these risks."

Gloria Gonzalez

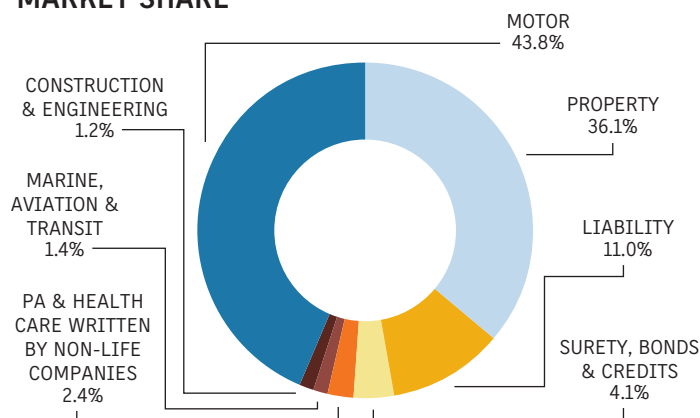
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GLOBAL
P/C MARKET
RANKING

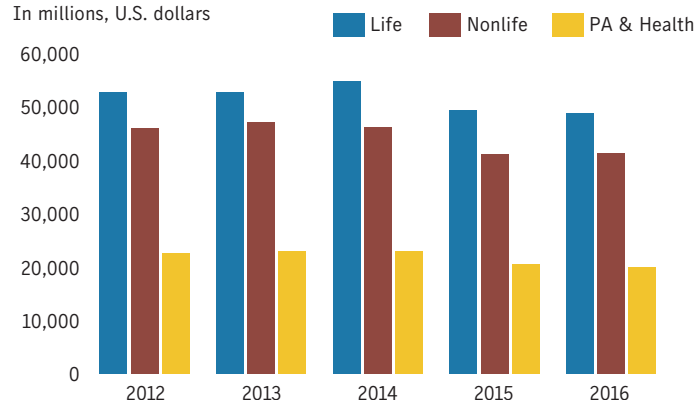
The Canadian economy is the 10th largest in the world. As part of the North American Free Trade Agreement, however, it's highly integrated with that of the U.S., which absorbs approximately three-quarters of Canada's exports. The property/casualty market is mature and dominated by a few large local insurers and foreign companies from Europe and the United States. Business written in Ontario predominates, accounting for nearly 50% of total premium, followed by Alberta, which has a significant amount of mining and energy activity, and Quebec. Canada is the only major economy without some sort of state-supported flood program, and discussions about how best to develop a market solution for flood-prone areas are ongoing. Interest in cyber-related risks is growing, but the takeup rate is still modest. Insurers and brokers see this sector as the main area of potential growth in the next few years.

MARKET SHARE



MARKET GROWTH

In millions, U.S. dollars



Source: Axco Global Statistics/Industry Associations and Regulatory Bodies

COMPULSORY INSURANCE

- Auto third-party bodily injury/property damage and automobile accident benefits coverage
- Workers compensation (state plan)
- Aviation liability
- Shipowners liability for marine oil pollution
- Liability for the operation of pipelines and nuclear installations
- Property and sometimes liability insurance (including D&O) for condominiums

NONADMITTED

Unauthorized insurers are not permitted to carry on insurance activity in Canada. At the same time, there is nothing in the law indicating that insurance must be purchased from locally authorized insurers, with some exceptions. This is generally interpreted to mean that insurers can issue policies from abroad, with some exceptions, if approached by a buyer and/or a specially licensed intermediary in some provinces.

INTERMEDIARIES

Intermediaries must be authorized to transact insurance business and are licensed and regulated at the provincial level. A reciprocal licensing system for agents and brokers has been adopted and provides that the host province will accept most of the licensing requirements established by the home province but may also request additional requirements.

MARKET PRACTICE

Canada's licensed market is large, and its unlicensed market is well established, operating through managing general agencies that have binding facilities available for most classes of business. Therefore, it is rarely necessary to deviate from established practice in placing business.

MARKET DEVELOPMENTS

Updated January 2018

- Overall profitability in Canada tends to be based on the extent of natural perils insured losses in any given year, with 2016 being affected especially by the magnitude of the claims arising from the Alberta wildfires. The underwriting profit margin in that year was just 1.07% of net earned premium.
- In recent years, there has been significant merger and acquisition activity among insurance brokers. Consolidators have been particularly active, buying up small and medium-sized companies to create nationwide operations, and some insurers have diversified into broking to maintain control of portfolios of business and expand the distribution base for their products.
- The market remains very competitive in most areas, although local sources suggest that rates stopped falling during 2017 and that many risks with a poor loss record are starting to be subject to modest rate increases. Some major insurers are refusing to grant continued premium reductions and are prepared to let business go rather than compromise on their terms.
- The Nuclear Liability and Compensation Act, which took effect on Jan. 1, 2017, repealed the Nuclear Liability Act and increased the no-fault liability of nuclear plants over three years to CA\$1 billion (\$775 million). Nuclear plant operators must carry an insurance policy for at least half this amount and may provide an alternative financial security for the balance.
- Overland flooding had been an uninsurable risk across Canada, but most insurers are now said to be offering some form of cover, albeit selectively and often not in high-risk locations.



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square miles

POPULATION

36.8

million

MARKET CONCENTRATION

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market share of top five insurers

2017 GDP CHANGE (PROJECTED)

3.1%

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Flight attendant's shuttle bus injury ruled work-related

■ A Pennsylvania appeals court ruled in favor of a US Airways flight attendant who claimed her slip and fall on a shuttle bus transporting her between a Philadelphia International Airport terminal and an employee parking lot was work-related.

On Jan. 23, 2015, flight attendant Kimberly Anne Zabroski was trying to place her luggage on the racks on a shuttle bus after parking in a city-owned lot. On the bus, she stepped in water on the floor, causing her right foot to slide out from underneath her, according to court documents in *US Airways Inc. v. Workers Compensation Appeal Board*.

A three-judge Commonwealth Court panel unanimously rejected arguments posed by US Airways that the incident did not take place on the airline's property and that the shuttle bus was part of Ms. Zabroski's commute to work, according to court documents.

The ruling found that her commute ended at the parking lot and work began on the shuttle: "As part of doing business with the airport, employer understood that the airport would transport employer's employees who drove to work. Thus, employer also understood that, in order to arrive at their work area to start their shift, employees who drive to work invariably board the shuttle bus after their commute to the airport."

IBM lawsuit casts diversity in starkly competitive terms

■ International Business Machines Corp.'s insistence in a lawsuit that its efforts to recruit and maintain a diverse workforce are trade secrets highlights how companies can see the issue in competitive terms, business and legal experts said.

Armonk, New York-based IBM last month sued its former chief diversity officer, Lindsay-Rae McIntyre, who left for a similar job at Microsoft Corp. The lawsuit alleges Ms. McIntyre violated a one-year noncompetition agreement and could disclose IBM's diversity data and hiring plans.

The lawsuit is unusual because IBM is arguing its diversity data and strategy are economically valuable "trade secrets," a legal term typically associated with closely guarded formulas like Coca-Cola's. It appears to be the first company to bring such a lawsuit against a rival over diversity efforts, legal experts said.

IBM cited in its complaint Ms. McIntyre's knowledge and oversight of its plans to hire 50 diverse candidates to executive positions and its development of artificial

intelligence-based tools to track the career development of women and minorities at the company. According to IBM, knowledge of this "highly confidential, proprietary and competitively sensitive information" would allow Microsoft to compete for the same talent and business from customers that value diversity.

Y-Vonne Hutchinson, an Oakland, California-based diversity consultant and lawyer who works with the tech industry, said IBM has had a legitimate edge over its industry rivals when it comes to diversity. IBM's tools for reaching its diversity goals could qualify as trade secrets if it can show they are valuable to competitors, said Villanova University law professor Michael Risch.

Redmond, Washington-based Microsoft, which is not named in IBM's lawsuit, said it had no interest in IBM's confidential information.

Reuters



AIG unit prevails in 'Catch-22' coverage dispute

■ A federal court ruled that a unit of American International Group Inc. does not have to pay a Jacksonville, Florida, maritime company that reportedly spent over \$2.5 million defending an executive from antitrust charges.

National Union issued an executive and organization liability policy to Crowley in November 2007, according to court records in *Crowley Maritime Corp. v. National Union Fire Insurance Co. of Pittsburgh, Pa.* The policy provides that the "criminal ... investigation of an insured person" triggers coverage once the "insured person is identified in writing" by an "investigating authority as a person against whom" a criminal proceeding has commenced.

On April 17, 2008, the U.S. Department of Justice served a search warrant at Crowley Liner Services, a Crowley subsidiary, seeking various documents from the company and four Crowley Liner employees, including Vice President Tom Farmer. The affidavit listed Mr. Farmer as a "subject" of

the investigation; the affidavit was sealed until 2015. On April 25, 2008, Crowley provided National Union notice of a claim under the policy and asked the insurer to advance Mr. Farmer's defense costs.

National Union maintained that "based on the documentation currently available," which included a subpoena issued to Mr. Farmer, the policy did not provide coverage for him because it did not identify him "in writing as a target of any investigation." In February 2013, the Justice Department offered Mr. Farmer a plea deal, which identified him in writing as a target of an investigation. National Union agreed to cover Mr. Farmer's subsequent defense costs.

Mr. Farmer did not accept the deal and was acquitted by a jury of price-fixing and bid-rigging charges. Following acquittal, Crowley obtained a copy of the unsealed affidavit and went into arbitration with National Union to cover Mr. Farmer's defense costs from the original notice of a potential claim. But the parties did not obtain the affidavit during the arbitration, and the arbitrators determined that everything Crowley had submitted to National Union through 2012 did not amount to a claim.

"The answer is a Catch-22 for Crowley," Judge Timothy Corrigan of the U.S. District Court for the Middle District of Florida wrote in his decision. "If it was in 2008, then Crowley is precluded from re-litigating the issue; if it was in 2015, Crowley's demand is barred by the plain text of the policy's discovery period."

Construction firm wins appeals ruling in insurance dispute

■ The 10th U.S. Circuit Court of Appeals in Denver overturned a lower court decision and ruled that a construction company can seek up to \$25 million in coverage from two insurance firms for damages to equipment at four power plants.

In *Black & Veatch Corp. v. Aspen Insurance (UK) Ltd.* the court ruled that Overland Park, Kansas-based Black & Veatch can seek reimbursement from London-based Aspen Insurance and Lloyd's of London syndicate 2003 for damage Black & Veatch incurred due to damaged equipment that its subcontractor had constructed at power plants in Ohio and Indiana.

The U.S. District Court in Kansas City, Kansas, had ruled that Aspen did not have to pay Black & Veatch's claim under its commercial general liability insurance because the company's expenses arose from property damages that were not covered "occurrences" under the policy.

However, the appeals court held that "the damages were accidental and resulted in harm to a third-party's property, thus meeting the policy's definition of an 'occurrence.'"

DOCKET



WHISTLEBLOWER LOSES SUPREME COURT CASE

The U.S. Supreme Court in February refused to broaden protections for corporate insiders who call out misconduct, throwing out a lawsuit brought against a real estate trust by a former employee who had reported alleged wrongdoing internally but not to the U.S. Securities and Exchange Commission. The justices ruled 9-0 in favor of Digital Realty Trust Inc., deciding that the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act protects whistleblowers from retaliation only if they have brought their claims of securities law violations directly to the SEC.

Reuters

CONTRACTOR SETTLES RETALIATION SUIT

The U.S. Occupational Safety and Health Administration and Steubenville, Ohio-based Environmental Management Specialists Inc. settled a lawsuit alleging the company retaliated against an employee who reported workplace safety concerns about confined space and respiratory hazards when cleaning storage tanks. In addition to paying back wages, EMS will expunge the termination and all references to the action from the employee's record. "An employee's commitment to workplace safety should be commended — not punished," Ken Nishiyama Atha, OSHA Chicago area regional administrator, said last month in a statement.

COMP LAWYER FACES SANCTIONS OVER THEFT

The Board of Professional Conduct of the Supreme Court of Ohio recommended that a lawyer who allegedly stole workers compensation payment funds from clients be permanently disbarred. Brian Wade Harter of Columbus, Ohio, allegedly violated the state's professional conduct rule on numerous occasions documented in a 27-page court ruling in February. In addition to a permanent disbarment, the board recommended Mr. Harter be ordered to pay back his former clients and to pay for all court proceedings, the sum of which was not disclosed.

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Bill Scaldaferri was appointed CEO for Allianz Global Corporate & Specialty S.E. in North America in July 2016 and is responsible for the Allianz S.E. unit's business in the U.S. and Canada, which accounts for about 40% of AGCS's global annual gross written premium of €7.4 billion (\$9 billion) in 2017. He previously ran AGCS's alternative risk transfer group and represented that business to its board. He also managed specialty lines on a global basis for AGCS, serving as chief underwriting officer for that business. New York-based Mr. Scaldaferri recently spoke with *Business Insurance* Reporter Matthew Lerner about innovation, technology and other issues. Edited excerpts follow.

Bill Scaldaferri

ALLIANZ GLOBAL CORPORATE & SPECIALTY

Q Where are the growth opportunities in today's market?

A You talk about growth, growth opportunities, technology. I think everything is coming down to innovation. Tech, data, the doing your day-to-day differently. As an example, bridging the gap between capital markets and insurance — that is what we do ... Providing cyber insurance, it's what we do, but we're doing new things in those spaces. So, innovation there, as an example, is not based on technology, necessarily, but we're doing new things in that area.

And then I would also include culture, because I believe you can do these different things, different deals, executing different transactions that are innovative. But if you don't have the culture of innovation, those will be one-offs and you won't become a truly innovative entity.

If you develop that innovative culture, I think you also start to address the needs of attracting, retaining and developing the proper talent. So when I think of innovation, it goes from the obvious, which is technology, but also to the day-to-day doing what you do but doing it in a new and market-moving way, being first to market in a certain number of elements, and then also addressing the talent issue.

Q As you adopt new data and technology, does that then require a new layer of talent to manage, implement and drive?

A Yes. It's interesting. What do we do with that data? If previously I said you were underwriting a risk based on 10 points of data, now you're underwriting a risk based on 100 points of data. I've given you 90 new points of data. What do you do with it?

We have to make sure we're building the skill set not only to access those additional 90 points but also to know what to do with that information. So from an evolution of the underwriting role, I believe we're going to see the necessity to think more from a portfolio standpoint and more from a data scientist standpoint.

Q Could this lead to a different mix of employees — more data professionals and fewer traditional underwriters?

A I think, frankly, it's a bit of both. I think the reality is going to be that qualifications for a role are going to evolve, and this isn't going to happen from one day to the next. It's going to happen over a multiyear period, and it's going to be an evolutionary process as opposed to revolutionary.

I think that allows the current underwriting group to evolve, but we're also going to bring in new talent. And I think by bringing in new talent, we're going to start to look for new and different types of skills, and I think between those two you're going to have a very interesting balance.

students could potentially work their way into becoming a cyber underwriter?"

You still recruit the economics majors and finance majors, accounting. That doesn't stop. You need those skills, but we need to start looking at people that can think of risks from a different angle. So if you're learning about cyber security in college, you're learning it from a very different angle than those who have learned it from a purely underwriting standpoint or an insurance company role.

Q Is third-party capital really "alternative" anymore? Or has it crossed that threshold?

A We believe that capital market investors — as an example, pension funds — now look at insurance as a true asset class. If it's reached that level, I don't think it's actually still "alternative" anymore.

Working with capital market investors for over a decade led us to a unique, first-to-market offering last year called Alternus. We partnered with Marsh (L.L.C.) and Nephila (Capital Ltd.) to offer a solution to corporate property customers with natural peril exposures. AGCS writes a 10% share of the shared and layered corporate property business of Marsh and cedes the natural peril component to the capital markets. This allows each risk-assuming party to keep the risk profile in which they are interested.



Q Is recruiting and attracting talent a challenge?

A I think it's fair to say insurance is not a dominant major in colleges and universities. So if you're facing that situation, that this is not a driving major in universities, how do you then count on that system to deliver to you the next generation of talent?

So what we've done proactively now is working on internships. We're working with some local universities developing an internship on the cyber space. There are some schools that now have a new major which is homeland security and cyber security.

We thought, "Wouldn't it be interesting to start bringing in some of these cyber security students into internships to see how those skills are being developed at the collegiate level and how these

Q What has occupied most of your time during this first year in this role?

A The first thing that popped into my head was culture, because I think we are an industry that is in the middle of a significant change. And when you think about the change that technology and data are bringing to this industry, I think in order to be successful you have to have the right culture because you must innovate. Again, not just by technology and data but also in how you execute your normal daily business in new and innovative ways.

You have to have a culture that is either like-minded or amenable to these types of changes. In order to get to that next-generation insurance company, we have to evolve into that, and you cannot evolve into that just by osmosis. You have to make a proactive effort to do that.

When you think about the change that technology and data are bringing to this industry, I think in order to be successful you have to have the right culture because you must innovate.



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COVER STORY

CONNECTED WORLD CREATES COVERAGE CONUNDRUM

Conventional insurance policies fall short when applied to exposures presented by internet of things

BY JUDY GREENWALD

judygreenwald@businessinsurance.com

The “internet of things” — the concept of connecting a device to the internet — and its potential for disaster are growing concerns for risk managers and insurers because the devices are increasingly embedded in infrastructure projects.

Often associated with devices used to build “smart homes” by connecting appliances, entertainment systems, communications systems, fitness devices and other consumer goods, the internet of things also has wide, and not always secure, applications in industry.

There is greater risk of bodily injury and property damage with internet-connected devices used in critical functions in the power grid, for example, including nuclear plants; marine; transportation, including aircraft and self-driving cars; and even in the development of so-called “smart cities” that apply a variety of digital and electronic technologies.

The potential source of that danger includes nation-states, criminal hackers and disgruntled employees, although nation-states may pose the greatest risk, observers say.

Recent examples of the infrastructure’s vulnerability include hackers’ exploitation of a fault last year in the technology of Ruel-Malmaison, France-based utility Schneider Electric S.E., which halted operations at an undisclosed industrial facility. In addition, several cyber attacks on Ukraine’s power grid since 2015 have been attributed to Russia.

Some observers believe the problem lies in historic lack of regard for security and the greater focus instead on the devices’ economic benefits.

The insurance industry, which can play a critical role in this area, is beginning to address internet of things exposures through its coverages, increasingly in the form of hybrid policies that contain elements of cyber, property and casualty coverage.

But while many internet of things risks are being addressed by regulators, such as the U.S. Department of Defense, that oversee their contractors, “for a lot of companies, there’s not really currently an incentive for them to build security by design into new devices,” said John P. Carlin, a partner with Morrison Foerster L.L.P. in Washington and former assistant attorney general for the U.S. Department of Justice’s national security division.

MILESTONES IN INTERNET OF THINGS DEVELOPMENT

1964	Teletypewriter allows deaf people to use the telephone by converting tones into electrical signals so that the text could be printed out
1972	Electric meter transfers energy consumption information via telephone
1974	First scanner transmits price from barcode on a pack of gum
1982	Carnegie Mellon’s computer science department uses the internet to track how many soda bottles are in a vending machine
1990	Internet conference features a toaster being turned on and off via commands sent over the internet
1999	Massachusetts Institute of Technology creates the term “internet of things” to describe technology that uses electronic tags for tracking specific objects and transmits that information using the internet, allowing for greater accuracy in tracking the distribution of goods
2008	Standardization organizations start the process of creating specifications for internet of things technology used to manage machines remotely (over networks)
2009	A turning point is reached in internet of things adoption as more internet-connected devices are in existence than people on Earth

Source: GAO

More can be done on that front by either the government or by industries agreeing to voluntary standards, he said.

Commercial policyholders are increasingly aware of the issue, said Adam Cottini, managing director of insurance and risk management in North America at Arthur J. Gallagher & Co. in New York. But, he added, “I believe they’re still trying to get their handle” on it.

In some cases, it may be a budgetary issue, Mr. Cottini said. There may be a combination of vulnerabilities that exist, “but they must deploy resources to stay on top of them,” he said.

The issue has led to an unsettled situation with respect to insurance, say observers.

Insurers are trying to figure out where the peril should be placed, said Gary Gresham, Tampa, Florida-based senior vice president with Aon Risk Solutions’

power practice.

“If there’s a property damage issue, should it be under the property policy or should it be under cyber?” he said. “Right now, the insurance market really hasn’t solidified.”

While FM Global offers property coverage with no cyber exclusions, including internet of things-related risks, “I see insurers responding to cyber risk in a very segmented way, meaning cyber policies are very cyber focused” and only look at digital assets protection and associated business interruption, said Grace Ries, the insurer’s president of cyber underwriting in Johnston, Rhode Island.

Similarly, property insurers only look at traditional perils, she said. “We need to start offering our clients more combined solutions, where they can have comprehensive solutions to address their property

risk and cyber risks all in one,” she said.

“Many markets are unclear both with clients and with themselves as to how coverage may respond,” said Marcin Weryk, New York-based vice president and underwriting manager at XL Group Ltd., which does business as XL Catlin.

Underwriters with an extensive knowledge base of property/casualty need to collaborate with underwriters who understand network connectivity and risk, Mr. Weryk said.

“It’s a very interesting proposition in the cyber world right now” because “companies may have coverage gaps when it comes to property damage and bodily injury caused by a cyber attack or cyber peril,” said Michael Born, Kansas City, Missouri-based vice president of the global technology and privacy practice at Lockton Cos. L.L.C.

Organizations should be looking at the issue holistically, said Joe DePaul, New York-based head of FINEX cyber/E&O for North America at Willis Towers Watson P.L.C.

“It is a combination of various different coverages really making up the solution that we’re currently talking about,” which could include property/casualty, cyber and directors and officers liability, he said.

This is beginning to be addressed, say observers. Cyber insurance traditionally has dealt with the monetary damages that could arise from a security breach, Mr. Born said. But “there is a movement now to add bodily injury and property damage to the cyber policies,” he said.

“This is a leading edge of what we think of as cyber insurance right now,” said Mr. Born.

Mr. Weryk said, “There are special products being developed by many under-

See IOT next page

SMART DEVICES ENHANCE CONTROL SYSTEMS, MULTIPLY RISKS

The growing deployment of internet-connected devices into “the infrastructure” may prove to be volatile.

While there is no set definition of the infrastructure, it can be described as society’s basic physical and organizational structures, including utilities, transportation systems, dams, sewage treatment plants and even traffic control.

Devices connected through the “internet of things” are increasingly being used to help operate these complex entities.

The technology will tell a utility’s engineers, for instance, that its water level is too high or too low, or that a smelting processes’s temperature is over its limit and its furnace must be shut off, said Scott Corzine, New York-based senior managing director at Ankura Consulting Group L.L.C., a cyber security consulting firm.

Every internet of things device, whether it is a webcam, a thermometer or another connection, adds an additional



entry point into a network, said Gerry Kane, Schaumburg, Illinois-based cyber risk engineer for Zurich North America. “They’re all just like a computer on a regular network,” he said.

Smart devices that can be hooked up to industry control systems “can be potentially harmful if somebody can get access to those devices and then control

access” to the systems, said Adam Cottini, managing director of insurance and risk management in North America at Arthur J. Gallagher & Co. in New York

“The biggest challenges with IoT devices is they’re so easy to deploy, and they’re just exploding in their ability to transfer data from the devices that historically have not been smart,” said Wade Chmielinski,

Norwood-Massachusetts based assistant vice president of cyber security at FM Global. Historically, however, the devices were not developed with security in mind.

“They can wreak havoc at a level potentially more damaging to society than just the inconvenience of stealing your credit cards,” said Mr. Corzine. “If you can hack one of these machines, you can black out” a city or country, he said.

Mr. Corzine said he believes the most serious danger is from nation-states and potentially well-funded terrorist groups that have the wherewithal to launch such attacks and are uninterested, in this context, in financial gains.

These are well-funded nation-states and terrorist groups “that have enough funding to bring smart guys onto the scene,” and have the same impact warfare once did without “dropping a bomb or shooting a bullet.”

Judy Greenwald

COVER STORY

IOT

Continued from previous page

writing companies” that clearly delineate where coverage may lie if an event occurred because of a network hack that has caused property, bodily injury or third-party loss.

“I think the marketplace will keep moving in that direction, where there is more dedicated product,” he said.

“I can see some gradual progress” toward comprehensive solutions, said Ms. Ries.

Mr. Born said while “the insurance business is beginning to respond to this peril, and to the exposure,” where “that coverage is ultimately going to lead is still up in the air.”

“In my opinion, it still primarily belongs in the cyber policy” rather than in property or commercial general liability policies,” Mr. Born said. “It’s probably more important to understand the threats and the risks and the chances of something going wrong than to understand the damages if something does go wrong.”

Cyber exposures are evolving from being an information technology department issue to an enterprisewide concern.

SECURITY AN AFTERTHOUGHT IN INTERNET OF THINGS DESIGN

Many devices connected through the “internet of things” are not secure simply because they were not designed with security in mind, say experts.

The internet of things was designed “without any real attention to security, which is the same thing we did with the internet 30 years ago,” said Larry Clinton, president and CEO of the Arlington, Virginia-based Internet Security Alliance trade association.

“Much of the world’s infrastructure is built on older, less secure operating

systems and models,” said Marcin Weryk, New York-based vice president and underwriting manager at XL Group Ltd., which does business as XL Catlin. Their interconnectedness “was just a piece of hardware that people didn’t think about,” he said.

“The whole point is that IOT risks weren’t really understood until millions of IOT devices were already fielded ... and, in many cases, we’ve allowed these to become part of our networks,” said Alan Brill, senior managing director at Kroll

Associates Inc. in Secaucus, New Jersey.

Economics, not security, has been the main driving force, say experts.

“The main driver for the IOT is the enormous economic benefits that it can drive for corporations and consumers,” Mr. Clinton said. “But the economics mitigate against embedding adequate security in many of these devices, and as result, the widespread deployment of these devices could dramatically increase the overall vulnerability of the system.”

Judy Greenwald

“The history of cyber security has been almost solely focused on IT operations, and not as an enterprisewide issue,” said Larry Clinton, president and CEO of the Arlington, Virginia-based trade association Internet Security Alliance.

But insurers tend to look at issues, including cyber, much more from an enterprisewide perspective, which is critical.

“The insurers have really been leaders in that regard,” said Mr. Clinton.

However, “If there’s a true catastrophe,

there might be enough insurance, but I don’t know if enough people are buying it,” said Bob Parisi, New York-based cyber product leader for Marsh L.L.C.

“People really need to take a fresh look at that piece of the puzzle,” not just the firewalls in their computer systems but the devices their networks are controlling, said Mr. Born.

The first step is for entities to understand their environment in conjunction with “what’s out there in the field,” said Scott

Corzine, New York-based senior managing director at Ankura Consulting Group L.L.C., a cyber security consulting firm.

“They have to get a handle on all that, and then they have to create a strategy for security of those industrial control devices,” he said.

“We need to design an overarching cyber security plan. We’re not doing this right now,” said Mr. Clinton. “Right now, the way to deal with cyber security is incremental.”

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MANAGEMENT LIABILITY

#MeToo prompts corporations to look within

BY JUDY GREENWALD

judygreenwald@businessinsurance.com

INSIDE

HARASSMENT CLAIMS

Accusations against high-profile personalities have turned a focus on D&O liability insurance. **PAGE 25**

CYBER SECURITY

Cyber exposure is a rapidly emerging issue, although D&O claims have been largely unsuccessful. **PAGE 26**

MED MAL MARKET

The medical professional liability market remains soft, with consolidation keeping rates flat. **PAGE 27**

The “#MeToo” movement — the deluge of accusations by women charging sexual harassment that was sparked by the controversy surrounding former Miramax L.L.C. co-founder Harvey Weinstein — is likely to confront employers indefinitely.

It is already encouraging underwriters to more closely scrutinize employment practices liability coverage resulting in reduced capacity in entertainment-related accounts, though to what degree claims will increase is still unclear.

Further intensifying scrutiny on the issue was the January sentencing of former USA Gymnastics team physician Dr. Larry Nassar for up to 175 years in prison for the sexual abuse of female gymnasts and other student athletes.

While sexual harassment charges are

most likely to affect employers’ employment practices liability coverage, they may also affect companies’ directors and officers liability policies (see related story).

To avoid litigation, experts say employers should take a fresh look at their harassment policies and avoid a “check-the-box” mentality in addressing these issues (see box).

Charges against Mr. Weinstein have led to many more, particularly against prominent entertainment, journalism and the media figures, with no immediate signs

of abatement. And executives and well-known figures in other sectors also face accusations.

The movement is not a flash in the pan, say experts.

"It's so high-profile, with some famous people — I think it will trickle down and embolden people to bring more claims" as time goes by, said Tom Hams, Chicago-based managing director and national employment practices liability insurance practice leader at Aon Risk Solutions.

It has led to a "closer look at corporate culture and how it impacts corporate behavior," said Talene Megerian, New York-based national employment practices liability leader in Willis Towers Watson P.L.C.'s FINEX North America practice. "This is where we're going to see the real change."

"There's going to be greater scrutiny at renewal around what the company has done to ... prevent those claims from happening. (Companies) need to articulate to underwriters how they are better than their peers."

Kelly Thorig,
Marsh L.L.C.

HARASSMENT CLAIMS HIT D&O LIABILITY INSURANCE

While employment practices liability insurance is the primary focus of claims in connection with the "#MeToo" movement against sexual harassment, directors and officers liability insurance is being affected as well.

Observers point to the \$90 million settlement of shareholder claims reached in November last year by New York-based Twenty-First Century Fox Inc. arising from the sexual harassment claims at its Fox News Channel against Roger Ailes and Bill O'Reilly.

The Weinstein Co., based in New York, has been named as defendant in litigation filed against former film mogul Harvey Weinstein, while Wynn Resorts Ltd. has been sued by shareholders in connection with sexual harassment charges made against founder and former Chief Executive Steve Wynn.

In general, plaintiffs allege that company boards did nothing to remedy long-standing problems and the subsequent publicity has resulted in a diminution of shareholder value, said Kelly Thorig, Richmond, Virginia-based U.S. employment practices liability product leader for Marsh L.L.C.

"There's definitely a dynamic here that's going to continue to be a part of D&O liability issues," said Rob Yel-



REUTERS

Demonstrators called for the firing of Fox News Channel TV anchor Bill O'Reilly in New York City in April 2017. Fox News fired Mr. O'Reilly that month after five settlements related to harassment allegations against him were disclosed.

len, New York-based executive vice president of Willis Towers Watson P.L.C.'s FINEX North America practice, although not all cases affect people at the top level or firms' securities.

"I think there'll be not only more high-profile revelations, but we'll see

examples of investors and other stakeholders seeking to hold the directors and officers accountable following misconduct," said Kevin LaCroix, executive vice president of RT ProExec, a division of R-T Specialty L.L.C., in Beachwood, Ohio.

Judy Greenwald

The issue has already affected entertainment-related accounts, said Paul Nash, Beazley P.L.C.'s London-based EPL focus group leader, who said the insurer avoids writing in the sector. "We're definitely seeing a shrinkage of capacity in that industry for EPL," with some insurers cutting limits or introducing higher retentions, he said.

Marie-France Gelot, New York-based senior vice president and insurance claims counsel for Lockton Cos. L.L.C., who has seen an uptick in sexual harassment claims, particularly in the Bermuda market, said clients have "sought to increase their policy limits, starting with the January renewals."

"I think the entire market is still holding its breath, so to speak, as to how things play out," she said.

"It is too early to tell what the impact will be either on the frequency of sexual harassment claims or, indeed, the impact on severity of sexual harassment claims," Mr. Nash of Beazley said.

"Let's just see how it pans out," he said, adding the most egregious claims that have arisen in this context are not only sexual harassment but sexual assault, which involves bodily injury and "is different from a straightforward sexual harassment claim." Employers may also be affected by wrongful hiring theories, he said.

"If there will be a massive increase in (sexual harassment) claims, I don't think

that it's here yet," said Michael Schraer, senior vice president of EPL and non-profit product manager at Chubb Ltd. in Whitehouse Station, New Jersey.

"I don't think it will have any long-term impact on pricing, because it's so unique in terms of the exposure to certain industries," Mr. Hams of Aon said.

The harassment issue has changed the insurance market's perspective in terms of how it evaluates the risk, though, said Ms. Megerian of Willis Towers Watson.

Underwriters are "certainly taking a closer look at company's policies and procedures" and at their training and at how these policies are implemented "because what they really want to get at is companies' corporate culture and ... dig deep into the policies they have in place," she said.

There are also starting to be more face-to-face interviews with the C-suite so underwriters can better evaluate the risk, she said.

"There's going to be greater scrutiny at renewal around what the company has done to ... prevent those claims from happening," said Kelly Thorig, Richmond, Virginia-based U.S. employment practices liability product leader for Marsh L.L.C.

Companies "need to be able to articulate to underwriters how they are better than their peers" and, if they have had claims in the past, "what they've done to improve their process," she said.

Natalie Douglass, senior managing director, management liability practice for Arthur J. Gallagher & Co. in St. Louis, said while coverage is widely available, "whether (policyholders) buy adequate limits, that's always the million-dollar question."

"We evaluate each client's risk and make our own recommendations," but obtaining the coverage is often based on other factors, and firms decide to self-insure in some cases, Ms. Douglass said.

One possible issue that could arise is that some charges are being made in connection with occurrences of many years ago and may not be actionable, said Mr. Hams.

There might be policy provisions with regard to late notice, or prior acts exclusions that bar coverage, so it is important for companies to review policy terms, Ms. Douglass said.

Meanwhile, "it is more challenging" now to settle claims that were already filed, said Mr. Schraer.

"Plaintiffs are a little more emboldened now," which is creating a different negotiating environment that could lead plaintiffs to litigate instead of settling, said Ms. Megerian.

In addition, some plaintiffs who had previously settled are now seeking to reopen their cases, said Brian Zink, New York-based senior vice president and head of corporate management solutions at Zurich North America.



MITIGATION CHECKLIST

To reduce the chances of sexual harassment claims, experts recommend that employers:

- ✓ Introduce policies and procedures that call for zero tolerance
- ✓ Be sure sexual harassment policies are up-to-date
- ✓ Distribute policies to all employees, including the C-suite
- ✓ Require effective, not just "check-the-box," training
- ✓ Introduce an employee complaint hot line
- ✓ Have risk management, legal and human resources departments collaborate
- ✓ Work with quality insurance and legal firms
- ✓ Improve investigative protocols
- ✓ Produce tangible documentation on actions taken
- ✓ Buy adequate employment practices liability insurance limits

Cyber exposure risk works its way to C-suite

BY JUDY GREENWALD

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Cyber-related claims against directors and officers have been largely unsuccessful to date, but given the plaintiff bar's creativity and persistence, it is too soon for companies to relax and consider themselves off the hook, say experts.

Cyber D&O cases have generally been dismissed on the basis the breaches have not caused companies any material harm. But plaintiff law firms continue their efforts, and market participants say it is premature to dismiss them as a threat.

While a cyber policy is the most likely coverage for a cyber breach, corporate directors and officers have also been targeted in litigation.

"A cyber event could potentially trigger two policies," but in different ways, said Adam Cottini, managing director of insurance and risk management in North America at Arthur J. Gallagher & Co. in New York.

Cyber policies are "clearly responding to a failure to protect a computer system," while D&O policies reflect an operational concern on the management liability side, said Mr. Cottini.

Cyber exposure is "absolutely" an emerging issue in terms of D&O exposure, said Chris Rafferty, Chicago-based managing director with Aon's Aon Risk Solutions' financial services group.

"Five years ago, D&O underwriters would often ask the question of insureds, 'How are your cyber security procedures?' and insureds could provide a fairly abbreviated, simplistic answer, and underwriters would check the box and move on."

Now, though, there is "a growing wariness by D&O underwriters" of the cyber issue, he said. They are exploring firms' enterprise risk management, including cyber security, much more carefully.

Some experts said they had expected more such suits.

"I thought we'd see a lot more cyber-related D&O litigation," said Kevin



REUTERS

Richard Smith, former chairman and CEO of Equifax Inc., testified on Capitol Hill last year. The company faces securities class action litigation related to a massive data breach.

LaCroix, executive vice president of RT ProExec, a division of R-T Specialty L.L.C., in Beachwood, Ohio, adding he was surprised "we haven't seen more." He said part of the reason is "several high-profile cases" in 2014 and 2015 "didn't go far" and resulted in dismissals.

"We have seen a bounce-back" on stock prices, said Mr. Cottini. When an event happens, there may be an initial downturn, but they have not been sustainable, and there is no long-term impact on shareholder value, he said.

However, "It's always risky to underestimate the creativity of the plaintiffs bar," said William Boeck, senior vice president at Lockton Cos. L.L.C. in Kansas City, Missouri. "They are continuing to bring lawsuits, primarily shareholder derivative lawsuits, and they are learning from past decisions," he said.

"I expect they'll eventually succeed," but "maybe not across the board" he said. A favorable ruling "may not open the floodgates, but if they find a way to plead the allegations in the complaint in a way that prevents courts from dismissing them, that

is likely to generate interest in bringing more suits," Mr. Boeck said.

Mr. LaCroix said while earlier cases that were dismissed were shareholder derivative lawsuits, cyber-related securities class action lawsuits filed last year against Sunnyvale, California-based Yahoo Inc., Atlanta-based Equifax Inc. and San Jose, California-based PayPal Holdings Inc. are taking a different approach.

In both the Yahoo and Equifax lawsuits, "the plaintiff lawyers are trying to capitalize on the delay between the discovery of the breach and the disclosure," he said.

There has also been the issue of Equifax executives who sold company stock during this period. Equifax said in a statement that none of the executives had been aware of the breach when their trades were made.

"I think the Equifax lawsuit will be particularly interesting to watch, because I think the potential for plaintiff attorneys to be able to exploit this as a new product line, so to speak, might turn on their ability to show the delay harmed investors," said Mr. LaCroix.

D&O underwriters are aware of the issue.

CYBER SUITS

Litigation against directors and officers in response to cyber breach cases, though largely unsuccessful to date, has attracted regulatory attention. Significant legal developments include:

- The **2014** dismissal of derivative litigation filed by shareholders against Parsippany, New Jersey-based Wyndham Worldwide Corp. in connection with three cyber breaches.
- The **2016** dismissal of a shareholder derivative lawsuit filed in connection with Minneapolis-based Target Corp.'s 2013 cyber breach.
- Although initially dismissed, while on appeal The Home Depot Inc., based in Atlanta, reached a settlement in **April 2017** of derivative litigation filed by shareholders in response to the retailer's 2014 data breach, under which plaintiff attorneys would receive up to \$1.1 million.
- Securities class action litigation was filed: In **September 2017** against Atlanta-based Equifax Inc. in connection with its massive data breach; in December 2017 against San Jose-based PayPal Holdings Inc. in connection with data security issues at a bill pay management company it has acquired; and in January 2018 against Sunnyvale, California-based Yahoo! Inc.
- The New York State Department of Financial Service's Cybersecurity Requirements for Financial Services Companies regulation, which was finalized in **March 2017**, requires regulated companies to implement controls to ensure a robust cyber security program. Covered Entities were required to submit the first certification under the regulation by Feb. 15.
- The U.S. Securities and Exchange Commission's Office of Compliance Inspections and Examinations listed cyber security as among its priorities last month. It also updated its **2011** guidance on public companies' disclosure of cyber security risks and breaches, stating cybersecurity is critical to companies' operations.

"It's already started to impact the questions that are being asked at the underwriting stage," said Sarah Downey, New York-based FINPRO and D&O product leader for Marsh USA Inc.

Mr. Rafferty noted that in its dismissal of the D&O suit filed by shareholders against Parsippany, New Jersey-based Wyndham Worldwide Corp. in 2014, the U.S. District Court in Newark, New Jersey, said the company had taken prudent steps with regard to cyber security and had discussed the issue during multiple board meetings.

Mr. Rafferty said if a board can establish in the context of a D&O claim that it was diligent about assessing risk, tested its vulnerabilities, quantified and mitigated the risk, insured it to the extent feasible, had a post-breach response plan in place and relied on qualified consultants and counsel, "it's going to be that much more difficult" for plaintiff firms to successfully file a lawsuit that survives a motion to dismiss.

CLASSIFIED

REQUEST FOR PROPOSAL



Bridge & Excess Liability Insurance Broker
The Delaware River Port Authority (DRPA) is requesting a Technical Proposal and a Price Proposal for Broker/Consultant Services for Bridge Property & Excess Liability. Interested parties can find the Request for Proposal documents by going to the DRPA website www.drpa.org, clicking on the "Working with DRPA" link, and clicking on "Bids and Contracts".

REQUEST FOR PROPOSAL



Traditional & Casualty Insurance Broker
The Delaware River Port Authority (DRPA) is requesting a Technical Proposal and a Price Proposal for Broker/Consultant Services for Traditional Property & Casualty Insurance and Pollution Legal Liability. Interested parties can find the Request for Proposal documents by going to the DRPA website www.drpa.org, clicking on the "Working with DRPA" link, and clicking on "Bids and Contracts".

REQUEST FOR PROPOSAL



Health & Welfare Benefits Broker
The Delaware River Port Authority (DRPA) is requesting Proposals for Health & Welfare Benefits Broker/Consultant Services. Interested parties can find the Request for Proposal documents by going to the DRPA web site www.drpa.org, clicking on the "Working with DRPA" link, and then clicking on "Bids and Contracts".

Health care deals help keep med mal rates flat

BY MARK A. HOFMANN

It's steady as she goes for the medical professional liability insurance market.

That's despite the efforts of underwriters to achieve some rate increases in a marketplace that's been soft for more than a decade. Where increases can be implemented, they tend to be in the low single digits.

Part of the reason for the flatness in the market is the ongoing consolidation of the health care industry. Larger hospitals acquire smaller ones, and independent health care professionals leave private practice to become employees of the larger institutions. Insurers must compete with one another for a piece of a smaller market.

"What we're seeing in overall med mal is continued consolidation: mergers and acquisitions and also unique affiliations, as the fee-for-service model transitions to a population health model," said Chris Heckman, vice president of underwriting for health care at Chicago-based CNA Financial Corp. "We are studying the impact that employed physicians have on claims and the marketplace. It's much less common to see independent physicians today."

At the same time, new exposures such as



those presented by telemedicine create both opportunities and challenges for underwriters. They have to settle issues of how and whether policies will respond to new exposures created by cyber issues as well.

Randall Nukk, area president and managing director of the health care practice with Arthur J. Gallagher & Co. in Rolling Meadows, Illinois, said that on the physician side of the market, "in the late fall, the

national players all started talking about how they wanted to see more bottoming out. Nobody's talking about dramatic changes. It's been soft for 15 years. The average doc is paying half of what they did 15 years ago. Accident year combined ratios are almost uniformly over 100%. Reserve releases from prior years are beginning to evaporate."

Mr. Nukk said that on the hospital side,

conditions vary. "For small institutions, the market is still pretty soft."

"I think results were mixed, flat to somewhat up," said Martha Jacobs, national health care industry practice leader for Aon Risk Solutions in Pittsburgh.

She said some insurers wanted higher rates, with a few "pushing for some hard-market pricing and conditions. But there was nothing systemic across the book, overall results were flat with some pockets of upward pressures."

Through the third quarter, "we had a very good combination of renewal retention and rates," said Howard H. Friedman, chief actuary and president of the Healthcare Professional Liability Group at ProAssurance Corp. in Birmingham, Alabama. He said that renewal retention was over 90% and rates increased about 1%, "which was a favorable change over what we've seen over the past few years."

Another underwriter also expressed optimism.

"We were really pleased to achieve meaningful rate and improved terms and conditions for those areas that need it the

See **MEDICAL** page 29



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SPECIAL REPORT

LARGEST D&O INSURERS

Ranked by direct premiums written through the third quarter of 2017, in millions of dollars

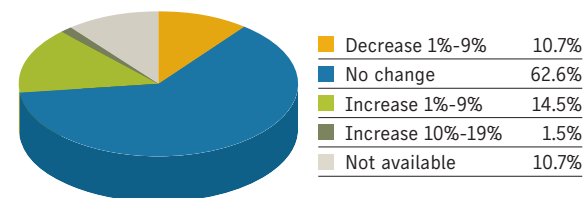
2017	2016	Insurer	Direct premiums written	Percent increase (decrease) vs. 3Q 2016	Direct incurred losses	Direct loss ratio	Market share
1	1	American International Group Inc.	\$665.2	(7.9%)	\$611.1	84.3%	14.8%
2	2	Chubb Ltd.	\$563.3	(2.5%)	\$260.1	43.1%	12.5%
3	3	XL Group Ltd.	\$439.8	(13.1%)	\$319.3	66.0%	9.8%
4	4	Tokio Marine Kiln Group Ltd.	\$406.9	(0.5%)	\$223.4	53.9%	9.0%
5	5	CNA Financial Corp.	\$281.8	(1.8%)	\$142.3	49.6%	6.3%
6	6	Travelers Cos. Inc.	\$221.1	(0.3%)	\$110.4	48.6%	4.9%
7	7	American Financial Group Inc.	\$188.4	7.5%	\$71.7	39.3%	4.2%
8	14	Zurich Insurance Group Ltd.	\$154.6	65.9%	\$218.1	138.2%	3.4%
9	13	Liberty Mutual Holding Co. Inc.	\$119.7	26.9%	\$30.3	16.1%	2.7%
10	8	Alleghany Corp.	\$113.9	(6.4%)	\$28.6	24.6%	2.5%
11	N/A	Sompo Holdings Inc.	\$108.1	N/A	\$63.6	54.6%	2.4%
12	10	W.R. Berkley Corp.	\$101.9	(3.7%)	\$64.8	60.2%	2.3%
13	12	Berkshire Hathaway Inc.	\$101.4	2.9%	\$56.0	56.6%	2.3%
14	30	Fairfax Financial Holdings Ltd.	\$97.0	407.9%	\$65.0	62.6%	2.2%
15	15	Axis Capital Holdings Ltd.	\$86.8	(5.0%)	\$46.0	46.6%	1.9%
16	27	Nationwide Mutual Group	\$84.0	252.9%	\$45.6	50.8%	1.9%
17	18	Arch Capital Group Ltd.	\$83.3	6.5%	\$27.9	30.4%	1.9%
18	19	Old Republic International Corp.	\$62.4	6.8%	\$48.2	79.1%	1.4%
19	21	ICI Mutual Insurance Co.	\$54.4	(5.4%)	\$4.2	7.4%	1.2%
20	20	Everest Re Group Ltd.	\$51.2	(12.0%)	\$26.9	55.9%	1.1%
Top 20 total			\$3,985.2	(1.8%)	\$2,463.5	58%	89%
Industry total			\$4,500.4	(1.3%)	\$2,705.0	57%	100%

N/A = Not available

Source: S&P Global Market Intelligence, based on National Association of Insurance Commissioners statutory P/C statement filings

D&O PRICING

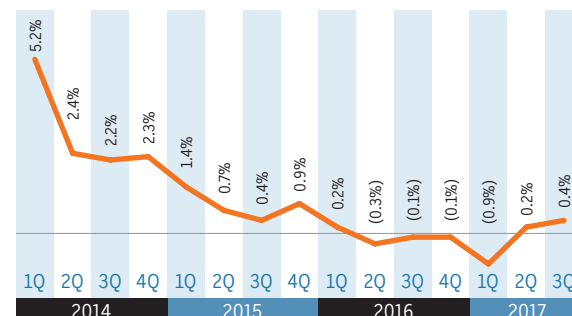
Of survey respondents, 73.3% saw no change or a decrease in premium rates for directors and officers liability coverage during the third quarter of 2017.



Source: Council of Insurance Agents & Brokers

RENEWAL PRICING

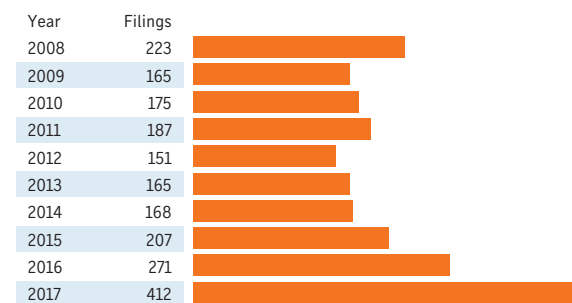
Average D&O renewal pricing changes by quarter since 2014



Source: Council of Insurance Agents & Brokers

CLASS ACTIONS

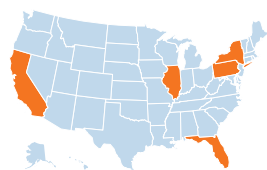
The number of 2017 federal class action filings jumped to 412 cases, a record for the second consecutive year.



Source: Cornerstone Research Inc.

TOP STATES

States with the most direct premiums written for medical professional liability insurance in 2016

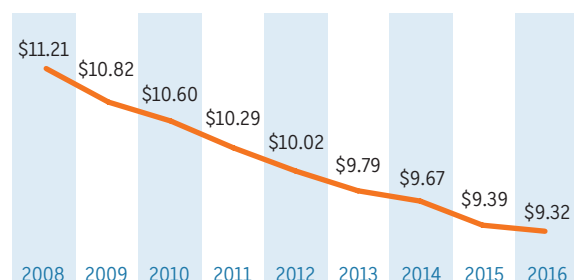


State	Direct premiums written	Number of insurers
New York	\$1,629,216,038	130
California	\$756,983,318	133
Pennsylvania	\$684,053,209	147
Florida	\$594,567,473	131
Illinois	\$474,201,263	132

Source: National Association of Insurance Commissioners

PROFESSIONAL LIABILITY COVER

Direct premiums written for U.S. medical professional liability insurance, 2008-2016, in billions of dollars



Source: National Association of Insurance Commissioners

LARGEST MEDICAL PROFESSIONAL LIABILITY INSURERS

Ranked by direct premiums written through the third quarter of 2017, in millions of dollars

2017	2016	Insurer	Direct premiums written	Percent increase (decrease) vs. 3Q 2016	Physicians	Hospitals	Other health care professionals	Other health care facilities
1	1	Berkshire Hathaway Inc.	\$841.9	0.7%	\$548.1	\$71.2	\$126.0	\$96.6
2	2	The Doctors Co.	\$539.7	0%	\$499.9	\$3.4	\$17.8	\$18.6
3	3	Medical Liability Mutual Insurance Co.	\$402.7	3.7%	\$370.9	\$21.6	\$10.2	—
4	5	ProAssurance Corp.	\$371.6	4.8%	\$259.2	\$24.3	\$80.9	\$7.1
5	4	CNA Financial Corp.	\$369.2	0.5%	\$41.7	\$69.7	\$188.7	\$69.2
6	6	Coverys Insurance Group	\$322.3	6.7%	\$240.9	\$42.6	\$11.6	\$27.1
7	7	MCIC Vermont Inc.	\$292.6	4.8%	N/A	\$292.6	N/A	N/A
8	9	NORCAL Mutual Insurance Co.	\$271.5	9.7%	\$266.3	\$0.2	\$2.2	\$2.7
9	11	MAG Mutual Insurance Co.	\$195.9	8.2%	\$178.2	\$15.2	N/A	\$2.5
10	10	Hospitals Insurance Co.	\$174.2	(6.7%)	\$107.6	\$66.6	—	—
Top 10 total			\$3,781.7	1.6%	\$2,512.8	\$607.5	\$437.4	\$223.9
Industry total			\$7,516.0	(2.8%)	\$4,299.0	\$1,518.5	\$1,013.8	\$684.7

N/A = Not available

Source: S&P Global Market Intelligence, based on National Association of Insurance Commissioners statutory P/C statement filings

MEDICAL

Continued from page 27

most," Mr. Heckman said. "We had a very strong December, and we're encouraged by the results for the beginning of the year."

Carolyn Snow, director of risk management at Humana Inc. in Louisville, Kentucky, said the market "was really very good" for the excess coverage she renewed in January in Bermuda. "We actually had a small decrease," she added.

Capacity is not an issue, said John Geisbush, managing director at Marsh L.L.C. in Phoenix. "We continue to see an abundance of capacity for medical professional," he said. For a good account that is stable in terms of exposure and loss development, rates are "slightly" down, he said, while in general "we saw a range of 5% down to 5% up depending on the specifics of an account and where it was located."

With medical professional coverage, there is variation specifically with respect to jurisdiction, he said. Places such as Cook County, Illinois, Philadelphia County, and South Florida are viewed as difficult jurisdictions because of the tort climate, he added.

Increased attention is being paid to policy language, say observers.

HEALTH CARE TRENDS CHANGE RISKS

Looking ahead, risk managers, brokers and insurers alike see new exposures buffeting the medical professional liability insurance market.

"Telemedicine will create new risks," said Rebecca Cady, vice president and chief risk officer at Children's National Medical Center in Washington. "It will make it easier to spread claims across more players."

There is also the issue of how the internet of things will affect medical devices.

"We're just scratching the surface on that," Ms. Cady said. She added that if she were on the insurer side, "I'd be worried about how would I get roped into a claim that looks like a cyber claim but gets treated as a health professional liability claim."

Cyber is still a "significant issue," said Martha Jacobs, national health care industry practice leader for Aon Risk Solutions in Pittsburgh. People have remote device technology, and there is concern about if those medical devices can be hacked, she said.

The move toward more telemedicine brings in more technology as well.

"Carriers are interested in the levels of telemedicine and how it might be provided," said John Geisbush, managing director at Marsh L.L.C. in Phoenix. "All of us are monitoring the Affordable Care Act and how things may change."

"We are also seeing a rise in the number of medical malpractice cases involving nurse practitioners and physician assistants, collectively known as advanced practice clinicians or APCs," Joanne Gundersen, vice president and medical malpractice lead for QBE North America in Simsbury, Connecticut, said in an email. "The industry is making greater use of APCs to counter the growing physician shortage and manage the cost of care. The increased use adds complexity to liability risks because it triggers a variety of additional issues, such as proper training, certification and supervision. Moreover, rules and regulations governing these issues are constantly evolving and vary by state."

Events with no direct connection to medical malpractice could also affect the marketplace, said Mr. Geisbush, who added that even though the catastrophe property losses of \$100 billion didn't directly affect med mal, those losses could leak into other lines of coverage.

Mark A. Hofmann

"We are seeing increased interest from brokers and insureds for clarity in the contract as well as terms and conditions that are consistent all the way up the program tower," Joanne Gundersen, vice president and medical malpractice lead for QBE North America in Simsbury, Connecticut, said in an email.

While claims frequency has remained stable, severity has been creeping up, noted ProAssurance's Mr. Friedman. "The overall changes in health care over past 10 years, including efforts to contain costs on the part of the payers and consolidation in the hospital business, are having an impact on the market. When physicians become employed by larger groups, claims can get larger as the entities involved in the lawsuits generally have higher limits of insurance available."

Severity is up 3% to 4%, which is about 2% above inflation, Mr. Nukk said.

"In calendar year 2017, there were seven verdicts over \$40 million. The number of verdicts over \$10 million, 38, was the highest over the last 18 years," Ms. Jacobs said.

"Caps on noneconomic damages is an effective means of combating runaway verdicts, but currently only 26 states have noneconomic damage caps for medical malpractice cases," Bridget Zaremba, assistant vice president and health care claims lead for QBE North America in Chicago, said in an email.

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CAPTIVES
REPORT

Captive managers anticipate market changes

INSIDE

TAX REFORM AND CAPTIVES

When created for risk management reasons, captives are unlikely to be hindered by U.S. tax reform. **PAGE 33**

RISK RETENTION GROUP GROWTH

Risk management services and premium stability have helped RRGs capture market share. **PAGE 34**

RANKINGS & DATA

Business Insurance's 2018 rankings of the top captive managers. **PAGE 36**

BY GAVIN SOUTER

gsouter@businessinsurance.com

Global captive formations slipped in 2017 amid the continued soft commercial insurance market, but captive managers anticipate growing interest in alternative risk transfer vehicles as some lines of coverage see rates edge up.

In addition, while traditional captive risks — general liability, auto liability, workers compensation and some property coverages — continue to dominate, other lines, such as medical stop loss coverage, are increasingly being covered via captives, and owners are showing interest in covering cyber liability, operational risks and some parametric coverages through captives, captive managers say.

And recent tax rulings and changes in tax law don't appear to have yet dented

the appeal of captives as risk management tools, they say.

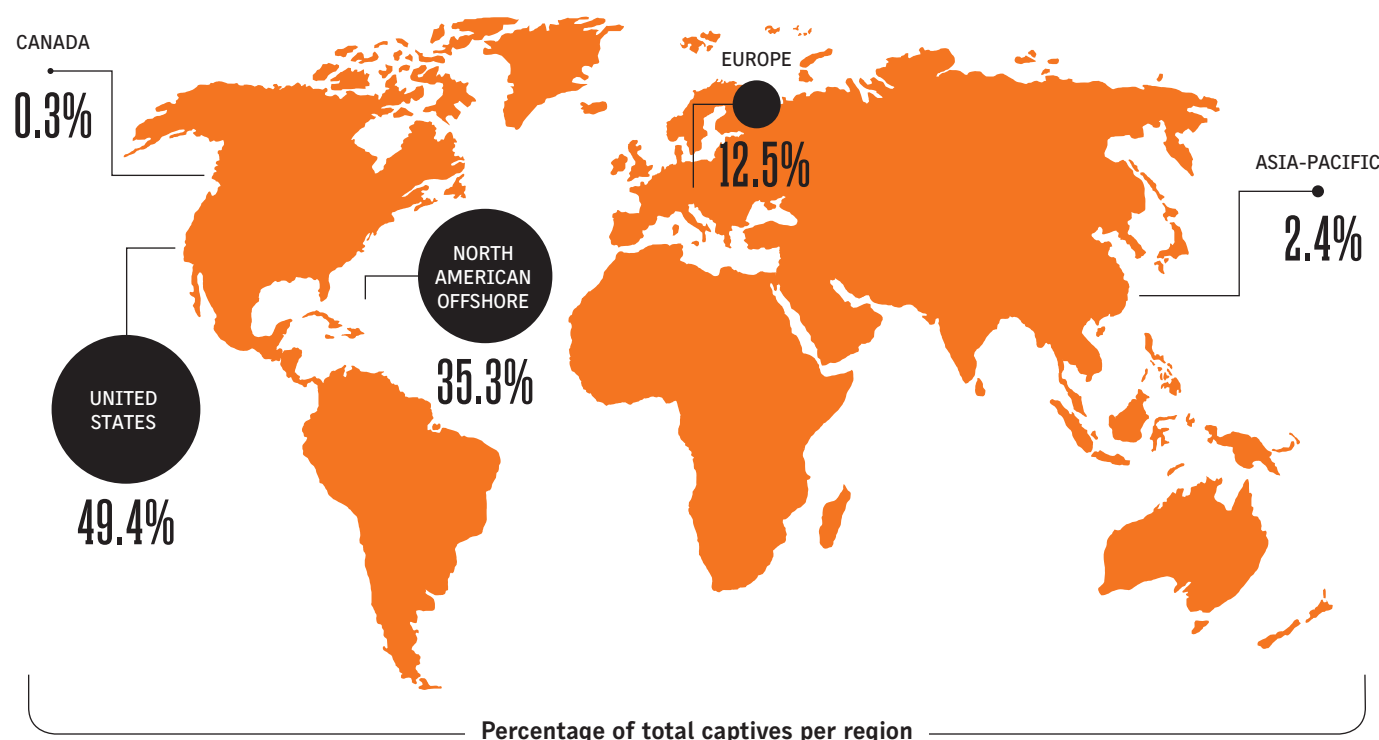
The total number of captives worldwide slipped less than 1% to 6,647 in 2017, according to a *Business Insurance* survey of captive domiciles (see chart, page 36). Domiciles submitted more robust data for the past two years as the most recent survey requested more detail.

Several of the larger, well-established domiciles, including Bermuda, Cayman Islands and Vermont, saw net reductions

ONSHORE/ OFFSHORE BY THE NUMBERS

There were 6,647 captives in 2017, not including microcaptives, series captives or individual cells or cell members in protected cell companies.

Source: BI survey



in the numbers of licensed captives, but smaller, more recently established domiciles, especially in the United States, continued to see growth in captive numbers (see chart, page 33). Tax changes arising from the 2010 Nonadmitted Reinsurance Reform Act, which can make it advantageous for captives to be domiciled in the same state as their parent company, in part continue to drive domestic domicile growth, captive managers say.

Captive opportunities

Looking forward, captive managers expect to see captive owners making more use of existing captives and other companies forming captives if commercial insurance rates rise in 2018.

Following the chain of catastrophe losses in 2017, various market surveys show rate increases of 5% to 10% for property coverages and more modest increases in some other lines of coverage.

“There’s finally a sense that rates are about to rise, and we are seeing captives look at deductibles and exclusions in their existing commercial policies,” said Karl Huish, Phoenix-based executive vice president-North America, at Artex Risk Solutions Inc., the captive management unit of Arthur J. Gallagher & Co.

And economic growth, especially the booming construction sector, is driving captive growth, he said.

“We have construction companies that have very strong cash flow, and they are looking to do medical stop loss, workers compensation deductibles and subcontractor risk in captives. I think construction is an area where we will see growth with captives this year,” Mr. Huish said.

The hardening in the property insurance market is prompting more interest in insuring a portion of named storms cov-



The construction sector and medical stop loss are expected to be growth areas for captive insurers, while cyber and other potential markets are still developing.

erage or wind or earthquake deductibles, which are increasing, in captives, said Indianapolis-based Anne Marie Towle, executive vice president, captive consulting practice leader, at JLT Insurance Management, a unit of Jardine Lloyd Thompson Group P.L.C.

Aon P.L.C.’s captive management business saw a 22% increase in premiums last year through a combination of new formations and existing captive owners utilizing their captives more, said Burlington, Vermont-based Nancy L. Gray, regional managing director, Americas, at Aon Risk Solutions.

“We are seeing increases in the property area and a reflection that captives are being utilized a bit more than they have in the past,” she said.

Captive owners are in some cases increasing retentions from a risk-reward perspective and utilizing their captives to access

the reinsurance market, Ms. Gray said.

New areas

Aside from lines of coverage that have traditionally been placed in captives, captive owners are placing — or at least considering placing — a more diverse range of coverages in captives.

In recent years, for example, more captives are being used to cover medical stop loss exposures, which cap exposures on self-insured health plans, said Ms. Towle.

“A lot of it is driven by the sheer numbers. If you are a smaller organization, we see some of those employers joining group captives for medical stop loss. If you are a larger employer and you have the numbers, there could be some savings in insuring a layer of the medical in your existing property/casualty captive,” she said.

Captive owners can achieve savings by covering medical stop loss exposures, said Ms. Gray.

“It’s an expensive coverage for companies to purchase and there’s a cost-benefit associated with it if they are able to retain that and write it through the captive,” she said.

However, growth in the coverage of ERISA-type benefits — group term life and long-term disability — is sluggish in part because the cost of the coverage in the commercial market remains competitive, Ms. Gray said.

Owners are also considering, and in some cases including, coverage for cyber risks in their captives, managers say. The interest is in part driven by the lack of comprehensive cyber insurance coverage available in the commercial market, they say.

“There’s cyber coverage out there, but it’s more limited in terms of some of the policy coverages being provided so you can utilize a captive to issue a stand-alone policy. There is some takeup in terms of looking at this, but this is an area that’s still developing,” Ms. Gray said.

More captive owners are considering cyber risk, said Mr. Huish of Artex.

“The cost for commercial cyber is going up, and there’s a realization in the market that the cyber policies that are provided in many cases have a lot of exclusions, so covering some of those risks, or a layer of the risks or the exclusions in your captive, seems to be a topic that people are considering,” he said.

While most captive owners would not want to cover potentially catastrophic cyber exposures in their captives, they might consider carving out some elements of the risk, such as business interruption or the cost of hiring outside advisers in the event of a breach, and providing cov-

See **OVERVIEW** page 32

OVERVIEW

Continued from page 31

erage for those risks through a captive, Mr. Huish said.

But captive owners have concerns about how to price cyber risks, said Ms. Towle of JLT.

“When you hear about these large limits, people are trying to understand and determine what layers make sense to insure in a captive and access reinsurance,” she said.

Some captive owners are looking to use captives for more sophisticated risk management strategies, said Sean Rider, executive vice president and managing director, consulting and development, in Willis Towers Watson P.L.C.’s global

captive practice in New York.

“It’s about using the captive as an aggregator or hub for correlated and noncorrelated risks to create a diversified approach to how you manage the financing of your organizational risk,” he said.

“When you take that and buy reinsurance for it on an integrated basis, the reinsurer also has the benefit of the non-correlation that provides the natural insu-

lation to adverse unexpected outcomes that comes by virtue of noncorrelation, and as a result you end up with a much more efficient risk transfer program at meaningfully lower cost,” he said.

In addition, captives can be used to structure protection for operational risks via parametric coverage, where coverage is triggered by various indices, such as wind speed for storm coverage.

“The growth of the parametric risk transfer market has triggered ideas around how you can use parametric structures to fund risk retention in a captive,” he said.

Industry developments

In addition to insurance-related changes, last year saw regulatory and legal developments that affected captives.

For example, the Organization for Economic Cooperation and Development’s Base Erosion and Profit Shifting initiative, or BEPS, is likely to affect captives globally, Mr. Rider said.

The initiative, which began in 2012, targets multinational companies that use tax planning strategies that exploit gaps and mismatches in tax rules to shift profits to low or no-tax locations where they have little economic activity, such as through a small subsidiary. About 100 countries and jurisdictions have signed up to the project, according to the OECD.

Different tax authorities are applying the initiative in different ways, and in the United States, the initiative has been addressed by the base erosion and anti-abuse tax provision included in the recent tax reform law, which targets financial payments between U.S. companies and foreign affiliates, he said (see story, page 33).

Captives and captive managers in the United States are also facing changes in light of last August’s *Benjamin Avrahami and Orna Avrahami v. Commissioner of Internal Revenue* tax court decision against the owner of an 831(b) captive.

In the case, the IRS alleged that the microcaptive for a jewelry business in Phoenix that ostensibly covered insurance risks charged unrealistic premiums and did not meet risk distribution requirements for captives.

Captives that are established for risk management purposes and include true risk transfer should not be affected by the *Avrahami* ruling, said Ms. Gray of Aon.

“If an 831(b) captive is structured correctly, there’s no problem with tax election,” she said.

Even though the *Avrahami* ruling went against the captive owners and their advisers, the case could be beneficial to other captive owners, said Mr. Huish of Artex.

“*Avrahami* has been a learning experience for the industry — a positive learning experience where people have a chance to evaluate their captive,” he said.



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US tax reform law unlikely to hinder captive formations

GLORIA GONZALEZ

ggonzalez@businessinsurance.com

Captive insurers are losing some of their tax benefits after the U.S. tax overhaul, but the new law is not expected to result in a decline in captive formations for owners creating captives for risk management reasons.

"People should go into captives for the right reasons, and tax should not be your primary motivating factor," said Anne Marie Towle, Indianapolis-based executive vice president and captive practice leader for JLT Insurance Management, a unit of London-based Jardine Lloyd Thompson Group P.L.C. "It's based on risk management, the control and the ability to smooth out your cost of risk over time and having consistency."

"I don't see that there's a mad rush to make significant changes because of the loss of some of the tax benefit," she said, adding that a "good portion of our clients" do not take the tax benefit for the captive, instead using it for risk management or to access the reinsurance market. "For them, this is a nonevent because they're not going to make changes just because the tax law changed."

In December, President Donald Trump signed the Tax Cuts and Jobs Act, which replaced the graduated corporate income tax structure and its previous top rate of 35% with a 21% rate and included new rules for computing discounted loss reserves, namely a switch to using a corporate bond yield curve to calculate discount factors instead of the applicable federal rate, which will result in smaller deductions for the reserves, experts say.

"That aspect of the change in law is likely going to offset a big portion of that rate reduction," said Matt Gravelin, a Burlington, Vermont-based principal with tax and audit consulting firm Johnson Lambert L.L.P.

The rule determining what constituted a controlled foreign corporation was also changed. A CFC is generally defined as a foreign corporation in which U.S. persons owned more than 50% of the corporation's stock, with the standard for insurers being that the combined voting power of all classes of stock had to exceed 25%. However, the definition of U.S. shareholder, which had been defined as a U.S. person that owns 10% or more of the voting stock of a foreign corporation, was expanded to also include U.S. persons that own 10% or more of the value of the stock of the foreign corporation.



REUTERS

President Donald Trump signed the \$1.5 trillion tax reform measure into law in the Oval Office of the White House in December.

"If you own a lot of nonvoting stock, the entity might not have been a controlled foreign corporation, but it may become one now," said Charles Lavelle, senior partner in the tax and employee benefits department of Bingham Greenebaum Doll L.L.P. based in Louisville, Kentucky.

Meanwhile, the passive foreign investment company rules are essentially designed to prevent U.S. persons from investing in corporations with a view toward not reporting the earnings and profits as if they were earned in a foreign corporation, with penalties imposed on the taxes that must be paid on this income.

"I don't see that there's a mad rush to make significant changes because of the loss of some of the tax benefit ... (a) good portion of our clients" do not take the tax benefit for the captive, instead using it for risk management.

Anne Marie Towle, JLT

A company is defined as a PFIC based on either income, meaning at least 75% of the corporation's gross income is "passive" income that is derived from investments rather than from the company's regular business operations; or

based on assets, meaning at least 50% of the company's assets are investments that produce passive income or are held for the production of passive income.

Companies in the "active conduct" of the insurance business were exempt under the old law and can remain so under the new law, but they must now meet a test that their active insurance assets constitute more than 25% of the insurer's total assets.

Foreign companies that become CFCs or PFICs under the new law will likely face the biggest impact, Mr. Lavelle said.

"I don't think these two changes will affect a huge number of captives, but those that it does affect are seriously reviewing the law and beginning to consider their options," he said. "My sense is that people are still assessing."

The U.S. tax overhaul also included the Base Erosion Anti-Abuse Tax provision, which imposes a minimum tax on certain deductible payments made to a foreign affiliate, including payments such as management fees and royalties, but excluding costs of goods sold, beginning in tax years after Dec. 31, 2017. The BEAT provision applies a minimum tax of 10% of taxable income.

"They're trying to cut down on shifting of profits between the U.S. and low-tax jurisdictions, which has been an issue for at least the last five to 10 years," Mr. Gravelin said. "The BEAT tax is only going to impact really large captives because there is a threshold of essentially a three-year average gross receipt that has to exceed \$500 million. I don't think a lot of captives will meet that."

COUNTING CAPTIVES

Ranked by number of captive licenses at year-end 2017

Rank	Domicile	2017	2016
1	Bermuda	739	776
2	Cayman Islands	669	683 ¹
3	Vermont	566	593
4	Utah	480	462
5	Delaware	391	385
6	Guernsey	315	321
7	Barbados	266	246
8	Anguilla	258 ²	287 ²
9	Hawaii	230	208 ¹
10	North Carolina	220	189 ¹
11	Nevada	204	200 ¹
12	Luxembourg	203	208
13	South Carolina	172	164
14	Tennessee	155	149 ¹
15	Nevis	151	150 ^{1,4}
16	Montana	140	163 ¹
17	Arizona	121	113
18	British Virgin Island	111	137
19	Isle of Man	109	111 ¹
20	District of Columbia	102	100
21	Kentucky	84 ²	84
22	Dublin	83	85
23	Oklahoma	75 ³	75
24	Singapore	70	71
25	Turks and Caicos Islands	67	64
26	New York	62	62 ¹
27	Alabama	50	48
28	Missouri	48	48
29	Labuan	40	39
30	St. Lucia	38	35
30	Texas	38	34
32	Sweden	35 ²	40 ²
33	South Dakota	34	26 ¹
34	Switzerland	26 ²	31
35	Micronesia	24	18 ¹
36	Bahamas	23	21
36	New Jersey	23 ²	23
38	Michigan	22	20
39	British Columbia	21	20
40	Georgia	20	28
41	Ohio	15	14
42	Connecticut	14	14
43	Puerto Rico	13	11 ^{1,4}
44	Denmark	11	13
45	Gibraltar	10	10 ¹
45	Liechtenstein	10	11 ¹
45	Malta	10	10
45	Norway	10 ²	10 ²
45	Panama	10 ²	10
50	Germany	9 ²	9 ²
51	New Zealand	6 ²	8
52	Australia	5 ²	5
52	Colorado	5	4
52	Vanuatu	5	8
55	Arkansas	4	3
55	Nebraska	4	4
55	U.S. Virgin Islands	4	4
58	Guam	3	3
58	Hong Kong	3	3
58	Illinois	3	3
61	Maine	2	2
61	Jersey	2 ²	2
61	Dubai	2 ²	4 ²
64	Mauritius	1	6
64	Kansas	1	2 ¹
	TOTAL	6,647	6,700 ¹

¹ Restated. ² B/ estimate. ³ From annual report. ⁴ Restated to exclude individual cells/cell members from total captive count.
Source: B/ survey

RRGs evolve, grow from modest beginnings

BY JERRY GEISEL

More than three and a half decades after Congress passed legislation allowing the formation of risk retention groups, the alternative risk transfer vehicles remain a vital source of coverage for their tens of thousands of policyholder-owners.

Risk retention groups, which are multiple-owner captives and can do business in any state after meeting the licensing requirements of one state, have grown significantly over the past couple of decades: As of the end of January, 230 RRGs were operating compared with 100 in 2003, according to the Risk Retention Reporter, a monthly newsletter covering the sector.

Some RRGs reported huge growth in the number of policyholders, as well as their premium volume.

For example, United Educators Insurance, a Reciprocal Risk Retention Group, which is licensed in Vermont and based in Bethesda, Maryland, now has about 1,600 policyholders and \$200 million in premium volume. That compares with 900 policyholders and \$25 million in premium volume 20 years ago.

"We provide significant risk management services and stability of premium rates," said Janice Abraham, United Educators' president and CEO, adding that the RRG has a 99% policyholder



renewal rate.

"Members stay with us not just because premiums may be the least expensive, but because of the total package of services," Ms. Abraham added. For example, the United Educators' RRG, Ms. Abraham says, offers an extensive array of online courses targeted to the specific risks of schools and colleges.

Even during the current soft market, some RRGs continue to attract new members, boosting their premium volume. For example, the Alliance of Nonprofits for Insurance, Risk Retention Group, which was licensed in Vermont in 2000, added

760 policyholders between 2016 and 2017, with premium volume rising by about \$3 million. The RRG now has about 7,600 policyholders and more than \$43 million in premium volume.

"We are definitely continuing to grow," said Pamela Davis, president and CEO of the RRG in Santa Cruz, California. "We believe we are a great long-term value. Those who will stay will benefit from premium stability, broad coverage and extensive risk management services."

The RRG offers coverage for improper sexual conduct liability, employment practices liability, professional liability,

general liability, commercial auto liability, directors and officers liability and umbrella liability.

"We've had 100% renewal for the last six years," said Mike Miller, senior program director in St. Charles, Illinois, for Washington, D.C.-licensed Trinity Risk Solutions RRG. The RRG, which initially provided general liability and professional coverage to nonprofit senior care facilities, recently began offering coverage to for-profit senior care operators.

Stable premiums and "top risk management services" have driven that 100% renewal rate, even "in the face of tough competition" from the commercial market, Mr. Miller said, adding that Trinity Risk Solutions "provides clinical, regulatory and compliance assistance from highly qualified risk management experts, all with years of experience working in the senior care field."

Not all RRGs have that kind of retention rate, due in large part to stiff competition from commercial insurers.

"Insurers have a big war chest, and they can compete aggressively," said Jeremy Brigham, a director in the Hartford, Connecticut, office of Willis Towers Watson P.L.C., adding that in some cases the need for RRGs has tapered off.

Indeed, while the number of RRGs has, over the last couple of years, stayed in the 230-235 range, it is down from the peak of about a decade ago when premiums

EFFORTS TO EXPAND RISK RETENTION GROUP COVERAGES FALL SHORT

Risk retention groups have pressed federal lawmakers for nearly a dozen years to expand the coverages RRGs can provide, but they have yet to win broad congressional support.

Under the original Risk Retention Act passed by Congress in 1981, RRGs — which, unlike other types of captives, are allowed to do business in any state after meeting the licensing requirements of one state — could only write product liability and completed operations coverage for their policyholder-owners.

Five years later, Congress, responding to soaring premiums in the traditional market for a wide range of liability coverages, expanded the Risk Retention Act to allow RRGs to write all commercial casualty coverages except workers compensation.

That 1986 expansion had a huge effect on the RRG market. While only a handful of RRGs were formed after the passage of the 1981 legislation, several hundred RRGs have been licensed since the 1986

expansion was approved by Congress.

Lawmakers have discussed expanding the law to allow RRGs to cover property risks since 2006, but expansion proposals have yet to attract widespread congressional support.

A key reason no congressional action has been taken on the various expansion proposals is soft conditions in the traditional commercial market, observers say.

"We have had a soft market for so long that there is limited interest in expansion," said Robert Myers, a partner with the law firm Morris, Manning & Martin L.L.P. in Washington.

"The product liability crisis of 1981 and general liability crisis of 1986 gave rise to the Risk Retention Act," said Jon Harkavy, executive vice president and general counsel for captive and RRG manager Risk Services L.L.C. in Washington. "There has not been an equivalent insurance availability and affordability crisis for



property to spur expansion of the Risk Retention Act."

At the same time, the scope of RRG expansion has become more limited. While earlier proposals would have allowed all RRGs to offer property coverage, the most recent legislative proposals have been much narrower.

For example, legislation introduced in the last congressional session would have only expanded RRGs' underwriting authority to allow the groups to provide property coverage for policyholders that are nonprofit organizations with tax-exempt status or educational and educational-related institutions

were soaring for many lines of coverage. At the end of 2008, just over 260 RRGs were operating.

As the traditional market softened, “The need for RRGs tapered off,” said Bruce C. Whitmore, senior vice president and senior resource consultant in Willis Towers Watson’s Tampa, Florida, office.

One thing that hasn’t changed is where RRGs decide to be licensed. While RRGs are spread across states with captive laws, Vermont — from the start and today — is home to more RRGs than any other state.

Currently, 90 RRGs, or close to 40% of all RRGs, are licensed in Vermont.

Vermont regulators “really understand RRGs. Vermont has a reputation of being the gold standard,” said Michael Serricchio, a managing director with Marsh Captive Solutions in Norwalk, Connecticut.

What has changed is the size of some RRGs. For example, Attorneys’ Liability Assurance Society Inc., a Risk Retention Group, provides coverage to 62,000 lawyers and has projected premium volume this year of more than \$350 million.

The RRG’s size is due to loss control services “unmatched” by the commercial market, said Mark Galen, general counsel and executive vice president-member relations in Chicago for ALAS, which is licensed in Vermont.

That commitment to risk management, which includes numerous loss control conferences, such as one in March on cyber security, for example, has held down losses and enabled the

RRG to offer rates that are lower compared with its formation in 1996, Mr. Galen said.

In addition to conferences, ALAS offers members other “unique resources and services that cannot be purchased commercially,” Mr. Galen said.

Those resources and services “include a wide variety of printed and electronic publications, customized on-demand programs and presentations addressing current issues from ALAS claims, with 25 experienced ALAS lawyers to answer complex questions and assist firms with difficult internal issues or major projects,” he said.

“There is a strong commitment to risk management and loss control,” Mr. Galen added.

In all, RRGs with the highest longevity have several shared characteristics, said Michael Bemi, who retired last year as president and CEO of Vermont-domiciled The National Catholic Risk Retention Group Inc., which has operated for more than 30 years.

Those common threads, Mr. Bemi said, include a “bona fide raison d’être for establishment — including coverage unavailability, coverage inadequacy and/or unaffordability in the traditional market — and strong grass-roots support from potential policyholder-owners.”

In addition, Mr. Bemi said, RRGs with the greatest longevity have “worked hard to be good and stay good at the fundamentals, i.e., underwriting, claims management, risk control, investment management, reinsurance placement and marketing.”

that are nonprofit organizations or governmental entities.

In addition, an eligible RRG would need to have been operating for at least 10 years and maintain capital and surplus of at least \$10 million.

Observers say chances are low that Congress will soon expand coverages RRGs can offer. The commercial property market is “functioning pretty well,” said Jeremy Brigham, a director in the Hartford, Connecticut, office of Willis Towers Watson P.L.C.

But some RRGs say they would welcome such an expansion.

“That kind of flexibility makes sense,” said Christopher Smith, Atlanta-based president and CEO of MCIC Vermont, a Reciprocal Risk Retention Group.

“Why should RRGs be limited in the coverages they offer? Allowing RRGs to expand outside of providing liability-only coverages could be a benefit to their members,” said Mark Tabler, chief operating officer of Physician Solutions Risk Retention Group, a

Vermont-domiciled RRG, which provides professional liability coverage to about 400 physicians.

Backers of such an expansion say they will continue to press federal lawmakers to approve, at least for nonprofits, legislation to enable RRGs to cover property risks of their member-owners.

“We are continuing to work on this issue that is so important for nonprofit organizations,” said Pamela Davis, founder, president and CEO of Alliance of Nonprofits for Insurance, Risk Retention Group, which is headquartered in Santa Cruz, California, and was licensed in Vermont in 2000.

“We have demonstrated that small and midsize nonprofits are offered property from commercial carriers only in a ‘package’ policy with the liability and property combined. The stand-alone auto physical damage and property policies that these small nonprofit members of a risk retention group need are not available,” Ms. Davis added.

Jerry Geisel

Keenan

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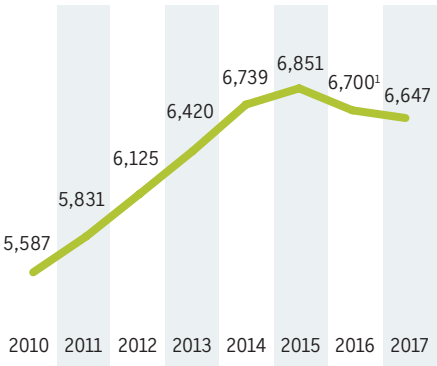
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\$1 Billion and Counting...



RANKINGS OF CAPTIVE DOMICILES & CAPTIVE MANAGERS

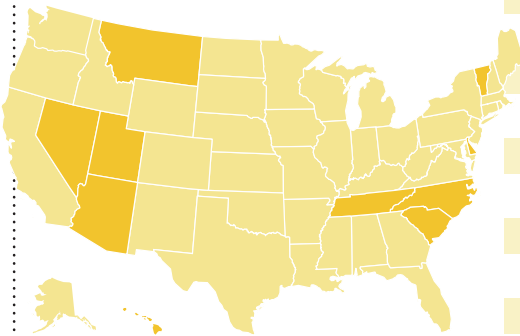
TOTAL CAPTIVES WORLDWIDE



¹ Restated
Source: *BI* survey

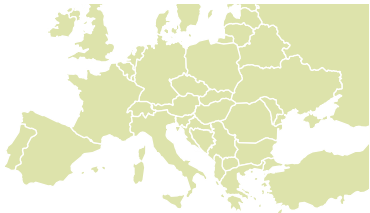
TOP U.S. CAPTIVE DOMICILES

Ranked by number of captive licenses at year-end 2017



Rank	Domicile	2017	2016
1	Vermont	566	593
2	Utah	480	462
3	Delaware	391	385
4	Hawaii	230	208 ¹
5	North Carolina	220	189 ¹
6	Nevada	204	200 ¹
7	South Carolina	172	164
8	Tennessee	155	149 ¹
9	Montana	140	163 ¹
10	Arizona	121	113

¹ Restated
Source: *BI* survey



TOP 5 EUROPEAN CAPTIVE DOMICILES

Ranked by number of captive licenses at year-end 2017

Rank	Domicile	2017	2016
1	Guernsey	315	321
2	Luxembourg	203	208
3	Isle of Man	109	111 ¹
4	Dublin	83	85
5	Sweden	35 ²	40 ²

¹ Restated. ² *BI* estimate.
Source: *BI* survey

TOP 10 CAPTIVE MANAGERS

Ranked by number of captives managed worldwide in 2017¹

Rank	Company	2017 total captives	2017 captive premium volume ²	Domiciles	Total staff	Officers
1	Marsh Captive Solutions	1,244	\$55,666,742,491	49	400	Ellen Charnley, president; Julie Boucher, practice leader-Americas; Ian Clancy, practice leader-EU
2	Aon Captive & Insurance Management ⁵	984	\$31,000,000,000	48	558	John English, COO
3	Artex Risk Solutions Inc. ³	745	\$6,500,000,000	32	416	David McManus, president/CEO; Jennifer Gallagher, president-Artex North America; Nick Heys, CEO-Artex International
4	Willis Towers Watson P.L.C., Global Captive Practice	398	\$6,929,030,000	36	196	Paul Owens, CEO; Sumit Mehra, chief operating officer; Sean Rider, director-business development
5	Strategic Risk Solutions Inc.	298	\$3,100,000,000	23	100	Brady Young, president/CEO; Michael O'Malley, senior vice president/managing director; Andrew Berry, chief operating officer
6	USA Risk Group Inc.	288	\$3,358,258,364	27	47	Gary Osborne, president; Shawn Burger, chief operating officer; Paul Macey, head of captive operations
7	JLT Insurance Management	171	\$2,341,672,100	20	61	Steve Arrowsmith, CEO; Melissa O'Sullivan, chief financial officer; Richard Daley, president
8	Quest Management Services Ltd. ⁴	105	N/A	9	22	Nicholas Dove, chairman; Nicholas Frost, president; Jeff Kenneson, president-Quest USA
9	Risk Services L.L.C.	104	\$305,600,000	10	32	Mike Rogers, chairman/CEO; Jon Harkavy, executive vice president; Troy Winch, vice president
10	Atlas Insurance Management	92	\$250,000,000	14	30	Martin Eveleigh, chairman; Elaine Tapp, executive vice president

¹ Captives electing to operate under Section 831(b) of the U.S. Tax Code are now included
² Premium volume includes total gross premium volume of captives managed by the company or on behalf;
³ Acquired Chandler Insurance Management Ltd. in October 2017.
⁴ Formerly R&Q Captive Holdings Ltd. R&Q's international insurance services assets acquired by The Davies Group and new organization is being renamed.
⁵ Restated on May 3, 2018. Following recent discussions between Aon and *Business Insurance* in which clarification was sought as to the intended definitions sitting behind the captive survey categories, Aon has revised the submission to more accurately reflect the Aon Portfolio.
Source: *BI* survey



TOP 5 NORTH AMERICAN OFFSHORE CAPTIVE DOMICILES

Ranked by number of captive licenses at year-end 2017

Rank	Domicile	2017	2016
1	Bermuda	739	776
2	Cayman Islands	669	683 ¹
3	Barbados	266	246
4	Anguilla	258 ²	287 ²
5	Nevis	151	150 ¹

¹ Restated. ² *BI* estimate.
Source: *BI* survey



TOP 5 ASIA-PACIFIC CAPTIVE DOMICILES

Ranked by the number of captive licenses at year-end 2017

Rank	Domicile	2017	2016
1	Singapore	70	71
2	Labuan	40	39
3	Micronesia	24	18 ¹
4	New Zealand	6 ²	8
5	Australia	5 ²	5

¹ Restated. ² *BI* estimate.
Source: *BI* survey

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COMMENTARY

Self-driving cars may disrupt market

The advent of fully autonomous vehicles raises some obvious and not-so-obvious issues for insurers and their customers. Demand for auto insurance coverage will undoubtedly change. Although we may still be some years away from widespread use of autonomous vehicles, as we report on page 6, established car manufacturers and newer rivals are making rapid progress in the development of driverless cars and plan for their limited introduction soon.

Their uptake — if they work according to plan — may well be more rapid than expected. Drivers eager to be rid of the frustration of sitting behind a wheel in traffic or the monotony of driving down seemingly never-ending highways will likely quickly embrace the new technology. And if firms making retrofit kits to convert existing cars to autonomous or semiautonomous vehicles are successful, the migration to self-driving cars could accelerate.



Gavin Souter
EDITOR

Add to that the economic benefits of not having to own, maintain or insure a vehicle — several experts predict that the business model for autonomous vehicles will be some form of on-demand setup — and many car owners will likely eagerly convert from drivers to riders.

If that happens, accidents, which are usually caused by human error, will fall dramatically and the cost of auto liability insurance should plummet, too. Demand for product liability, cyber liability and other commercial coverages to cover manufacturers, suppliers and others in the autonomous vehicle field may rise, but surely not so much to take over the capacity in the massive auto insurance sector.

That then leads to the not-so-obvious issue: What will insurers do with all that excess capacity? While they may follow the lead of buggy whip makers and close up shop, that seems unlikely. With all the underwriting, marketing and financial expertise that auto insurers hold, more likely they will look for other opportunities in the commercial and personal lines insurance sector.

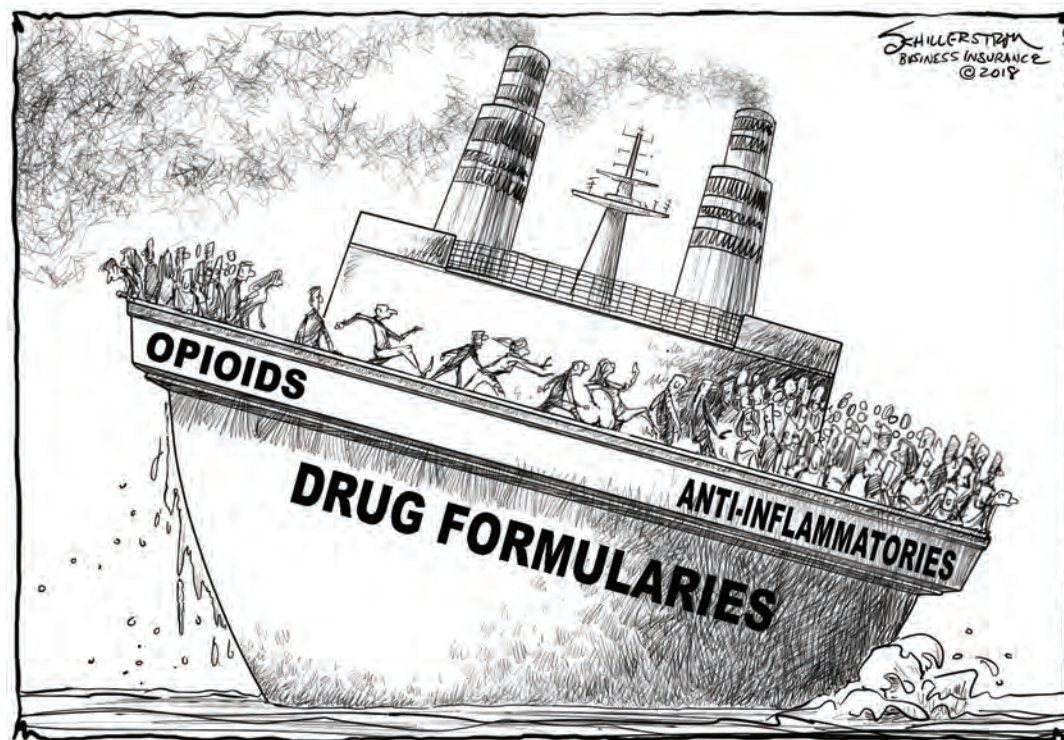
Efforts to spread the purchase of insurance to developing countries may accelerate as a result of insurers looking to tap new markets, but it's hard to see demand increasing that dramatically.

Another route would be to look for other opportunities in existing markets. Some underwriters over the years have shown an aptitude for getting out of one line of coverage and pursuing another when prices change. Recently, for example, several reinsurers have targeted commercial insurance as reinsurance rates have fallen.

If that trend accelerates, commercial insurance buyers, already enjoying a market awash with traditional and nontraditional capital, may find even more capacity available to cover their exposures. If cyber liabilities in general continue to grow they many need the added capacity but it's still too early to tell.

Of course, if catastrophe losses such as those that occurred in 2017 become a regular occurrence, claims from large commercial policyholders, Main Street businesses and homeowners will use up plenty of the excess capital, but let's hope for all our sakes that that's not the solution to the problem.

SCHILLERSTROM



VIEW FROM WASHINGTON

Action needed on opioids

There are signs Congress is starting to understand the imperative of tackling America's opioids epidemic. It's well past due.

The U.S. House of Representatives on Feb. 15 held a joint hearing of its subcommittee on Health, Employment, Labor and Pensions and its subcommittee on Workforce Protections titled The Opioids Epidemic: Implications for America's Workplaces. This was one of several hearings held or scheduled to examine the multiple facets of the opioid crisis and potential legislative solutions.

The costs of the opioid crisis are staggering. Corwin Rhyan, a senior health care analyst for non-profit research and consulting organization Altarum Institute in Ann Arbor, Michigan, testified that the total U.S. economic burden exceeded \$95 billion in 2016, a figure that included productivity and earnings losses, increased health care costs and criminal justice expenses. He estimated the total U.S. economic burden could exceed \$500 billion over the 2017-2020 timeframe if these costs continue to grow at the current rate.

Mr. Rhyan and other experts testified about the impact of opioids on the workforce, with employers in some parts of the country foregoing drug testing because of an inability to hire candidates who can pass a clean drug test. Other employers remain confused and uncertain about their rights to drug test employees injured on the job because of the anti-retaliation provisions of the U.S. Occupational Safety and Health Administration's electronic recordkeeping rule.

The workers compensation industry is on the front lines of the opioids crisis and isn't waiting for Washington to act. But there are limits to what the industry can do, particularly when the first instinct of medical professionals is to prescribe an opioid, and the pharmaceutical industry continues to market

opioids as a first-choice, pain-relief method.

Christina Andrews, an assistant professor at the University of South Carolina in Columbia who researches how to improve access to opioids addiction treatment, was asked during the hearing about the marketing of opioids to doctors.

"It has been a very problematic trend that these drugs have been marketed to physicians over a long period of time," she said.



Gloria Gonzalez
DEPUTY EDITOR

Can Congress do something about that? That could be a challenging area to regulate, given free speech considerations. But Congress could pass legislation to preserve access to treatment provided by the Affordable Care Act and uphold existing regulations on association health plans rather than allowing the proliferation of plans that may not provide coverage for opioid use disorder treatment — just two of the solutions suggested by Ms. Andrews.

President Donald Trump can help with this legislative push. He mentioned opioids during his State of the Union in January, referencing the 64,000 Americans lost to drug overdoses in 2016. His comments focused on tough measures against drug dealers, but the mere reference to the crisis is a hopeful sign.

White House staffers spend weeks discussing and debating what should or shouldn't be said in that speech so its inclusion demonstrates that there is some understanding of the urgency of the situation. But the president and legislators must be willing to listen to the people on the front lines of the addiction battle in crafting their solutions.

Navigating reps and warranties claims when M&A complications arise



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Despite the best efforts of conscientious counsel, almost half of all merger and acquisition deals are subjected to post-closing price adjustment claims. Traditionally, these disputes were resolved through working capital adjustments, earn-outs or indemnification payouts — solutions that frequently cause unwelcome delay and increased contentiousness. Moreover, attorneys often found their requests for more diligence at odds with the clients' desire to close the deal quickly.

Addressing the need to leave no stone unturned while remaining nimble, representations and warranties insurance policies were developed. Although early policies were costly and riddled with exclusions, the reps and warranties industry has evolved and expanded. Today, approximately 25% to 33% of private M&A deals provide for reps and warranties coverage as recourse for breaches of representations or warranties in purchase or merger agreements.

The policies can insure either the buyer or the seller, but most policies purchased insure the buyer against breaches by the seller. Often used in addition to or in place of indemnity, the coverage can attract better offers by offering greater indemnification, ease concerns regarding collection, and preserve relationships by shifting risk to a third party.

Seller-insureds might use a reps and warranties policy to manage their own risk or successor liability, whereas buyer-insureds might look to the coverage to distinguish a bid in a competitive auction or mitigate credit risk in a distressed asset setting.

The American Bar Association estimates that between 12% and 17% of policies purchased are subjected to claims. An American International Group Inc. 2016 study — What Happens After the Deal Closes? Representations and Warranties Insurance Global Claims Study — estimates that about 14% of reps and warranties policies issued between 2011 and 2014 reported a claim. And other sources put the number as high as 35%, depending on the year.

Representations and warranties related to financial statements, taxes, contracts and intellectual property are the most common sources of claims, but claims can also cover unexpected events such as civil antitrust judgments — breach of representation that the seller complied with all laws — or fraud by a third party resulting in overpayment by the target company.

Many reps and warranties policies require claims to be resolved through confidential arbitration, resulting in a dearth

of information on the outcome of these claims. But certainly, the proliferation of the coverage has led to a growing pool of claims to be resolved in relatively uncharted territory.

A few considerations policyholders navigating this process must consider include constraints on evidence, consistency when litigating parallel claims, and avoiding conflicts.

Constraints

While reps and warranties policies are often tailored to a particular deal, the process for filing a claim is usually straightforward:

1. A breach is discovered, and proper notice is sent to the insurer.
2. The policyholder submits proof of loss, a calculation of damages and details on the facts and circumstances surrounding the breach.
3. The insurer conducts a comprehensive review to evaluate whether there is a breach covered by the policy, whether there are relevant exclusions and whether loss flows from the breach.
4. The insurer and policyholder endeavor to negotiate a settlement.
5. If no settlement is reached, the claim proceeds to the dispute resolution process in the agreement, often a confidential and closed arbitration.

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Closed arbitrations limit admissible evidence to the parties' submissions during the initial notice of claim and investigation process.

But, as previously stated, buyer-side reps and warranties insurance is often

used to entice sellers by relieving them from involvement in post-closing claims. Where the breaching seller is not a party to the claims process and cannot be relied upon to provide information and evidence on the alleged breach, presenting sufficient evidence can prove challenging.

Policyholders on the buyer side of transactions must therefore consider the constraints and limitations of a policies' arbitration clause at the outset, resist a false sense of security and be diligent in gathering information from the seller prior to closing.

Post-closing cooperation clauses are one possibility but unlikely to have much practical effect. This is particularly true where the insurer may seek to recover its payout from the breaching party, although the insurer typically has no subrogation rights against the seller under the policies, except for instances of fraud.

Consistency

Policyholders and their counsel must also maintain a consistent approach where both indemnity and insurance funds are available as recourse.

Some policies are structured to replace escrow and indemnification altogether (e.g. where an escrow is impossible, such as bankruptcy, public company transactions, etc.), whereas others are used to supplement those obligations (e.g. a buyer-side policy where the seller is responsible for paying a portion of the retention with escrowed funds).

However, negotiating the settlement of indemnity claims in parallel with reps and warranties claims requires attention to consistency. Policyholders seeking full damages from insurers must be just as diligent in pursuing indemnity funds, lest they arouse skepticism from the insurer.

Conflicts

Finally, insureds must carefully consider who will litigate reps and warranties claims submitted to dispute resolution.

Naturally, when a deal dispute arises, transactional lawyers are quick to call a litigator in their own firm. And there can be efficiencies when the firm who “did the deal” handles the dispute: they have cleared conflicts with the client, built relationships, and become familiar with the diligence and events that led to the dispute at hand.

However, if the firm's underlying deal work becomes an issue in litigation of a claim or other dispute, the law firm's work can be called into question.

Marsh offers GL cover for construction sector

■ Marsh L.L.C. has launched Project Edge, a U.S. project-specific general liability product designed for the construction industry.

Project Edge is intended to respond to the evolving nature of the industry, including the risks associated with drones, the internet of things, alternative project delivery methods, and off-site construction, Marsh said in a statement. It was developed by Marsh's global construction practice, is underwritten by Lloyd's of London syndicate Apollo Underwriting Ltd. and contains nearly a dozen liability coverage enhancements.

Project Edge is available to Marsh construction clients as either a standard general liability policy or as a wrap-up and offers up to \$2 million in primary limits per occurrence, according to the statement.

Swiss Re partners with data firm on underwriting

■ Geospatial insurance technology company SpatialKey Inc. will offer insurers multiperil hazard data from Swiss Re Ltd. through SpatialKey's proprietary underwriting solution.

The collaboration integrates Swiss Re's CatNet hazard data directly into SpatialKey's platform, giving insurers access to 10 hazards, including flood, earthquake, tsunami, wind, hail, tornado, wildfire and storm surge, Denver-based SpatialKey said in a statement.

"Traditional cat models may lack coverage for certain perils or regions, leaving substantial gaps," Peter Hausmann, Zurich-based head of natural catastrophe and engineering solutions at Swiss Re, said in the statement. "In light of last year's heavy catastrophe-related losses, deeper intelligence is needed to underwrite these volatile risks."

PartnerRe links with agricultural data firm

■ PartnerRe Ltd. and Farmers Edge Inc. have entered a four-year agreement to develop agriculture insurance products in crop-growing areas worldwide.

Their goal is to help farmers improve the efficiency and sustainability of their operations by using insurance products with integrated precision-farming capabilities from Winnipeg, Manitoba-based Farmers Edge, the companies said in a joint statement.

Farmers Edge combines hardware, software, agronomy and support to farmers, provides a "turnkey system" including soil sampling and analysis, field-centric weath-



California OKs surety bond program for pot

■ California has approved the state's first surety bond program for the cannabis industry, according to State Insurance Commissioner Dave Jones.

Surety bonds for marijuana business can now be issued by Mayfield Heights, Ohio-based Continental Heritage Insurance Co., the first insurer in the state to be approved to offer surety bonds for the cannabis industry, the commissioner's office said in a statement.

Such bonds are required for certain licensing. The state of California requires a \$5,000 surety bond for most licensing categories, the statement said.

"Cannabis businesses should have insurance coverage available to them just like any other California business," Mr. Jones said in the statement.

er monitoring, in-field telematics and data transfer, daily satellite imagery, data analytics, predictive modeling and other features. Its platform helps farmers collect, store and transfer data, allowing them to measure results and make management decisions, according to the statement.

"We are delighted to be at the forefront of this exciting and innovative new initiative with Farmers Edge and look forward to partnering with our insurance clients to bring it to market," Emmanuel Clarke, president and CEO of Pembroke, Bermuda-based PartnerRe, said in the statement.

Ryan Specialty launches Latin American MGU

■ Ryan Specialty Group L.L.C. launched Latin America-focused managing general

underwriter Capital Bay Underwriting Group L.L.C., which focuses on financial lines insurance and reinsurance for financial institutions and commercial entities.

The main products being offered by the Miami-based managing general underwriter are directors and officers liability insurance; employment practices liability insurance; bankers blanket bond and electronic and computer crime; financial institutions professional indemnity; investment managers insurance; private equity/venture capital; commercial crime and commercial professional liability, Chicago-based Ryan Specialty said in a statement.

Limits of \$10 million are offered, according to a spokeswoman.

Ryan Specialty group announced in July that it had hired Pascal Alvarez, Capital Bay's president and CEO, and David Gonzalez, the unit's chief underwriting officer.

Hub launches specialty practices

■ Hub International Ltd. has started offering eight specialty insurance practices.

Hub said in a statement that its first specialty practices include transportation, financial institutions, entertainment-sports, construction, agriculture, hospitality, real estate and health care.

The Chicago-based brokerage said it selected the industries based on position for growth, depth of expertise and strength of industry value proposition, and where it has a substantial portfolio of clients. Hub Specialties are based on a model that will allow the brokerage to scale and establish future industry specialties based on regional needs and client demands, it added.

Coverage program for cannabis industry

■ Cannasure Insurance Services plans to launch a comprehensive coverage program for the cannabis industry, the MGA and wholesale broker said in a statement.

The program will offer property, general liability, products liability, crop and excess liability to dispensaries, cultivators, processors/manufacturers, ancillary businesses, landlords and testing laboratories, the Westlake, Ohio-based managing general agent and wholesale broker said in the statement. The program is backed by Topa Insurance Co., a Calabasas, California-based commercial lines insurer.

"The cannabis industry is evolving at an unprecedented rate, and because of this so are the industry-specific risk factors and operational demands," Patrick McManamon, CEO of Cannasure, said in the statement.

DEALS & MOVES

Ryan Specialty to buy underwriting manager

Ryan Specialty Group L.L.C. reached a definitive agreement to acquire specialty intermediary New Day Underwriting Managers L.L.C.

Terms of the transaction were not disclosed.

Hamilton, New Jersey-based New Day specializes in environmental liability and construction-related professional liability insurance, Chicago-based Ryan Specialty said in a statement. It will become part of R-T Specialty L.L.C., Ryan Specialty's wholesale brokerage unit.

New Day President Jefferey S. Lejfer, who founded the company in 2005, will continue to lead it as it combines into RT-Specialty, according to the statement.

AssuredPartners acquires four agencies

AssuredPartners Inc., based in Lake Mary, Florida, has acquired four agencies in Ohio, Louisiana, Tennessee and Georgia, representing a combined \$3 million in revenue.

Terms of the deals were not disclosed. The agencies are DeVenne Insurance L.L.C. in Columbus, Ohio; Delco Insurance Group L.L.C. in Metairie, Louisiana; BWE Insurance in Nashville, Tennessee; and William Adams & Associates in Norcross, Georgia, AssuredPartners said in a statement.

Hub acquires California multiline brokerage

Hub International Ltd. has acquired Fresno, California-based brokerage Der Manouel Insurance & Financial Services Inc. Terms of the deal were not disclosed.

Der Manouel, which also has offices in Pleasanton, California, is a multiline insurance brokerage specializing in agriculture, transportation, nonprofits and construction markets, as well as employee benefits, the Chicago-based brokerage said in a statement.

Alera Group buys Spring Consulting

Deerfield, Illinois-based insurance brokerage Alera Group acquired Spring Consulting Group L.L.C. Terms of the deal were not disclosed.

Boston-based Spring Consulting provides strategy and product development advice to insurance and financial institutions; and overall financing and funding solutions for benefit programs, including the use of captive insurance vehicles.



Stay curious. There are so many interesting and challenging problems in this industry, and a lot of opportunity to grow by continuing to learn and improve your skills.

UP CLOSE

Roger Grenier

NEW JOB TITLE: Boston-based senior vice president, global resilience practice leader at AIR Worldwide

PREVIOUS POSITION: Boston-based director of catastrophe research and development at Liberty Mutual Insurance Co.

GOALS FOR NEW POSITION: The big-picture goal is to help close the gap between the economic and insured losses from catastrophes. That includes applying the tools that have been widely used in the insurance industry to help governments derive a similar value. We're focused on educating and working with partners toward practical and tangible solutions.

ON LEADERSHIP: Assembling and developing a strong team is critical. With the right team working together, you put yourself in a position to be successful. Vision, enthusiasm, communication, being open-minded — these all help create the right environment for the team.

CHALLENGES FACING INDUSTRY: Communicating our value proposition. The industry has not been as effective as we could be in communicating the value of insurance to various stakeholders — individuals, businesses, governments and taxpayers. Insurance plays a key role not only in financial recovery from disasters but also in creating the conditions and incentives which lead to greater resilience, like building codes and land use decisions.

CRYSTAL BALL: A positive trend in the resilience area is available capital moving closer to sources of risk. A somewhat concerning issue is our industry's struggle to attract top talent. We have a good story, but competition is fierce.

FIRST INDUSTRY JOB: I'm trained as a civil engineer and spent several years applying various kinds of environmental models in the engineering consulting industry. My first job in insurance was on a team building a storm surge model for the U.K.

ADVICE: Stay curious. There are so many interesting and challenging problems in this industry, and a lot of opportunity to grow by continuing to learn and improve your skills.

OUTSIDE THE INDUSTRY, A DREAM JOB: Teaching and coaching. I was actively engaged in both during graduate school, and I hope to do more in my current role and in the future.

HOBBIES: Running, saltwater fly fishing

PETS: Dogs, large dogs especially.

THING MOST PEOPLE DON'T KNOW ABOUT ME: I still play organized competitive baseball. It resembles the game you see on television, only slower and with much less skill.

BIGGEST OBSTACLE FOR WORK-LIFE BALANCE: Long commute. I live where I want to, and work where I have to. Also, I don't like to work remotely too often. I prefer the energy in the office.

PET PEEVES: As a co-worker used to say: claims without proof. Also, please check your work!

FAVORITE BOOK: Nate Silver's book "The Signal and the Noise" is an enjoyable, must-read book for anyone who develops or uses models.

MONDAYS: Make a list and get to work. Keep moving forward.

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ON THE MOVE



American International Group Inc. named **Caroline Krass** senior vice president and general counsel, general insurance, and deputy general counsel of AIG. Previously,

Ms. Krass was general counsel of the CIA under President Barack Obama. She is based in Washington.



JLT Re, the reinsurance brokerage unit of London-based Jardine Lloyd Thompson Group P.L.C., named **Erica Davis** senior vice president in New York to lead the cyber and

errors and omission practice for JLT Re in North America. Previously, she was senior vice president and head of specialty E&O at Zurich North America.



Chubb Ltd. named **Michael W. Smith** chief claims officer, replacing Frank Lattal, who continues as senior vice president. Previously, Mr. Smith was chief transformation

officer at American International Group Inc. He is based in New York.



The Bermuda Insurance Institute named longtime market executive and former regulator **Malcolm Butterfield** as CEO. He succeeds Dawnnelle Walker,

who left the organization in September. Mr. Butterfield worked at KPMG L.L.P. from 1994 to 2013 and spent five years as Bermuda's Registrar of Companies.



Zurich North America named **Lillian Labbat** head of trade credit and political risk. She succeeds David Anderson, who left the firm in January. Previously, Ms. Labbat

was managing partner and co-founder of Metis Markets. She is based in New York.



Integro Insurance Brokers has added **Ellen Rensklev**, formerly chief risk officer of Oregon Health & Science University, as a principal in its national health care

practice, a newly created position. She is based in San Francisco.

SEE MORE ONLINE



Travel insurers leery of boozy holidays

Think your travel insurance will cover that drunken tumble on the dance floor while on vacation? Think again, says an article on BBC News' website.

Many insurers have a clause in travel insurance policies that says coverage is refused if the policyholder's accident was caused by excessive alcohol, and many claims wind up in court, said the story: A man who fell and hit his head after "drinking all night" was correctly refused travel insurance cover, an ombudsman ruled, while another who slipped in a nightclub's toilets after a drink should have been covered. "Insurers may choose not to pay out if they believe someone's been drinking excessively, although this doesn't necessarily mean holidays should be totally alcohol-free," Chief Financial Ombudsman Caroline Wayman told BBC News.

Fab Four fakes face the music

Can you find a great Yellow Submarine T-shirt while internet shopping? A Ringo Starr throw pillow? But of course!

And that's why Apple Corps Ltd. and Subafilms Ltd. are suing 48 internet dealers and aliases for promoting, distributing and selling items that bear counterfeit logos or imitations of their respective trademarks, according to Billboard magazine.

The companies, run by Paul McCartney, Ringo Starr and the estates of John Lennon and George Harrison, filed a lawsuit Feb. 1 against the distributors, alleging trademark counterfeiting and infringement, according to the magazine. The suit also claims "false designation of origins" to confuse buyers.



GRUMPY CAT COPYRIGHT RULING A PURR-FECT WIN FOR HAPPY OWNER



Grumpy Cat finally has something to smile about, NPR reported: The owner of the kitty, whose real name is Tardar Sauce, was awarded \$710,000 in a copyright infringement case.

An eight-member jury in decided in favor of cat owner Tabatha Bundesen's suit against Grenade Beverage, the maker of Grumpy Cat Grumppuccino, the station reported.

As the story goes, in 2013, at the height of this Grumpy Cat frenzy, Ms. Bundesen entered into a partnership agreement with father and son Nick and Paul Sandford to license and market the line of iced coffee using the cat's likeness, according to NPR, which added that "the deal went sour."

Janitor on comp caught dancing

A former janitor in California didn't give up his moonlighting gig performing at a nightclub after he told doctors his slip-and-fall at work prevented him from functioning normally.



Marcus Kelly, who was caught on camera dancing on stage, pleaded guilty to workers compensation fraud in February and was sentenced to 30 days in county jail and five years formal probation, and ordered to pay \$40,097 in restitution, the Elk Grove News Net reported.

He worked for the Sacramento City Unified School District as a janitor when he claimed an unwitnessed slip-and-fall at work in September 2014, and was placed on modified duty. Within a month, he told his doctor that his condition had worsened, and he was placed off work, the website reported.



Insurance guy has 'hot guy' alter ego

Red-headed British model Gwilym Pugh used to be an insurance salesman, pudgy and shy, said the Daily Mail. But today he's a svelte, bearded fashion model with a portfolio that includes GQ magazine and a coffee table book about hot guys with beards.

His transformation began in a home office, selling insurance and recovering from knee surgery, the newspaper reported.

"At that time I was pretty overweight, working 12 hours a day, plagued with injuries, which meant I couldn't train at all," he told the Mail Online.

Fast-forward five years and see the results after cleaning up his diet, working out, joining a folk band and having a barber convince him that facial hair could be his signature look.

Mr. Pugh's career is "soaring," the newspaper reported.



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