Captive & Self-Insurance Review

Insurers target market

In a tacit admission that corporations are sold on alternative risk funding methods, insurance companies are setting up special units to sell self-insurers and captive insurance companies their expert services separate from insurance policies. **Page 13.**

Bermuda delays regulation

Bermuda asks its insurance industry to apply for a one-year exemption by April 1 from the new insurance law. **Page 16.**

IRS misses a few

The Internal Revenue Service is only sporadically enforcing its prohibition on tax deductions for premiums paid to captives, while the corporate rush to form new captives has slowed, observers report. **Page 13.**

Municipal risk sharing

Cities, towns and counties all over the country are diving into risk sharing pools with like entities to cut their insurance costs and improve their loss control programs. **Page 13.** This development is just one example of how alternative risk management programs are becoming the norm, Editorial, **page 10.**

Benefits in captives

The long-awaited liberalization of the rule restricting insurance of employe benefit plans with captive companies is expected this spring, but it appears offshore captives will be shunned. **Page 28.**

Employes don't care

Firms don't always announce to their employes when they self-insure their benefit programs, but even when they do, employes don't seem to really care. **Page 32.**

Options for smaller firms

A firm doesn't have to be on the Fortune 500 list to form its own captive insurance company. **Page 39.** But if it doesn't want to solo, there are throngs of trade associations forming group-owned captive insurers. **Page 41.**

Week of January 8, 1979

business insurance

the national newsmagazine of loss prevention, risk financing and employe benefit management

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Allstate stages a blitz for commercial accounts

By JOHN MAES

CHICAGO—Allstate Insurance Co. is gearing up to capture a larger share of the commercial insurance market in 1979 and 1980, a step that company officials hope will ultimately make the firm a leader among commercial insurers.

This year, the company plans to deploy a force of up to 300 independent agents nationwide to sell commercial insurance to medium sized and large accounts under the authority of a special company, Northbrook Property & Casualty Insurance Co., set up by Allstate to handle the effort.

Allstate already writes some small and medium sized commercial business through its own employe sales force and more than 1,000 independent agents, whose efforts will continue this year. But the 300 agents being recruited will go after medium sized and larger risks for the new company, said Robert A. Leibold, an Allstate executive and vp of Northbrook

Continued on page 87

Tax court affirms IRS veto of captives in Carnation Co. test case; Ford settles

By KATHRYN J. McINTYRE

WASHINGTON—The U.S. Tax Court sided with the Internal Revenue Service in a dispute with Carnation Co. over dealings with its captive insurer, dispelling any delight taken in the favorable settlement recently won by Ford Motor Co. in a similar IRS case.

The first two court cases filed in objection to the IRS's unfavorable position on corporate dealings with captive insurers were resolved within weeks of each other: One by a court against the taxpayer and the other by an out-of-court settlement of compromise.

A tax court judge ruled Dec. 26 that premiums paid to Carnation's Bermuda captive underwriting Carnation's risk did not constitute insurance. Carnation therefore could not claim a tax deduction for premiums paid to the captive and could not classify the payments received by its offshore captive as foreign source income.

Just two weeks earlier, Ford and the IRS filed papers with the tax court finalizing their settlement on the tax consequences to Ford of operating a Bermuda captive. The IRS charged Ford with earning as a commission 5% of the premiums paid by Ford foreign affiliates to its captive, *Business Insurance* learned. The IRS had originally charged Ford with earning as constructive dividends the full $5.7 million paid.

At least four more cases are pending against the IRS in which corporations are challenging the IRS's unfavorable tax treatment of corporate dealings with a captive insurer.

Although Ford struck a highly advantageous bargain with the IRS, the judge's decision in the Carnation case presents a far more important regulatory development for the captive insurance company industry. The Carnation case involved insurance of domestic risks with an offshore captive insurer, a more common use of a captive insurer than in the Ford case in which Ford's Bermuda captive insured only the risks of Ford's foreign affiliates.

Furthermore, Carnation was decided in the court. Even though it was decided by only one judge instead of the full tax court as had been hoped—a possible indication that the tax court did not consider the case of great importance to many taxpayers—the decision in the Carnation case sets a precedent while the out-of-court settlement by Ford offers little, if any, precedential value.

Moreover, the Carnation case neatly fits one of the examples cited by the IRS in revenue ruling 77-316 in which the IRS determined an insurance transaction had not taken place for tax purposes.

Carnation is considering an appeal of the judge's decision, which its attorney, J. Patrick Whaley, called "bad, not just for Carnation but for everyone with a captive."

The tax court judge applied a test for insurance established by a 1941 Supreme Court decision and found the Carnation arrangement failed the test. Because insurance "poses unique characteristics," it is subject to a test that would not apply to other intercorporate dealings such as intercorporate inventory sales or asset sales, the judge noted.

Carnation's insurance arrangement, which the IRS and the tax court judge objected to, was based on American Home Assurance Co.'s reinsurance of Carnation's property risks with Carnation's Bermuda captive, Three Flowers Assurance Co. Ltd.

Carnation purchased a three-year blanket property insurance policy from American Home Sept. 22, 1971 providing coverage for up to $500,000 per occurrence with a $10,000 per loss deductible. American Home reinsured 90% of the liability with Carnation's Three Flowers subsidiary. Three Flowers paid American Home a 5% commission on the net premiums ceded and reimbursed American Home for premium taxes.

As a condition of reinsuring Carnation's business with its captive, American Home required

Continued on page 86

Risk Manager of the Year
Deadline: Jan. 15

Wage rules depress benefit hikes

By ELLIS SIMON

NEW YORK—Group insurers are beginning to feel the pinch of President Carter's wage and price guidelines in a falling off in new business coming from employe benefit plan improvements.

Insurers who have yet to feel the effects of the anti-inflation measures expect 1979 to be a lean year as a result of them.

"In the fourth quarter, which usually accounts for 35% of our annual business, we normally can expect 40% of that figure to come from benefit improvements," said J. Peter Hepburn, senior vp at Unionmutual Life Insurance Co. "This year we're getting only dribs and drabs."

Metropolitan Life Insurance Co. senses some falling off in benefit improvements and new benefit offerings such as group dental, said senior vp Philip Briggs. "In areas where there's need for improvements, people are starting to think maybe this isn't the time to do it in light of the wageprice guidelines."

However, benefit improvements already negotiated will continue to be implemented, he predicted.

These reports from insurers are the first indication that employers are shaping their employe benefit programs to comply with the anti-inflation guidelines.

But, not all group insurance executives contacted by *Business Insurance* said they had experienced a reduction in new business resulting from fewer benefit improvements. Gordon Thomas of John

Continued on page 89

Model product liability bill will propose tort solutions

By JERRY GEISEL

WASHINGTON—The Commerce Department this month will unveil for public comment a model product liability bill including a recommendation on how long after production manufacturers should be held liable for their products.

The 35-page bill, which has taken about four months to draft, also offers recommendations in 17 other areas of the tort law including:

- What the manufacturer's responsibility is when a product is improperly designed or when the seller fails to warn of a possible hazard.
- What the manufacturer's liability is for unavoidable defects, such as defects in new pharmaceutical products.
- Assessment of a manufacturer's responsibility when a product has been altered or modified.
- How relevant in a defense of a product liability case is compliance with industry or government safety standards.

The model law, which could be adopted by the states, represents one of the Commerce Department's long term solutions to the nation's product liability problems. A short term solution—increasing the carryback period for product liability losses from three years to 10 years—was approved last year by Congress.

In addition, the Commerce Department is reportedly studying how the use of alternative risk funding methods such as self-insurance or captives can be facilitated to ease liability problems.

The model law will attempt to resolve the current uncertainties in the tort litigation system, one of the causes of high product liability premiums cited by the Interagency Task Force on Product Liability.

Although insurers have applauded the 16 states that have passed product liability reform bills since the current drive to change the tort law began in 1977, they remain concerned about the lack of uniformity in the new laws as well as inaction in other states.

For example, South Dakota's law, passed in early 1978, requires product liability suits to be filed no later than six years after the product was delivered to the first user. Indiana and several other states, however, have 10-year statutes of limitations on filing suits.

Similarly, some states, such as Kentucky and Colorado give manufacturers a defense against liability if their products were made in accordance with industry safety standards. Other states have failed to adopt this provision.

These kinds of inconsistencies in state product liability laws result in uncertainty in underwriting a risk and make rate making difficult, the insurers complain. A uniform tort system would at least make it possible to judge a product exposure, they say.

"If you had uniformity in the tort areas, responsible insurers would consider the model bill in rate settings," said Victor Schwartz, the Commerce Department official who has directed drafting the model bill. "Insurers wouldn't be hit by 50 different approaches."

The bill will only be offered as a model for the states to consider, Mr. Schwartz said. "It is only being offered as a help. . .there is no sledgehammer involved."

Mr. Schwartz hopes that consumers, insurers and manufacturers consider the model bill a fair compromise. "It does not take the approach of making the tort law a compensation system such as no-fault," he said. "On the other hand, it maintains incentives for risk prevention on product sellers where appropriate."

The model bill will be published this month in the Federal Register for public comment. After a 45-day comment period, the bill may be revised. It will then be up to the Carter Administration to decide if it wants to endorse it. ▪

Federal task force wants employers to have tax incentive for work safety

WASHINGTON—A federal task force recommends that the tax code be dramatically altered so employers could only deduct the average cost of workers compensation premiums for their industry and size rather than deducting their actual premium as they do now.

In addition, the growing number of firms that self-insure their workers compensation also could deduct the average cost of workers compensation for their industry. This approach would be a radical change for the current situation in which firms that self-insure can only deduct the cost of claims.

Such a change in the tax code would give employers a greater financial stake in preventing workplace injuries, the task force argues.

"How would this proposal ever work?" pondered Robert Collyer, executive assistant of UBA Inc., a research and educational organization specializing in workers compensation. "The average premium for a class changes all the time. Are we talking about annual averages, three-year averages or what?"

The task force proposal on workers compensation taxation changes would be impossible to implement fairly, said Andre Maisonpierre, vp for the Alliance of American Insurers. "The task force seems to feel that if a plant has different operations, then each operation is rated separately. It just isn't so."

Changing the tax deductibility of workers compensation premiums to reflect an entire industry's experience rather than an individual firm's is one of the hundreds of recommendations the Interagency Task Force on Workplace Safety and Health made in its final draft report last month.

Other recommendations include requiring Occupational Safety and Health Administration (OSHA) field officers to make more frequent inspections at factories with high injury rates as well as providing businesses with more tax credits to encourage investment in safety technology.

The task force was formed in August 1977 by President Carter to explore possible incentives to supplement workplace safety regulations.

The task force could revise its recommendations after it reviews comments from employers, insurers and other interested parties.

Furthermore, the task force report has not yet been endorsed by any government agency or by the Carter Administration. Executive review of the report will not begin until the public comment period expires at the end of February.

The task force said allowing employers to deduct the average cost of workers compensation premiums for their industry and size would reward firms with low accident rates since the difference between the industry's average premium and their premium would result in an additional tax deduction.

At the same time, firms with a high injury rate would be placed at a competitive disadvantage since they would be unable to deduct the full cost of their workers compensation premiums if the premium exceeded the industry average.

Mr. Maisonpierre of the Alliance said the workers compensation tax deduction change would be unfair to many companies.

Two companies manufacturing television sets, for example, are in the same industrial rating classification. However, one company may assemble the cabinets, in which many injuries are likely to occur, while the other firm buys its cabinets from a subcontractor. The firm that assembles its own cabinets probably pays a higher premium than the firm that buys them, perhaps higher than the industry average premium because more injuries are associated with its operations.

However, the task force proposal does not make any distinction between the two companies because they fall in the same rating classification. As a result, the firm that made its own cabinet, even if it ran a safe shop, would be penalized through a reduced tax deduction if its insurance premium exceeded the industry average.

Even if the proposal could be implemented fairly, it's unlikely to be approved by Congress, said Mr. Maisonpierre. Furthermore, IRS officials traditionally have objected to tinkering with the tax code as a means of meeting social objectives.

The task force did reject a suggestion that appeared in the preliminary report to slap a special tax on firms with high injury rates. Such a tax "might have the perverse effect of drawing funds away from precisely those firms which most need resources for injury prevention," the task force said.

The task force also took a swipe at OSHA, the controversial federal safety agency, by chastising the agency for attempting to find and correct all violations of its rules, regardless of whether those violations result in injuries.

Finally, the task recommends, "When general economic conditions permit," the present investment tax credit should be made more flexible so credits also would be given for new non-capital expenditures made to prevent workplace injuries and illnesses. ▪

for your information

P/C carriers top $1.4 billion in 1978 underwriting results

NEW YORK—Property and casualty insurers earned more than $1.4 billion on underwriting operations in 1978, compared with $1.03 billion gained last year.

Total property/casualty premiums written in 1978 are expected to reach $80.5 billion, up from the $72.4 billion in 1977, according to the Insurance Information Institute, a public relations and educational organization representing 170 property/casualty insurance companies.

A net estimated gain from investment operations of $7.3 billion in 1978 should bring total revenue income for the industry to $87.8 billion. The industry's net income from all operations, after taxes, is estimated at $6.9 billion, or about 7.9% of total revenue, compared to the $5.9 billion and 7.5% income for 1977.

The Institute estimates put consolidated surplus at $36.2 billion for 1978, a 23.5% increase over last year. This, compared with the written premium estimate of $80.5 billion, produces a ratio of surplus to premium of 2.22 to 1, compared with 2.47 to 1 at the close of 1977.

Unpaid directors face new hazard

WASHINGTON—Directors of a firm who served on a board without pay or directors and officers liability coverage had to pay for the costs of settling a lawsuit out of their own pockets, but couldn't tax deduct the cost of settling the $1.5 million lawsuit, The Wall Street Journal reported recently.

The IRS decided in this case that directors who are paid to serve on a board could take the deduction as an "ordinary and necessary" business expense. But a recent private letter ruling doesn't allow directors who serve without pay to take the deduction because the board members aren't officially considered to be in a trade or business for which they could take the deduction.

New chemical dump sites riskier

NIAGARA FALLS, N.Y.—Three more chemical dumping sites maintained by Hooker Chemical and Plastics Corp. here are larger and potentially more dangerous than the Love Canal site that forced 239 families to abandon their homes after leaking toxic chemicals caused birth defects and miscarriages.

Hooker Chemical owned the Love Canal site until 1953 when it was donated to the city as a site for a public school. Notice of claims totaling $2.65 billion have been filed against the city, county and school district by residents of the area.

At another site at Hyde Park, containing more than 80,000 tons of hazardous wastes, toxic pesticides were found leaking into groundwater and threatening the nine homes in the vicinity. Reportedly, 3,300 tons of trichlorophenol were dumped there. Synthesis of that amount of the chemical would yield 2,000 pounds of dioxin, a poison as toxic as botulism or shellfish toxin. The Love Canal site is believed to contain 200 tons of trichlorophenol, yielding about 130 pounds of dioxin.

Hooker Chemical had sought permission for the city to construct a drainage system around the Hyde Park site, but state health commissioner Dr. David Axelrod asked that the project be delayed until a safety plan was implemented to protect workers at the site from accidental gasification of chemicals during the digging and prevent dioxin-contaminated particles from leaving the site.

Two other dumping sites were found adjacent to entry points for the city's drinking water system, but there has been no significant pollution of the water system as a result, according to Dr. Axelrod.

Medics suggest health care plan

CHICAGO—The American Medical Assn. will curb its activity in the debate over national health insurance next year, but will make four recommendations to Congress designed to cover uninsured Americans and to provide safeguards against catastrophic costs.

This limited approach, decided upon at the association's annual meeting, calls for minimum standards on all health insurance policies sold in the U.S. with appropriate deductibles and coinsurance; government-sponsored benefits for individuals who are unable to assume the cost of their own medical care; catastrophic insurance coverage for illnesses where the economic impact of the illness creates unnecessary hardship, and a national program based on these principles which could be administered at the state level subject to federal guidelines.

In the coming year, the AMA will also actively oppose mandatory second opinions or financial penalties imposed by insurers for failure to get a second opinion. In cases where a second opinion is required, the AMA strongly advises that it should be without cost to the patient and should allow the patient to choose any physician for a second opinion.

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the benefit beat

Clopay offers a payroll deduction stock plan

The Clopay Corp. of Cincinnati, Ohio, is offering its 1,600 employes a stock purchase plan under which workers can purchase each month up to $100 worth of stock through payroll deductions.

The plan calls for the corporation to handle stock brokerage fees and related costs, said Matt MacFadden, director of employe relations for the home products manufacturer. Merrill Lynch, Pierce, Fenner & Smith Inc. will administer the employe stock ownership plan (ESOP) and will purchase Clopay stock on the open market for workers' individual accounts.

Employes will have the option of leaving the ESOP any time they wish and once the account has been opened, employes will be able to trade the Clopay shares in for the purchase of other stocks, said Mr. MacFadden.

So far, no employes have committed themselves to the plan, but Mr. MacFadden said the forms inviting employes to join were only sent out Dec. 21 and workers have until Jan. 15 to return them. Based on past experience, Merrill Lynch projects that between 5% and 8% of the employes will participate, "but we think we'll do better than that," Mr. MacFadden said.

New life plan

The Metropolitan Sanitary District of Chicago awarded its life insurance contract for 2,500 workers to Great Western Life Assurance Co. of Canada as the low bidder among nine companies responding to the district's first workers call for bids. The new contract provides lower premiums to workers who want more than the $2,000 of life insurance paid for by the district than the previous contract with Crown Life, also of Canada.

Under the new program, premiums range from 14 cents per $1,000 of insurance for employes under 30 to $3.61 per $1,000 of insurance for workers 70 to 75 years of age, said personnel manager Don Morrison. Previously, employes under 30 paid 20 cents per $1,000 and those 70 to 75 paid $5.08 for each $1,000 of insurance.

Workers now can also purchase up to $25,000 worth of life insurance without providing evidence of insurability.

The district bid its insurance to be in strict compliance with state law requiring public agencies to do business by seeking public bids, Mr. Morrison said. Previously, the district accepted proposals from various insurers and negotiated coverage using a clause in the law exempting matters considered "too unique" from the bidding requirement.

Improved benefits

In improving its benefits package for 32,000 management and vocational workers, Bell Telephone of Pa. tried to contain medical costs by adding coverage for second opinions on surgery and for out-patient surgery.

The second opinion plan is voluntary, but Bell hopes to improve its effectiveness by educating employes about second surgical opinions through a movie the company is filming.

The medical plan was also improved last August to cover pap smears and provide 90% payment of the cost of a private room when semi-private rooms are unavailable.

A maternity plan was instituted, providing time off with pay after delivery. Workers with six months to two years of service receive half pay for six weeks; employes with two to five years of service get full pay for four weeks, and those with more than five years of service get full pay for six weeks plus full payment of the health insurance premium for the month of delivery.

Long term disability coverage was added for vocational, nonmanagement employes with a 50% of pay benefit paid after 52 weeks of accident and sickness benefits expire. But other benefit payments such as Social Security, workers compensation and pension payments are included in calculating the 50% benefit.

Orthodontia was added as a covered procedure in the dental plan with the maximum benefit set at $500 per case for employes and dependents under age 19. Gum surgery was also added to the plan that pays 50% of usual, customary and reasonable charges based on fee schedules in four areas.

Union starts HMO

District Council 37 of the State, County and Municipal Employes Assn., which represents New York City's civil service workers, is offering its own prepaid HMO plan to about 2,300 members and their families who reside in Manhattan.

Called DC-37 Med-Plan, the program covers doctor's visits, X-rays, lab tests, immunization and allergy tests, physiotherapy, well baby care, ambulance service and payment for appliance and psychiatric care in hospitals. Members can also purchase supplemental hospitalization benefits through the program for a $110 annual premium to cover 120 days stay while their city-paid basic Blue Cross covers only 21 days.

The union is offering the plan as an alternative to Group Health Insurance Inc. (GHI) and Health Insurance Plan Inc. (HIP), two current providers of health care benefits for city workers along with a Blue Cross basic health plan.

The New York University medical faculty will staff the union's facility assigned patients at first, but members will be allowed to change physicians at a later date. If the program is successful, the union plans to establish treatment facilities in all five boroughs.

•

Benefit beat keeps insurance and employe benefit managers up-to-date on what other companies are doing and informed of current developments in the employe benefit field. We'd like to know if you've made any changes. Write Kathryn J. McIntyre, Business Insurance, 740 N. Rush St., Chicago, Ill. 60611 or call 312-649-5286.

Buyers shun young N.Y. insurance free trade zone

By ELLIS SIMON

NEW YORK—After almost four months in operation, New York's insurance free trade zone, touted as a way to stem the flow of premium dollars out of the state and create new jobs, has yet to generate any new business for most insurers holding free trade zone licenses.

Only American International Group, principal backer of the free trade zone, has written free zone business to any significant degree. Other licensees contacted by *Business Insurance* reported little or no activity.

To date, AIG has written about $3 million in free zone business, reported vp John Johnstone. The business, he said, was split about evenly between the two classes of free zone business: risks generating $100,000 or more in annual premiums on a single line, and unusual or hard-to-place risks listed in the state insurance department free zone regulations.

Free zone risks can be written without prior regulatory approval on rate and form.

AIG's free zone accounts have included some major supermarket chains and a real estate organization. The ability to tailor a policy form to meet the insured's needs was a key factor in attracting the business, Mr. Johnstone said.

"If we didn't have the free trade zone, I don't know if we could have written the business. I think a lot of this would have otherwise gravitated to London," he said.

AIG intends to expand its free zone activities, activating this year Landmark Insurance Co., a California-domiciled company that recently obtained a free trade zone license. The company will only be licensed in New York and California and will operate as surplus lines insurer for other states, Mr. Johnstone said.

Other free zone insurers have not been as successful. "To my knowledge, it's been a big zero," said Richard Whynot, senior vp at Commercial Union group. Although a few general inquiries were made at first, there has been no serious interest among buyers, he said.

Officials at Continental Insurance Cos., Utica Mutual and the Atlantic Cos. also reported little or no free zone business. Sterling Chapman, assistant vp with The Home Insurance Co., said although his firm holds a free zone license, it hasn't intended to actively seek free zone business until early this year.

INA, like AIG, promoted the free trade zone but has yet to receive its first free trade zone premium dollar. Of five trade zone submissions to INA, three weren't eligible and the remaining two could have been written under existing rates and forms, said Bernard Buge, executive vp of INA Special Risks.

Ideal Mutual Insurance Co. president Edward Lalley offered free zone coverages to several customers, but they chose to accept conventional policies instead. To date, the firm has not written any free zone business.

Despite poor showings to date by most insurers holding free zone licenses, company officials are optimistic about the future of free zone operations. They simply attribute the slow start to soft market conditions, confusion caused by the still-in-formation New York Insurance Exchange and a general lack of knowledge about the free trade zone.

"The market's been so loose that there haven't been a lot of companies needing to go to the free zone for coverage," said Commercial Union's Mr. Whynot.

"It may still be too premature for the free zone to generate much business," said INA's Mr. Buge. Producers are still undergoing a learning process about the free zone, he added, predicting that the free zone will probably attract many exotic risks. "Going to a free zone company is much simpler than going through an excess and surplus broker," he observed.

Producers have overlooked the tax advantages of placing business in the free zone, Mr. Whynot noted. New York doesn't tax premiums on out-of-state risks insured in the free zone.

A Continental spokesman predicted that once operations on the New York Insurance Exchange begin, both the free zone and insurance exchange will write a fair amount of business. The insurance exchange is conceived as a syndicate market writing reinsurance, foreign risks and surplus lines risks that have been rejected by free zone companies.

Risk managers contacted by *Business Insurance* agreed with insurers on why the free trade zone has not taken off. "It's a market to help those who need help, but in soft markets like this, who needs help?" asked Paul Goldschmidt, insurance manager at Philip Morris Inc.

Risk managers might feel they need to know more about both the free zone and the insurance exchange and are waiting until the exchange takes a more definitive form, suggested Bankers Trust vp Burton Carbino.

"The free trade zone is no different from any other surplus lines facility and the opportunity for using surplus lines is not that great," he added. Insureds who use surplus markets have built relationships with brokers and markets. They don't want to jeopardize those markets at this stage by dealing with the free trade zone, Mr. Carbino suggested.

A key selling point for enacting the legislation creating the free trade zone was its economic impact. A memorandum released by Governor Hugh Carey's economic affairs cabinet predicted that between 678 and 1,017 new jobs would eventually be generated by the free zone, based on a ratio of nine jobs for every $1 million in new standard premium.

Based on the $3 million in new premium known to have been written to date, that means the free zone has only created about 27 new jobs. ■

Agency acquired

American National General Agencies Inc., a managing general agency that is part of Sperry and Hutchinson Co.'s insurance services division, purchased the High Country Corp. of Denver.

errors & omissions

• Insurance industry sources expect the commercial insurance market to turn sour after 1979 because of the strong downward pressure on rates while inflation simultaneously increases the cost of settling claims. Due to a typographical error the year was stated as 1977 in the Dec. 25 issue.

How will a captive perform for you?

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Ignoring any of the variables can cause big problems. For instance, a group of teaching hospitals recently found that its proposed captive could not arrange needed excess coverage from reinsurers. Johnson & Higgins was then invited to study the problem and spotted the organizational flaw. The coverage was soon obtained.

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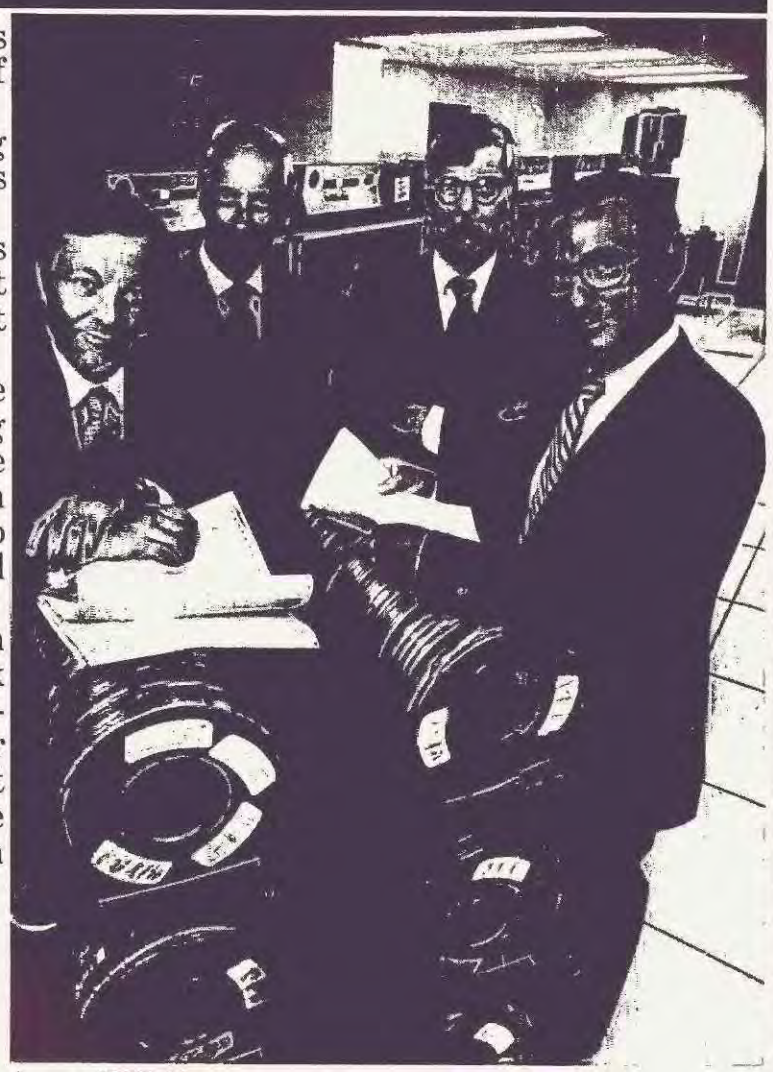

A group of J&H risk management specialists in captive funding: Richard J. Rice, New York; Patrick J. T. Stephenson, Bermuda; Roger Thomas, Los Angeles; and George H. Shattuck, Jr., Boston.

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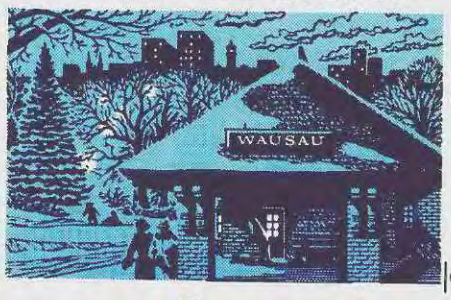

Wausau Insurance Companies
Employers Insurance of Wausau

A&A explores alternatives

N.Y. stockbrokers consider captive for fidelity bonds

By REBECCA A. FANNIN

NEW YORK—Stockbrokers on the New York Stock Exchange want to cut the cost and increase the availability of fidelity bond insurance, possibly by starting a captive insurance company.

Member firms of the exchange have retained Alexander & Alexander Inc. to study the feasibility of creating a captive insurer for them, as well as the effects on insurance costs of higher deductibles and using other risk funding mechanisms.

Also under consideration are better loss prevention programs and an association program for the member firms, using a single insurance company or syndicate insurers for primary or excess insurance.

The 97 member firms financing the study are seeking alternatives because fidelity bond insurance premiums have risen dramatically and are continuing to rise even though loss experience has improved. In addition, fidelity bond coverage has been severely restricted to cover only fraudulent acts where there is financial gain, said Albert D. Hetrick, account executive at A&A.

Two years ago, the New York Stock Exchange members formed an industry committee on insurance to address these problems. It first tried to persuade the Surety Assn., which advises insurers on fidelity bonds, to withdraw the exclusion for fraudulent acts.

Although that effort failed, since then the market has eased in other ways. Member firms who were unable to obtain fidelity bond coverage can now purchase it, according to Mr. Hetrick. Likewise, their loss experience has improved to a loss ratio of 41% in both 1976 and 1977 from a ratio of 86% in 1974.

This year, the Surety Assn. is even recommending that insurers reduce insurance premiums for stockbroker's fidelity bonds by 24%. Previously, stockbrokers were lumped in with banks, whose loss experience has not been as favorable as the brokers', according to Donald Seimer, senior interpretive specialist in rules and interpretations for the exchange.

These changes put the stockbrokers in a position of greater strength in studying alternatives, said A&A's Mr. Hetrick.

"Before, the member firms had to act out of necessity because coverage was unavailable for some, but now they can work to reduce costs on a long term basis," Mr. Hetrick explained.

The feasibility study should be completed by mid-year according to Mr. Hetrick. Meanwhile, A&A plans to collect information from the exchange firms on their claims, losses and payments for fidelity insurance over the last several years. Data on related lines of insurance, including mail loss insurance, will be gathered.

A&A will also try to isolate factors contributing to particularly good or poor loss experience, review loss control practices and suggest how to upgrade loss prevention programs.

As information from the stockbrokers is still being collected, neither A&A nor the stock exchange insurance committee knows which risk management alternative will be chosen to reduce costs and expand capacity.

A&A has offered some observations in its preliminary explorations, however, on how brokers' problems could be solved in certain situations.

If the claims are low in frequency but high severity, large amounts of risk would have to be ceded to excess and reinsurance markets, A&A noted. Also A&A said, it is unlikely that overall capacity for fidelity bonding would increase materially for several years, but a modest start could be made toward building a permanent long term fund for reserves to cover the exposure.

If the problem is high claims frequency but low loss per occurrence, A&A pointed out that loss control programs might help reduce claims. The broker also suggested increased deductibles could be instituted to absorb losses and reduce premiums.

If both types of loss histories emerge as problems, then perhaps an association designed program or a captive insurance company could be used in conjunction with the excess and reinsurance markets, A&A said.

A&A was selected for the study, according to the New York Stock Exchange, from a field of seven consultants ranging from insurance brokers doing extensive business with member firms and experienced in organizing captives to insurance consulting firms not engaged in the broking business.

"Inasmuch as A&A is not a major factor with member firms, but is the world's second largest insurance broker with extensive experience in organizing captives, the (insurance) committee felt that this firm offered a desirable combination of qualifications for this study," said a memorandum to stock exchange members from the insurance committee.

The stock exchange committee was also attracted to A&A's "broad diversity of operations and the use of specialized divisions." ■

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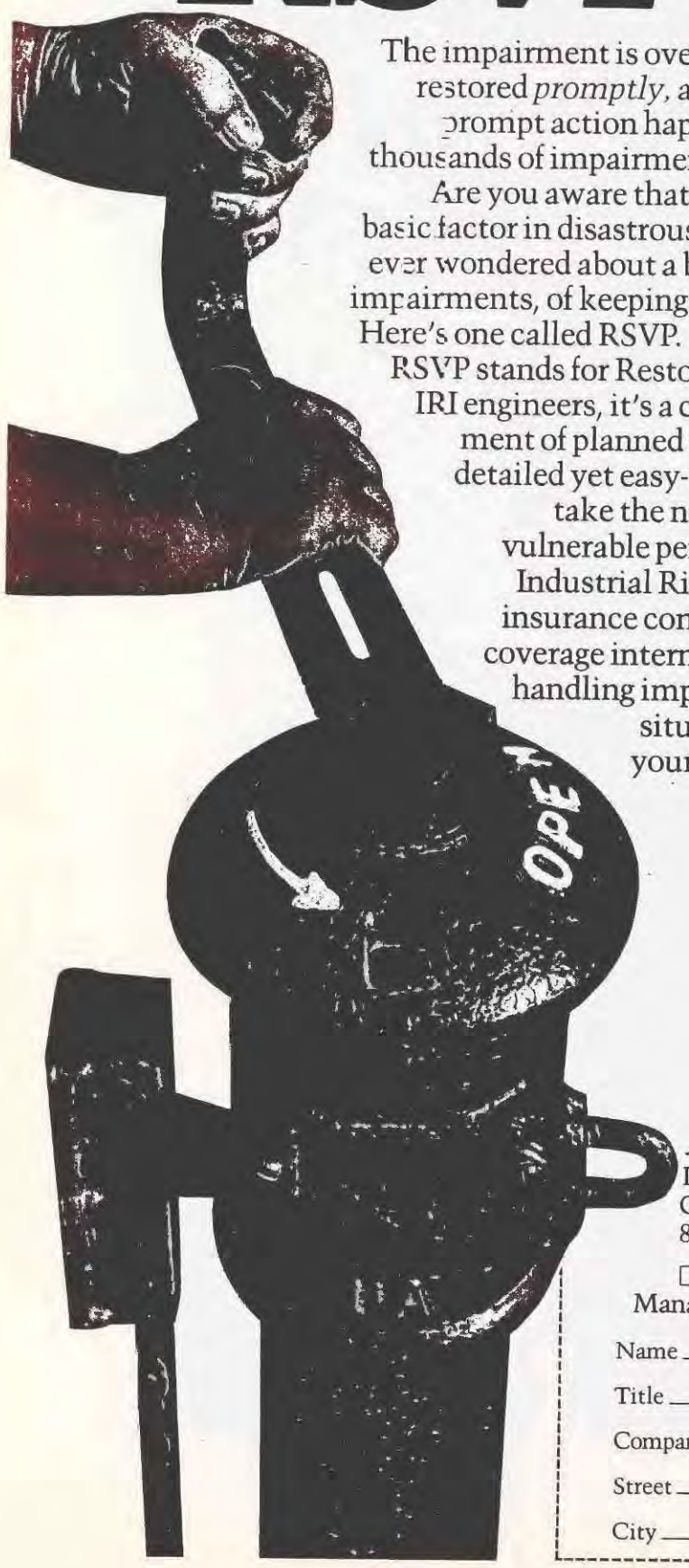

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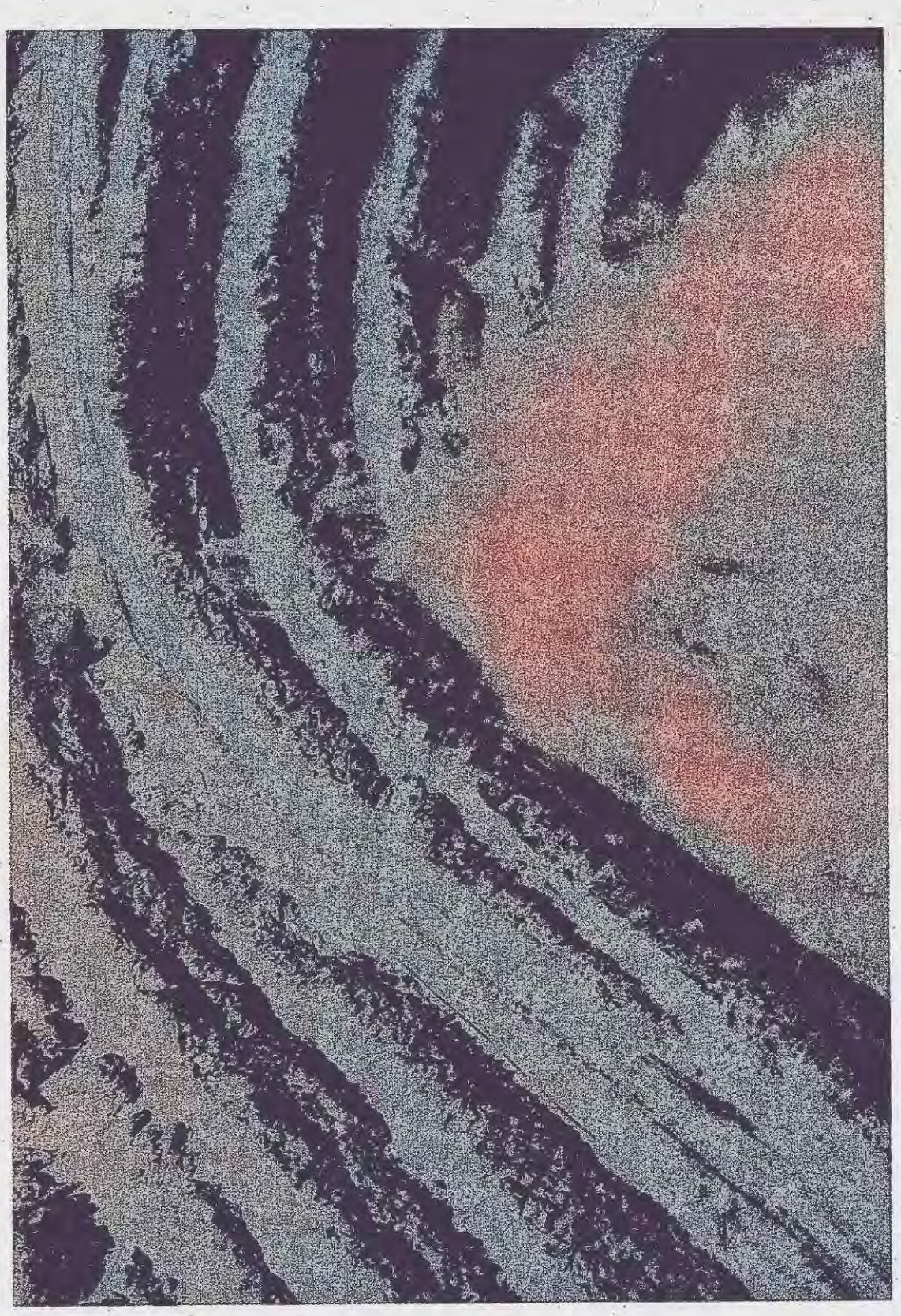

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At first glance, the photo at the left may appear to be an abstract form. Actually, it's an aerial photo depicting a portion of the open pit at Texasgulf's Kidd Creek mine in Timmins, Ontario.

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If you'd like to arrange to view *We look, but do we see?*, telephone your nearest Allendale representative or Michael C. McIntyre at (401) 275-4035.

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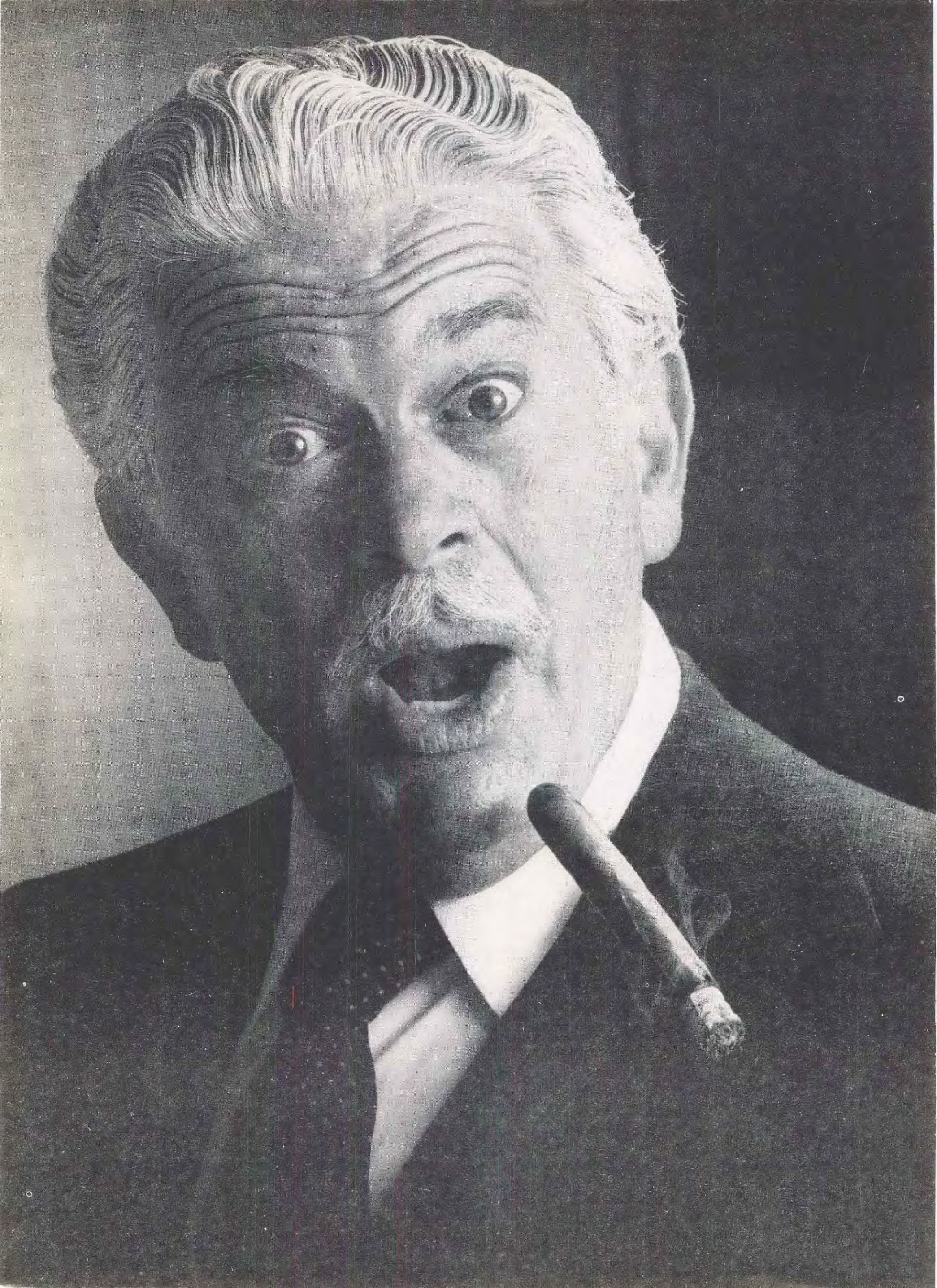

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editorial opinions

Who says nothing changes?

ALTERNATIVE RISK FUNDING techniques are becoming well entrenched. When do they cease being "alternatives?" At some point, risk retention may well become a primary method of handling risk, much like the textbooks have preached for several years. Some consultants have long advocated insurance purchases only for residual risks that can't be managed any other way.

Captive insurance companies, too, are on their way to becoming primary methods of funding future losses.

At one time, not so long ago, insurance underwriters looked warily upon captives and self-insurance as threatening devices designed to undercut insurers and reduce the premium flow available to them. It is, in fact, not uncommon for us to read speeches and press releases even now containing dire warnings of financial disaster for "bedpan mutuals" as the early hospital and physician malpractice captives were dubbed. Insurers are less frequently but no less audibly protesting that self-insurance isn't for everybody, and that it may be harmful to your company's health.

But the insurance industry has energetically responded to customers' demands, commendably, establishing and expanding fee-based services available to companies using captives and self-insurance and needing administrative help. Service operations in evidence at only a few companies several years ago have become de rigueur for more than a dozen major insurers now.

▪ People who've been in the insurance business (or insurance-related business, including risk management and the brokerage business) have often said nothing ever changes in the insurance industry. Nothing could be farther from the truth. That the insurance industry can match the market's demand for specialized services, restructuring the way commercial insurance is bought and sold in the space of several years, is testimony to the basic health and adaptability of the industry. Brokers and independent service organizations have to be included in this insurance industry classification, because they've played a key role in the shift to services-for-fees and the evolution of risk management.

Whether the captive insurance company movement is headed into a slough is a question that will only be answered over the next year or two. From our vantage point, though, it appears that if single corporations move more slowly to establish captives, there's another facet of the business that will pick up the slack: namely, groups of companies establishing a captive in order to underwrite each others' risks. Called by many names—association captives, group captives, multiple-owner insurance companies—these underwriting vehicles appear to provide the best of all worlds to firms not large enough individually to reap the profits of this type of vertical integration.

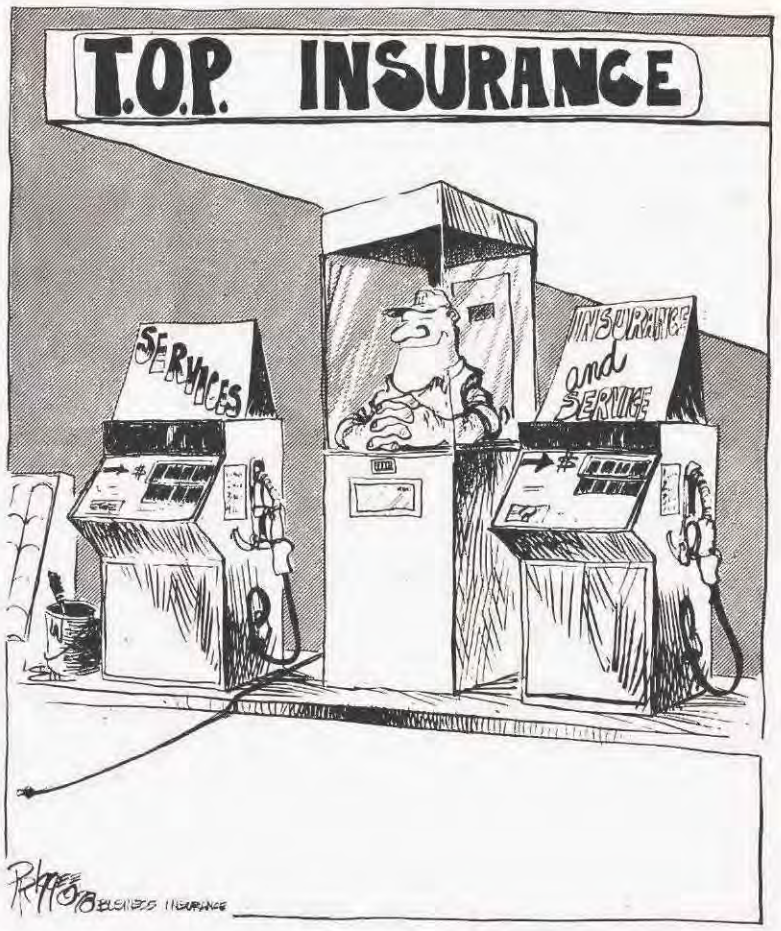
▪ One of the latest fast-moving developments is the trend toward state and city government risk-sharing pools. Associate editor Jerry Geisel reports in a story in this issue that joint underwriting vehicles have been established (or are being considered) for cities in Florida, Alabama, Kentucky, Illinois, Wisconsin and New Hampshire, among other places. Jerry noted after completing his reporting that he could have spent days gathering information in many other states where similar moves are underway. The overview he provides is a microcosm of a phenomenon taking place nationally, and one we will watch closely throughout this year.

These "alternatives" too will become entrenched and will alter the face of commercial insurance, forcing traditional brokers and insurers to accept new ways of dealing with old problems.

Looking back over the year just past, developments in the brokerage industry and the underwriting business internationally make it obvious 1978 is a milestone in altering for future years the way insurance is bought, sold and underwritten. Some of the effects won't be evident for years to come. For example, it seems plausible that major shakeups in the brokerage business will occur over the next year or two, as a result of the remarkably innovative links established between London and U.S. firms.

New York's free trade zone, the insurance exchange and more enabling legislation for captive insurance companies add up to major impact events.

We're enthusiastic about the news that will emerge during 1979 on the heels of an eventful 1978.



letters

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Retro factors

To the editor: Re: article on workers compensation retro development factors, Nov. 27, 1978. It would appear that we are now entering a new phase in insurance seller-customer relations, a phase in which the buyer finally will have some real impact on the product's character. How the insurance industry, if there is such an animal, will take this is going to be fascinating.

We should differentiate between the punitive damages issue and the RDF issue. With RDF issue, what buyers fought was pricing and cash flow and the buyers who did fight had a reasonable alternative, self-insured workers compensation. Also, only a limited segment of insurance purchasers were affected.

By contrast, the punitive damages issue was essentially a matter of a severe and uncertain coverage restriction, and the alternative (self-insured liability) was much more risky and less reasonable for a large section of the participants (virtually all purchasers of such coverage).

The populations differed, as did the issues, but in both cases the "industry" moved. For buyers, 1978 should be viewed as instructive, to say the least. Perhaps we can do more good for ourselves than we thought possible heretofore.

Robert Field
Insurance administrator, Rapistan Inc., Grand Rapids, Mich.

Dental plans

To the editor: Please note an error in your article of Dec. 11, 1978 entitled, "More Employes Are Switching to Self-funding."

You mention in the latter part of the article a number of insurance carriers from whom dental insurance is bought. Missing from this listing is the Delta Dental Plans Assn., the largest carrier of dental benefits in the country.

According to a chart we've compiled, Delta Dental had 6,785 programs in force as of year-end 1977, covering over 4.4 million employes, and with 11.3 million eligible employes, compared to the second largest dental insurer, Aetna Life & Casualty, with 4,337 plans covering just under two million employes. In 1977 alone, Delta Dental installed 999 new programs covering 86,035 employes and 630,638 eligibles. These were dental care plans written separately, not as part of major medical or other

Continued on page 86

business insurance

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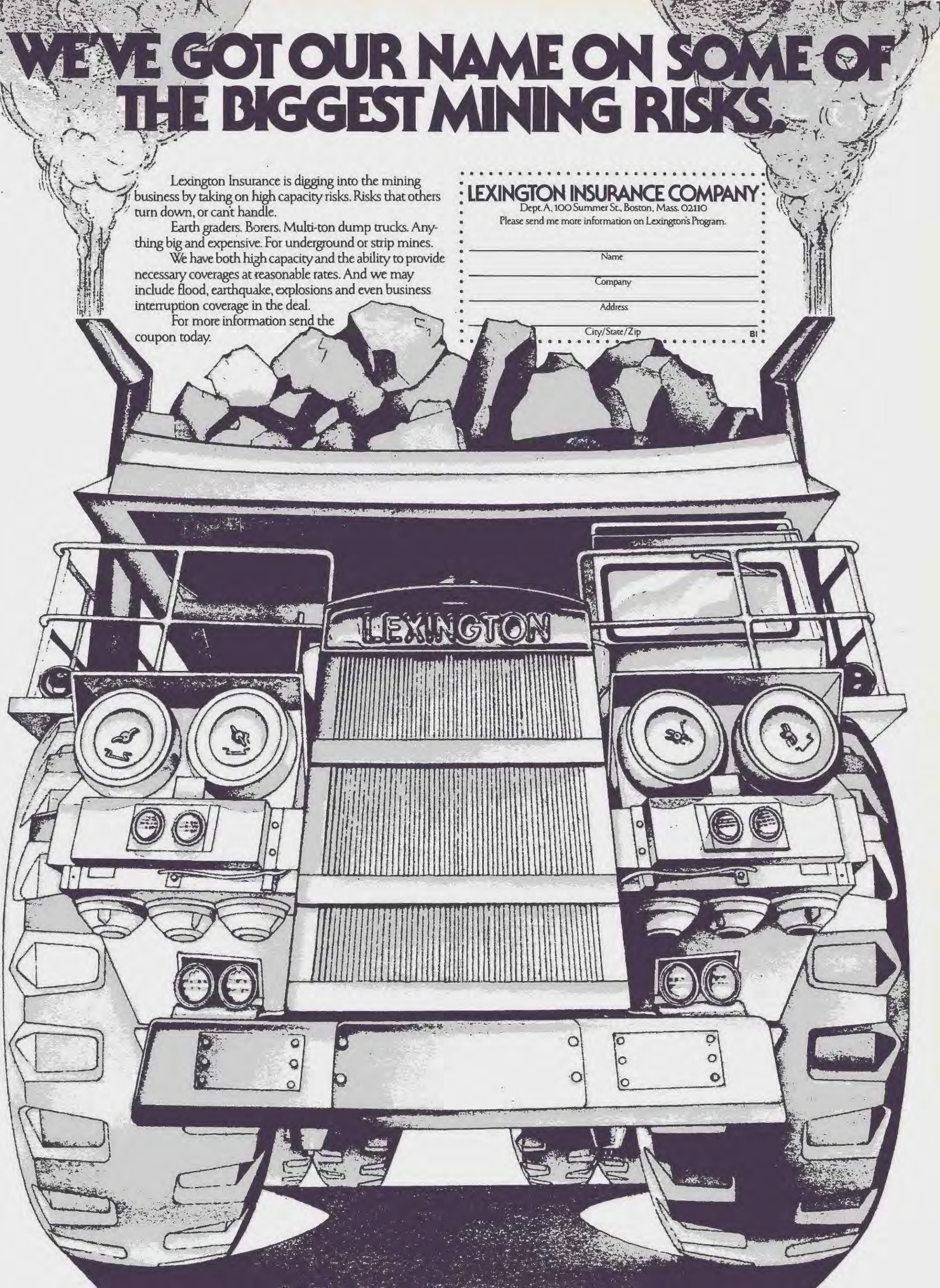

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Captive & Self-Insurance Review

Insurers target self-insurers, captives; establish units to peddle service wares

By REBECCA A. FANNIN

NEW YORK—Insurers are shedding their reluctance to sell unbundled services to large self-insurers and captives and are actively pursuing the market.

Indeed, during 1978 five insurers set up special divisions to sell loss control, claims handling and underwriting services to risk managers with innovative insurance programs.

Insurers had resisted supplying services, not wanting to encourage self-insurance and reduce premium income. But they've decided clearly that unconventional types of insurance are not just a fad and that they must cater to self-insurers to remain competitive.

"Some insurance companies have resisted selling services," said Robert J. Cymbala, principal for management consultants Booz Allen & Hamilton. "In fact, a major Hartford company did, because they feared the move might reduce their premium income. They didn't understand that offering these services could produce higher profits than underwriting."

F.A. Mina, left, says 2½ years of study preceded the recent formation of Home Group Risk Management. John C. Morrison, of INA Special Risks, right, directs a unit that already handles $500 million net of reinsurance business for captives.

But now insurers are rapidly following the lead of American International Group, which set up AIG Risk Management Inc. three years ago, and Insurance Co. of North America, which established INA Special Risks 18 months ago.

As the forerunners in combining loss control, claims handling and underwriting services in one department to cater to self-insurers, AIG and INA have the most extensive risk service divisions. Kemper Insurance Co. was also a forerunner with its NATLSCO division.

The Home Insurance Co., St. Paul Fire & Marine Insurance Co., Fireman's Fund Insurance Co., Continental Insurance Co. and Reliance Insurance Co. set up services divisions in 1978.

Other insurers that preceded this swarm of activity were Aetna Life & Casualty, which created Aetna Technical Services in 1973, and Commercial Union Insurance Co. whose service division became active mid-1976.

Travelers Insurance Co. also offers self-insurers and captives the same services as conventionally insured programs, but has not created a separate special accounts division for servicing self-insureds.

Insurers are aggressively selling their new services and expect high growth rates in the future. But their divisions won't become predominant over underwriting, directors of the risk management service divisions agreed.

Besides vigorously competing for the booming self-insured service business among themselves, insurers are also battling brokers for a share of the market.

More of the business currently

Continued on page 22

Cities, counties dive into risk sharing pools

By JERRY GEISEL

WASHINGTON—In 1974, the Texas Municipal League made waves in public insurance circles by establishing the first major fund for cities in the state to collectively self-insure their workers compensation.

Five years later, the waves keep rolling, not just in Texas where city membership in the fund has quadrupled to more than 400, but all around the country where cities and counties are flexing their public muscle by setting up collective pools to cover their liability risks.

"Governmental pools keep popping up so fast it is hard to keep track of them all," says John Hetrick, executive vp of Penn General Services Corp., a leading provider of risk management services to self-insured pools.

In New England, the New Hampshire Municipal Assn. this month began sponsoring a pool that will shave workers compensation costs by as much as 25% for the 20 communities participating.

Sister state Maine's pool, sponsored by the Maine Municipal Assn. in Augusta, went into operation in November and association officials believe the fund will eventually attract 250 cities with annual collective premiums of $7 million.

Farther south, the Kentucky Municipal League's six-month-old workers compensation pool already has saved the 80 participating counties and cities $200,000. League executive director R. Michael Amyx asserts that some participants will be able to slash their workers compensation bills 40%.

While most municipal pools are set up to insure workers compensation—usually a municipality's biggest insurance expense—some public entities are beginning to broaden their liability horizons.

In Illinois, for example, the Northwest Municipal Conference

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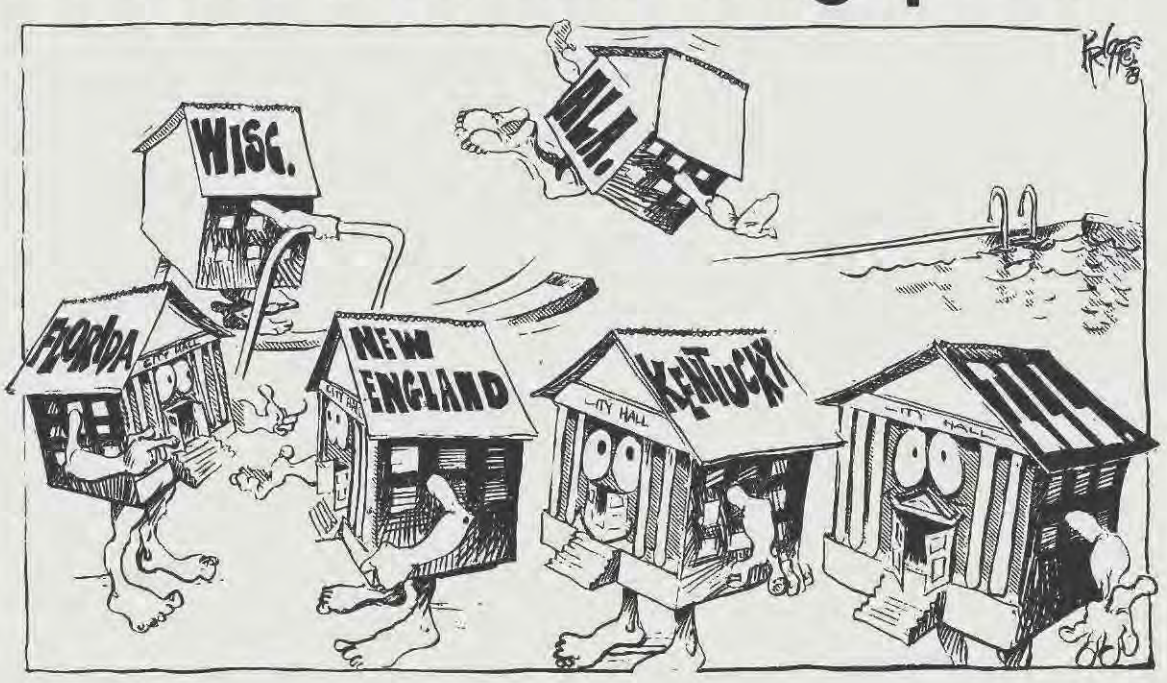

IRS spotty on captive deductions, observers say

CHICAGO—The Internal Revenue Service is only sporadically enforcing its prohibition on business expense tax deductions for premiums paid to captive insurance companies, say industry observers.

This could reflect a lack of diligence on the part of field auditors, a failure by the IRS to see through fronting arrangements or an IRS decision not to challenge tax deductions for premiums paid by the parent company to a captive that also underwrites unrelated risks.

Meanwhile, corporations keep forming new captives to insure their risks. But it's debated whether captive formations are taking place at the same harried pace as before issuance of the infamous 1977 revenue ruling eliminating tax deductions for premiums paid to captive insurers. Current estimates place the number of captive insurers at 800 to 900, with over 700 of them in Bermuda.

One observer sees a leveling off of captive formations while another predicts a forthcoming surge of activity. Still another contends corporations are dropping back from forming captives, disenchanted with the idea because of IRS disdain for captives and improved commercial insurance availability.

These are the observations of 20 captive experts interviewed by *Business Insurance*. Their observations offer insight to the state of the captive insurance company industry, which for the most part operates in near secrecy in offshore tax havens, eluding governmental and statistical analysis.

This story is based on reporting by Rebecca A. Fannin, John Maes and Ellis Simon. It was written by Kathryn J. McIntyre.

Even IRS challenges to tax deductions for premiums paid to captives are difficult to document. "It's hard to learn who is doing anything since this is usually out of the hands of the risk manager and in the hands of the tax department," complains Thomas Duffield, president of the Captive Insurance Companies Assn.

When corporations fight an IRS challenge in the courts, it becomes a matter of public record. But even the best-informed captive observers lack awareness that at least four court cases have been brought by irritated taxpayers: Ingram Corp. and Toyomenka (U.S.A.) have taken the IRS to court as well as Ford and Carnation Co.

"There have been about two dozen challenges" by the IRS of tax deductions for premiums paid to captives, says Bill A. Yeargan of the Blades Group. He considers that number small, perhaps indicating that few companies are writing off premiums paid to their captives.

Others, however, believe corporations routinely deduct premiums paid to captives, and they think the apparent low number of IRS challenges reflects the uneven application of the prohibition by the IRS.

The IRS, like other bureaucracies, doesn't move with uniform momentum, observes Arthur Deters, executive vp of American Risk Management. "As a result, there are some field agents beating their heads against brick walls where there are legitimate deductions and others who don't challenge deductions that are unlawful under 77-316," the revenue ruling which clearly established the IRS's long standing objection to tax deductions for premiums paid by a parent to its captive insurer.

"The IRS challenges some deductions, but not all," says Richard Rice, vp at Johnson & Higgins.

"The consensus seems to be

Continued on following page

IRS audits spotty . . .

Continued from preceding page
there is not IRS consistency," agree Bob Godfrey and Jim Bass of SCOR Risk Management. Most companies they know of have not been challenged by the IRS for tax deductions for premiums paid to captive insurers. "We've heard of cases where captives writing only 5% to 10% outside business were not challenged by the IRS." One can surmise, they suggest, that the IRS either has not yet worked its way to the captive or the agents auditing the operations overlooked the captive insurers.

Joseph C. Smetana, president of AIG Risk Management, estimates 10% of its clients are being challenged by the IRS for their deductions of captive transactions.

An offshore subsidiary raises IRS interest most, some sources say.

Captive & Self-Insurance

One sure flag to draw an IRS probe is to name the captive insurer after the parent company, warns Blades' Mr. Yeargan. On the other hand, "Where a fronting company is used, the IRS is less likely to challenge the deduction," he suggests. "But if the IRS knew it was really a fronting operation, they'd be challenging more."

Most corporations insuring risks with offshore captive companies use a fronting insurer on casualty lines, experts agree. Workers compensation is most often fronted, because proof of insurance is required by state regulators. Where third parties want insurance certificates, a fronting insurer is also often used. The decision to seek services from an insurer frequently results in choosing to first insure with an insurance company before the risk is transferred to the captive.

The policy issuing company is never a pure front, says Mr. Rice of Johnson & Higgins. Usually the insurance company issuing the policy retains the area of operational loss and cedes the area of uncertainty to the captive, he maintains. But it depends on the individual situation, Mr. Rice adds.

For property insurance or high risk policies such as earthquake and flood insurance, corporations are generally going direct to their captives, observers say. It saves money to pay the 4% excise tax on going directly offshore instead of the fronting fee that can run double that or more, they note.

Only three or four Colorado captives use a fronting company, says Colorado insurance commissioner J. Richard Barnes.

Corporations taking tax deductions for premiums paid to their captives apparently are willing to fight the IRS for their right to do so. "They have a strategy for fighting and they say they will go to litigation if necessary," says an executive at SCOR Risk Management.

Mr. Smetana doesn't know of a single client who has conceded to an IRS challenge of its captive transactions.

"Some are getting into third party business" in hopes of thwarting an IRS challenge to the legitimacy of parent company transactions with the captive, observes C.J. Clarke, vp at The Travelers Insurance Co.

SCOR Risk Management noted one corporation is waiting for its captive to stack up a few years of diversified parent and non-parent business before claiming a tax deduction for premiums paid to its captive.

How much outside business establishes a captive as a legitimate insurer and not a self-insurance mechanism in the eyes of the IRS remains unclear. Mr. Yeargan of Blades is conservative, offering his view that 50% outside risks surely establish a legitimate risk-bearing insurance company.

Assessments of the recent establishment of captives vary considerably among the experts interviewed, ranging from a perceived slowdown in 1978 to increased activity.

Mr. Duffield of CICA thinks captive formation was slower in 1978 than during the previous two years, citing improved commercial insurance markets this year and a negative reaction to the 1977 IRS ruling as reasons for the sluggishness.

Mr. Yeargan of Blades agrees there's been a considerable lull in captive formations since the IRS ruling was announced, "but there seems to be more activity now." Companies probably made plans to start a captive when the insurance markets were still tight and are going ahead with their plans even in the softer market of today. "They know what can happen with rates and they don't want to face that again," he observed.

Peter Densen, president of Alexander & Alexander's Anistics division, agrees captive formation is on the upswing again after a slowdown immediately following the IRS ruling. Corporations now consider the IRS to be on shaky enough legal grounds that the funding alternative is still worth pursuing, he said.

"Captive activity continues to expand," says Mr. Rice of Johnson & Higgins, though he admits he isn't sure why. Corporations are setting up captives without regard for the IRS, he believes. The chief detriment to new captive formation instead is the attractiveness of alternative cash flow programs being developed by insurance companies, he said.

SCOR Risk Management reports captive formations are occurring "on the second level," among companies ranked in the second half of the Fortune 1,000, and smaller. "They are facing growing premiums and they can benefit from a captive like the giants," the firm's experts suggest. Higher interest rates are making corporations look twice at holding onto their money for their own investment gain, they noted.

Among insurance company managers of captive and self-insurance services divisions, there is general agreement that corporations will keep forming captives at about the same pace. But Mr. Clarke at Travelers thinks the pace may slow because the market isn't as tight, while F.A. Mina, vp of Home Group Risk Management, thinks the pace will quicken with inflation and premium increases in lines as workers compensation.

Most sources agree there will be more group-owned captives formed, especially since the IRS approves of premium tax deduction in these arrangements.

Most bullish on captive activity are the insurance regulators in the two states that have passed legislation favoring captive insurance company formation.

Colorado insurance commissioner Mr. Barnes maintains that many corporations were waiting to see how others fared with their captives before starting their own. "The pace will accelerate," he predicts. "They've seen enough experience in the captive field."

Tennessee's assistant insurance commissioner Paul Tidwell is just as enthusiastic. "In the years ahead, in terms of commercial type coverage, I think that's the way it's going to be." Large firms will work their whole concept of risk management around the captive insurance company, he believes. ■

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Bermuda readies rules to enact insurance law

Captive & Self-Insurance

HAMILTON, Bermuda—Captive insurers and captive management companies here will get their first taste of government regulation in the next couple months.

The Bermuda Insurance Act of 1978 takes effect April 1. Captives and insurance intermediaries, such as captive managers, must apply by April 1 for the one year transitional exemption from the law provided by the act or else they will be subject to regulation.

"We want everyone to take the one year exemption for us to set up our regulatory framework," said Bermuda's registrar of companies Shelton Burgess.

The Bermuda Cabinet last month approved the draft of the form for companies and intermediaries to complete to secure the exemption. The legislature is expected to approve it when it meets later this month.

"It's a detailed application form," observed Mr. Burgess. Essentially, it will ask for all the financial and management information that will also be required under the law, only this application is for fact-finding instead of for regulatory action.

The government wants to know where the companies are now in relation to complying with the provisions of the new law.

The form asks the insurer to name the company's principal representative, its approved auditor, actuary, degree of unrelated risks being written, the company's retention, extent of reinsurance, a list of principal reinsurers and if the reinsurance treaties are transacted in Bermuda, to cite a few questions.

"Some of the questions anticipate there will be problem companies among the Bermuda population," Mr. Burgess said. "If they are deficient now under the act, they are asked to explain how and when it will be corrected."

A company, for example, may not maintain adequate capital and surplus to meet the three-to-one underwriting ratio required under the law.

The Cabinet has also approved for legislative action a new draft of the financial regulations implementing the new insurance law. These are the prescribed form and content of financial reports to be filed when a company becomes subject to the law.

The new draft differs more in form than in substance from the draft of regulations circulated by the government last fall, Mr. Burgess said (*BI*, Oct. 16, 1978).

"The concepts have stood up, but the format is easier to read and understand," Mr. Burgess explained. The concept of the regulations, and indeed the new law, is to provide for ongoing surveillance and supervision of the Bermuda insurance industry.

The Minister of Finance has always had the power, also provided by the law, to step in and direct the business of a troubled Bermuda insurer, Mr. Burgess noted. However, the government has had to rely on tips from industry sources to learn of problem companies.

Now, under the new law, the government will have the financial information necessary to know if an insurer is insolvent.

The financial reporting will also give the Bermuda government, and hopefully the public, a clearer picture of the captive insurance industry in Bermuda.

Right now even Mr. Burgess is unsure how many captives operate in Bermuda. Of the 1,000 exempted companies registered in Bermuda, no one knows how many of them are true captive insurers—underwriting only the business of their parent companies—and how many are also underwriting unrelated parties' risks.

The information supplied by companies in compliance with the new law will be strictly confidential, Mr. Burgess stresses. However, it has not yet been determined how much of the statistics compiled from the information about the insurance business in Bermuda may be released. ■

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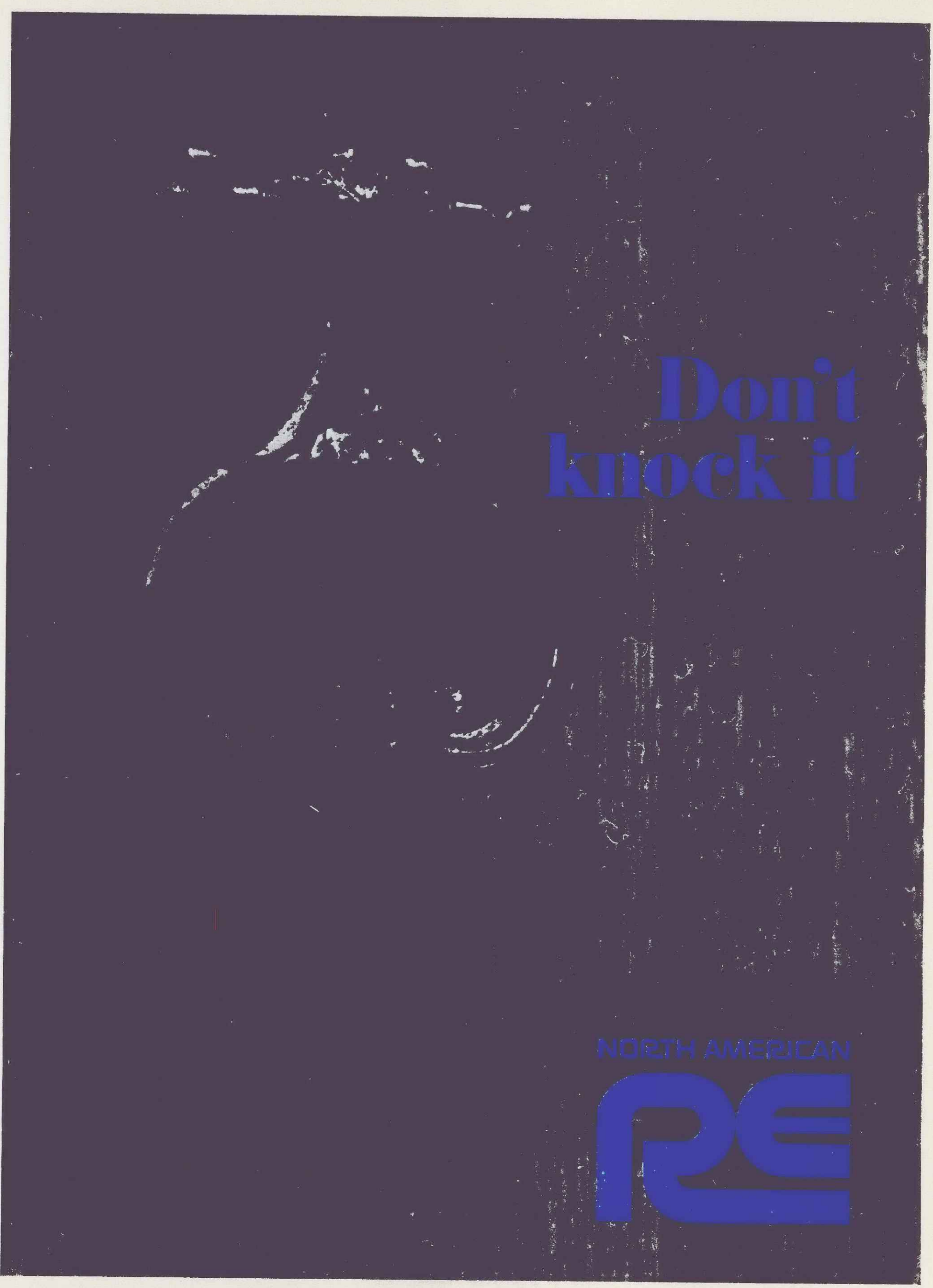
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Preventing the Washington Takeover

Lee R. Meyer, President
Independent Insurance Agents of America, Inc.

This text is an excerption from a recent speech given by Mr. Meyer.

It is apparent that the bedrock issue facing our industry is to demonstrate to the federal government the dependability and sufficiency of the system of insurance regulation that has worked well for over a century at the state level.

First, let's look at ourselves, the agents, who definitely are not without blame with regard to many problems we face today. One thing that agents individually and collectively are doing or discussing is going to the legislative bodies in attempts to solve our problems with the companies, or to legislate restrictions that will impair the ability of insurance companies to do business or threaten their solvency.

I realize that we often do feel as agents that "There oughta be a law," and other agents will find themselves in a position where they are virtually put out of business.

I, for one, am of the opinion that if there is any way whatsoever possible to avoid seeking legislative action, we must use those methods rather than inviting the government into our business. It is bad enough to have to rely on state legislatures, but it is suicide to go to the federal government.

On this particular point we are getting very, very close to the point of no return. When you consider social security, medicare, insurance on loans and mortgages, and other federal programs, it becomes clear that the federal government is already in the insurance business in a big way. In 1960, 25% of all premiums paid in this country were to the federal government. In 1975, that percentage increased to 44%. By 1980, payments to the federal government for insurance premiums will most likely exceed those to the private sector.

The federal government is already competing directly with private insurers in some instances. The federal crop insurance program is a good example, and there is federal legislation currently pending that would expand this program drastically, without giving a role to private insurers that want to write this coverage.

1968 was a good year for government insurance – The Federal Riot Reinsurance Program, The Federal Crime Insurance Program and The National Flood Insurance Program. The National Flood Insurance Program was considered by many as being a model program where government and industry could work together. That was before the latter part of 1977. I am sure all of you are familiar with the take-over of the full administrative responsibilities of the program by the federal insurance administrator with the consent and support of the secretary of HUD.

The history of federal involvement in any industry is one of increasing regulation, where the federal bureaucracy constantly seeks ways to expand its authority.

Changes in the McCarran-Ferguson Act could be a logical starting point for the gradual federal take-over of the regulation of the insurance industry. Federal no-fault similarly could be the launching point for increased federally mandated cost controls in the industry. Bank holding company intrusion would provide an almost monopolistic grasp on our business by people who don't belong in it.

It deeply disturbs us as an association to find that there are certain companies within the insurance industry and certain organizations who appear to be wavering in their historical support for strong state

regulation. From some standpoints, it looks as if some companies may be actively promoting a transition of regulatory authority from the states to the federal government. Possibly they would like to see a federal insolvency fund and relief from prior approval rating laws. Some companies would probably prefer working with one central regulatory body instead of with 51 regulatory authorities. It won't work. Before playing with fire again, the most important question that insurance companies should ask is: "If insurance does become federally regulated, how long could that regulatory authority resist the inherent political pressures that would arise to press for at least some degree of rate regulation?"

Another question which begs for an answer is: "Under federal regulation, or under a dual system of federal and state regulation, would the benefits of the current open and competitive rating system – which we fully support – continue to provide our customers with the same competitive climate that they have come to expect when shopping for insurance? Or would unwarranted regulation do nothing more than increase those same problems at the direct expense of our industry?" We believe the latter is the answer.

It seems to me that the only practical answer to the problem of federal control of our business is to more actively seek solutions at individual state legislative levels to make state insurance departments more responsive to the needs of the insurance-buying public.

We firmly believe that unless individual states provide sufficient funds for proper regulatory activities, the chances are that the states may surrender their historical regulatory functions to the federal government, and ultimately lose their right to tax the insurance industry.

We have got to keep communicating that we support state regulation and taxing of insurance. It is our contention that this is a proper role for the states to assume, and we are firmly convinced that this regulation is more valid at the state level than it would be at the federal level.

Some of our companies are pushing their agents and consumers to the point of no return with the programs and changes they are making today. Many of the decision-makers in our companies probably have never seen the inside of an agent's office and obviously have never had to sell insurance and service a customer.

When insurance companies forget who their customers are and the needs of their policyholders, they will, like in any other business, begin to lose out in the market place.The customer may not always be right, but he is always the customer. Our companies, to a large degree, forget that we have no choice as agents but to cater to the customers'needs as best we can.

I feel that some of the actions and attitudes of the regulatory authorities are hastening the day when the center of the insurance world will be Washington, D.C. The states are closer to the public, more sensitive to its needs, and therefore better able to provide responsive regulation. These needs call for a solvent insurance industry which can provide customers and businesses with the basic financial protection to sustain them in time of loss. State regulation is not and will not be either uniform or fully responsive to all the social and economic needs. The requirements for a densely populated industrial state are vastly different from those of a sparsely populated agricultural state.

The survival of our industry depends, absolutely, on the ability of our companies to make an underwriting profit. States must permit proper rate increases and maintain adequate rates to insure reasonble profitability and continued solvency of insurance companies. The state insurance departments must reject, out of hand, any rate filing that would result in inadequate premiums that jeopardize the solvency of insurance companies. The state regulators, and their departments, must be able to distinguish the difference between an adequate and an inadequate rate. Failure to do so can only damage the solvency of the private property and casualty business and open the gates for increased federal control and regulation.

You and your state and local associations must cooperate with state regulators to develop a climate which will produce underwriting profits for multi-line companies doing business in your state and maintain an open market for the public.

Let me urge all of you to support in every way possible your local, state, and national associations. They will be calling on you for assistance soon in the legislative areas. As insurance professionals, we must not sit idly by while our elected representatives make decisions that will have a drastic effect on the future of our business.

There are many problems that need our attention these days, but I am of the opinion that the greatest threat to the independent agency system and the independent insurance agent's livelihood lies in Washington, D.C.

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Cities, counties dive . . .

Continued from page 13

has set up a pool to cover 15 Chicago suburban communities' workers compensation exposure as well as their property, general and auto liability risks.

The drive toward public self-retention of liability through joint pooling arrangements began in the early 1970s when municipalities around the country started seeing skyrocketing workers compensation premiums.

Some Alabama cities, for example, found their workers compensation premiums doubling. Other cities couldn't find coverage at all and were forced into the state's assigned risk pool where they were slapped with an automatic 8% surcharge.

While premiums climbed, cities and counties charged insurers were doing little to deserve those

Captive & Self-Insurance

extra premium dollars. "What kind of services were cities getting? Zero," said Jerry Bowman, director of research at the Florida League of Cities in Tallahassee.

The twin desires to save public money and get better services fueled the drive by the Kentucky Municipal League and the Kentucky Assn. of Counties to set up a workers compensation pool.

Incorporated in July, the fund gives participating members a 10% reduction from standard manual rates. In addition, after a two-year period, dividends will be paid to members based on their loss experience.

While the initial cost savings are important to financially pressed cities and counties, Mr. Amyx emphasized that the fund's biggest selling card is its individually tailored loss control and safety programs.

Loss control engineers from Hewitt Coleman & Associates Inc., the fund's servicing company, assist members in developing effective safety programs.

Like many other municipal pools, the Kentucky fund pays losses up to $100,000 on a per occurrence basis. Specific excess insurance purchased from Aetna Insurance Co. covers any single loss over $100,000, while aggregate excess coverage, also supplied by Aetna, comes into play once the fund has paid out more than $1 million in claims. Excess insurance costs the fund 11% of its earned premiums.

Right now the fund has a premium flow of $1.2 million, but Mr. Amyx is predicting a $3.2 million annual premium flow by July.

Another new fund, sponsored by the Florida League of Cities, has attracted 71 cities, mainly communities with less than 5,000 population. Director of research Mr. Bowman expects the current premium flow of $3 million to more than double in three years with an eventual potential membership of 200 cities.

Engineers from Risk Management Services of Orlando, Fla., make at least two safety inspections per city each year. In addition, Risk Management Services gives each city an updated safety and claims report monthly.

Like the Kentucky fund, the Florida League of Cities pool covers the first $100,000 of claims on an occurrence basis. Excess insurance provided by Lloyd's of London covers aggregate losses that exceed $1 million or catastrophic losses over $100,000. Excess insurance costs the fund 17% of its premium flow.

So far, the pool has cut the participating members workers compensation costs by $500,000. Mr. Bowman projects that some cities will be slashing workers compensation expenses by 50% due to the fund's dividend program that rewards good loss experience.

The Alabama Assn. of County Commissioners' Self-Insurers Fund has seen its premium flow jump to $1.2 million from $300,000 in 1976, the fund's first year of operation. Forty-nine counties now are in the fund, up from 33 in 1977.

The fund's loss ratio has been running between 41% and 44% during the three years of operation. Because of this "fantastic" loss ratio, the fund now is preparing to distribute $90,000 in dividends to participants, said administrator O.H. Buddy Sharpless.

The dividends coupled with the automatic 15% discount from standard rates translate into big savings. Mobile County, for example, would have had to pay $100,000 for its workers compensation insurance if it purchased coverage from a commercial carrier. However, by opting for membership in the fund, Mobile County received a $15,000 advance discount and will soon be receiving an $18,000 dividend.

Administrator Mr. Sharpless, pointing to the success of the pool, believes the insurance industry has been crying wolf when it says it can't make any money on workers compensation.

In Illinois, 15 Chicago suburbs not only are covering workers compensation in their collective pool, but also are sharing general liability, auto liability and property losses.

Under the program, which began this month, each municipality assumes the first $1,000 of each loss. Above that, the fund covers the next $250,000 of risk. Excess insurance, purchased from several insurers, including Lloyd's of London, will offer an additional $10 million of coverage for property losses and $5 million of protection for the other liability areas.

The Northwest Municipal Pool is funded by members who pay $1.88 per $100 of receipts. This contribution formula was based on a study performed for the conference by consultants Risk Planning Group of Darien, Conn. It found a correlation between losses and gross revenues in each of the communities that range in size from 9,500 to about 45,000 people, said league executive director William Muhlenfeld.

The pool contracts with Gallagher Bassett Insurance Service, the self-insurance service affiliate of Arthur J. Gallagher & Co. of Rolling Meadows, Ill., for loss control services and for excess insurance placement.

Currently, the suburbs have contributed $1.5 million to the pool, but Mr. Muhlenfeld expects a major infusion of contributions in May when another six communities are expected to opt for pooling.

Pools aren't limited to cities and counties. In California consultants Warren, McVeigh & Griffin, pioneers in the development of West Coast municipal pools, have recommended that the 300-member Assn. of California Water Agencies pool their liability risks.

In Wisconsin, Warren, McVeigh is exploring the feasibility for governmental entities in Rock County, which includes the cities of Janesville and Beloit, to pool all their liability risks. Elsewhere in the state, 20 urban transit districts are considering a pooling arrangement to cover motor vehicle liability.

Dave Warren of Warren, McVeigh & Griffin envisions continued expansion of municipal pools around the country. "It is a sound concept because it gives professional risk management to governmental entities that often were not receiving any." ■

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Risk services . . .

Continued from page 13

flows to the brokers because they are more accustomed to providing the services to self-insureds, said Mr. Cymbala, who recently completed a study about how insurance companies will change as a result of growth in the service area.

But this trend will reverse in the future, as insurers capture a much larger share of the services market, Mr. Cymbala predicted.

The growth of such services in insurance companies might also depend on insurance availability, he noted. For instance, if the excess and surplus lines markets tighten, he said then those insurers able to arrange for excess coverage might also stipulate that the client purchase services from that insurer.

Adding self-insured services to an insurer's business has not

Captive & Self-Insurance

caused a dramatic change for most insurers. They traditionally have offered such services to conventionally insured programs. So most are merely extending the same services to self-insureds on a fee basis.

Most insurers limit their offerings to claims handling, claims information and loss prevention services. They include Aetna's Technical Services, Kemper's NATLSCO, Commercial Union's Risk Management Inc. and St. Paul's Risk Services Inc. But a few of the risk management service divisions have expanded further into captive management, captive feasibility studies and have incorporated special underwriting services into the separate service centers.

Commercial Union and St. Paul underwrite special programs for self-insureds, but utilize the underwriting staffs of the parent company rather than setting aside underwriters to exclusively provide such programs as excess insurance for self-insureds, fronts for captives, retrospective rating plans or other cash flow programs.

Travelers provides claims handling and loss prevention as well as

Photo: AIG

AIG Risk Management under president Joseph Smetana will do a captive feasibility study.

underwriting services to self-insureds, but these functions also have not been segregated from the mainstream of conventional underwriting.

AIG is the only insurer currently managing captives and providing captive feasibility studies. INA manages captives through its INA International Co. Ltd. in Bermuda separate from INA's Special Risks, but does not sell consulting services to captives. INA's Special Risk division serves only domestic risks.

Several insurers, however, plan to branch out into captive management and captive feasibility studies, including St. Paul Risk Services, Continental Special Risk Underwriters and Home Group Risk Management.

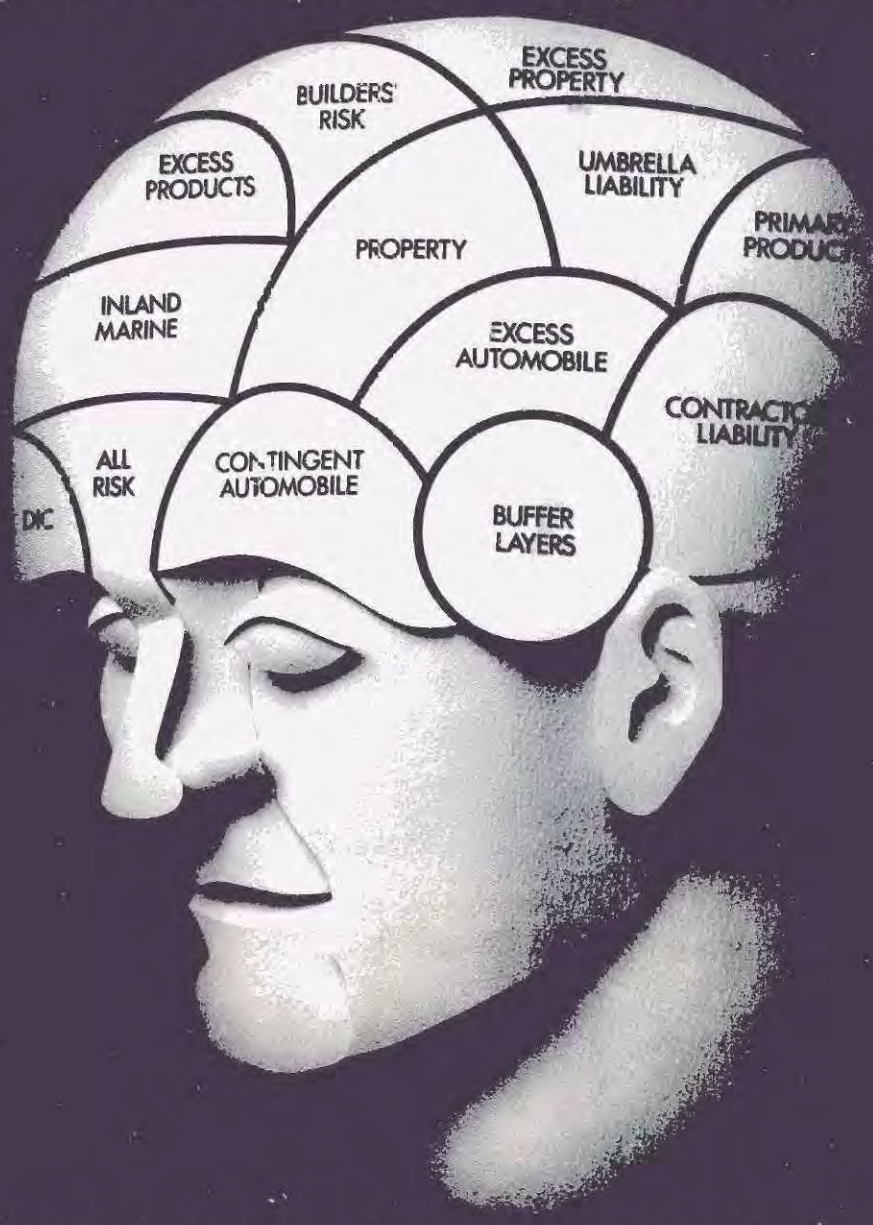
But many of the insurers view captive management and captive consulting as a conflict of interest to providing insurance services to captives and to underwriting.

"It might be a conflict of interest for us to advise companies that are considering captives and then turn around and offer these captives services," explained Richard L. Whynot, president of Commercial Union Risk Management Inc. Consultants and brokers should sell captive feasibility studies and captive management, he added.

"Offering such services would

Continued on page 24

Thoughtful Answers to Complex Questions



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Rita Garcia
Risk Manager
Castle & Cooke, Inc.

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"It's obvious why we concentrate a substantial amount of our self insurance in the area of workers' comp. In agriculture, fishery operations and food processing – three of our major fields – the possibility of injury is often present. And in the many states where we operate, regulations are steadily increasing the level of disability payments.

"Since 1968, when Castle & Cooke started self insuring, we've achieved better financial control over the entire situation. And ESIS shares the credit for that. Their people are on the scene in every state. And with a working knowledge of each state's laws and methods, they've been particularly helpful in claims investigation and handling.

"ESIS' loss reports, on a state-by-state basis, help us pinpoint potential problem spots...and serve as an accurate tool in assessing loss predictability. This gives us a good handle on determining reserve levels from year to year. They've also contributed to safety consulting in many of our plants across the country."

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Risk services . . .

Continued from page 22

be in direct competition with insurance," suggested Robertson Mackay, president of Aetna Technical Services.

Travelers, Reliance and Kemper also do not expect to get involved in captive management or captive feasibility studies.

Most of the insurers sell their services individually, a procedure known as unbundling. Home Group Risk Management, however, only sells its services as a package and Continental Special Risk Underwriters prefers to sell

Captive & Self-Insurance

them as a whole. Continental's only firm stipulation is that if it writes an excess policy for a large self-insurer, then Underwriters Adjusting Co. must handle the claims.

The insurers formed their special divisions for a wide variety of reasons. They also specialize in varying services and industries, though they claim to be strong in all service areas and industries. A common characteristic of the newly formed divisions is the rapid growth rate they expect.

Continental Special Risk Underwriters, formed in June 1978 to capture captive business, plans to become as large as INA Special Risks or AIG Risk Management, said Robert H. Dorgan director of the special accounts division. Although already serving clients, Continental is just beginning full swing operations this month from four zone offices in New York, Dallas, Chicago, and San Francisco. The company wants clients with annual casualty premiums exceeding $200,000.

Home Group Risk Management Inc., which studied the self-insurance movement for 2½ years before deciding that the time was ripe to create a division, expects to grow "large enough that we will have more than our fair share of the market," according to F.A. Mina, secretary of the Home and vp of the special division.

Home waited to form the division until April of 1978 because "we wanted to feel the temperature of the water before we jumped in," Mr. Mina said. "Home was very mature in that it wanted to build risk services on a solid foundation. We didn't get in late, we just got into it at the right time."

The Home is strong in serving retail stores, Mr. Cymbala of Booz Allen noted. Its greatest strength, according to Mr. Mina, is its large network of facilities in all 50 states, using the parent company's office network.

Mr. Whynot of Commercial Union Risk Management credits a progressive management for starting up the special division before the flurry of activity began in 1978. Commercial Union Risk Management, which currently handles $5 million of business with a staff of 130, expects a growth rate of 30% this year. Its product liability studies and fire protection capabilities are its high points, Mr. Whynot said.

St. Paul Risk Services, formed in March 1978, plans a minimum growth rate of 25% in 1979, said vp E. Warren Bessler, who heads the division. Jon A. Roeder, marketing officer of St. Paul Risk Services, said the company examined the trends in self-insurance for approximately half of 1977 before deciding that captives and self-insured retentions are here to stay.

St. Paul is currently servicing more hospitals than any other industry, a natural outgrowth of the insurer's prominence in medical malpractice coverages, said Mr. Roeder.

Fireman's Fund Risk Services, which begins operations this month, plans to specialize in loss control, although it also offers fronting arrangements for captives, paid-loss retrospective programs as well as claims services.

The division's greatest strength is industrial hygiene, which director James B. Runyan said offers "one of the finest testing labs" for air pollution and noise levels.

Loss control in general will become another specialty, Mr. Runyan said. The division is planning to hire about 20 engineers with skills in heavy construction, marine, oil and petrochemical industries.

Captive management or captive feasibility studies are not offered because these services are normally reserved for brokers and consultants, and might be a conflict of interest for an insurer, Mr. Runyan said.

Although the risk service staff consists of only six people, the division will rely heavily on branch offices, which will sell services and underwrite. The risk service division will give final approval to the branch's activities and will back them with specialized knowledge, Mr. Runyan explained.

The division requires that Fireman's Fund American Loss Control Co. be used for claims handling.

Fireman's Fund, created the division because of competition from other insurers and because it decided conventionally insured methods were passe. Two years from now it plans to handle a minimum of $250 million in annual premiums. Currently, the division is only servicing three accounts. Mr. Runyan said most of the accounts the division will service will have combined premiums in excess of $1 million.

Reliance Insurance Co. formed its risk service division out of a need to offer its agents this competitive edge, said Harry L. Richter, senior vp of the division. Because Reliance's clients are small to medium sized, Reliance did not believe that offering services was as important to it as to other insurers with larger clients, Mr. Richter explained.

Mr. Richter does not expect the embryonic risk services division to become very large. It is utilizing the present staff to handle the loss control and claims services it provides.

Mr. Mackay of Aetna Technical Services declined to disclose specifics about its potential growth or

Continued on page 26

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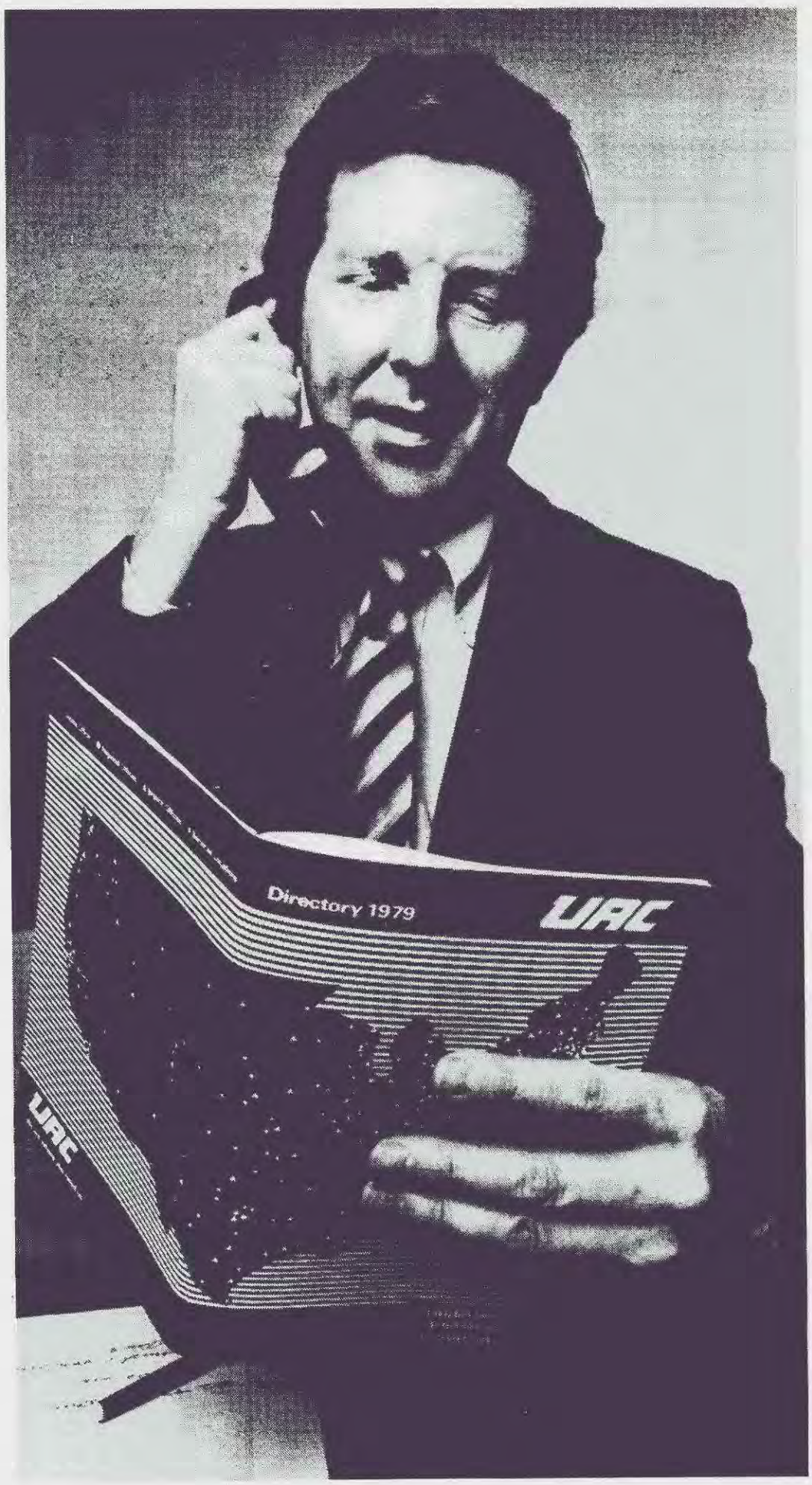

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Risk services . . .

Continued from page 24
the amount of business it handles. Engineering services are a major strength at Aetna Technical Services, according to Mr. Mackay. "There's a lot of competition in claims, but in loss control and industrial hygiene, we have greater expertise," he said.

Joseph C. Smetana, president of AIG Risk Management, was also hesitant to give specifics about clients and income, but noted that the division is "growing at a phenomenal pace." AIG is strong in hospitals and municipalities, said Mr. Cymbala. Mr. Smetana said the division services many hospitals (350), but it is not intended to be its only specialty.

One of the more extensive service divisions, AIG Risk Management is broken down into consulting, general operations, employe benefits and foreign risks. Actuarial, feasibility and loss control functions fall under the consulting title while claims management and claims statistical and information work are incorporated under general operations. The employe benefit division is heavily involved in administrative service contracts for employe benefit packages.

Captive & Self-Insurance

INA Special Risks was formed, according to president John C. Morrison, because "we felt it was an idea whose time had come." In addition, he said, the trends toward self-insurance are helping to ease surplus. A separate division was needed to divide the work according to unique abilities, he added, with special risks handling self-insured casualty programs with annual premiums in excess of $200,000 to $250,000 and workers compensation programs with premiums in excess of $250,000 to $300,000.

The special risk division of INA currently handles $500 million of business net of reinsurance to captives, Mr. Morrison said, with a growth rate of 20% expected in 1979. It's strong suits are marine and aviation risks, noted Mr. Cymbala. But it covers the field through 11 divisions.

A property group consists of INA Underwriters for large property risks, Banker's Standard Insurance Co. for homeowners and INA Farm Center Inc. for crop and hail insurance and reinsurance. A marine and aviation division provides underwriting and services to these industries.

For casualty risks, INA Special Risks consists of: INA Underwriters Casualty; Employers Self Insured Services (ESIS), which provides loss control, claims statistical services and claims handling, and Alaska Pacific Insurance Co., which specializes in logging, trucking and fishery businesses.

An excess and surplus group includes: California Union Insurance Co., excess and surplus underwriters in 48 states writing short-line railroad, large construction and other special liability risks; Montgomery & Collins General Agency, operating in 14 states and offering excess brokerage services in short-line railroad, excess and umbrella liability and long haul trucking for small to medium sized companies, and INAX Underwriting, which provides all types of professional liability and errors and omissions coverages excluding medical malpractice. Extra Cover Agency Inc. provides directors and officers liability insurance as part of INA Special Risks.

NATLSCO expects to grow 25% to 45% this year, said president Robert W. Satterfield. The loss control division of Kemper currently serves approximately 1,000 clients per year, Mr. Satterfield estimated, with a staff of 200, excluding the claims handling staff, which is part of Kemper.

As one of the forerunners of risk services, NATLSCO, which was formed in 1968, foresaw a need for this type of service very early, Mr. Satterfield pointed out.

A known leader in loss control services, NATLSCO has found that its occupational health and industrial hygiene services are becoming more popular, according to Mr. Satterfield.

Since Travelers has not created a special division to service self-insureds it couldn't break out figures about the amount of business it handles for self-insureds, said vp C.J. Clarke. ■

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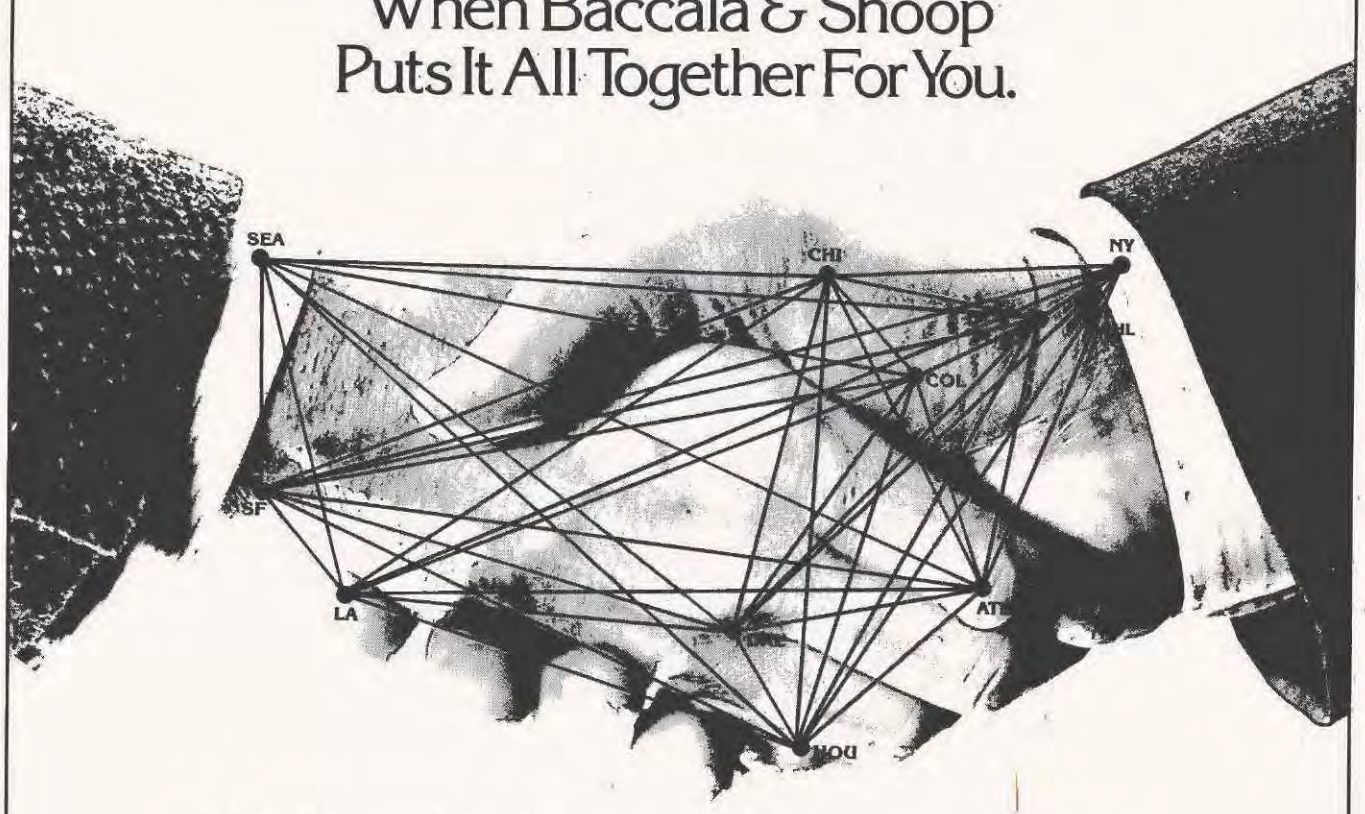

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Staff problems delay action

U.S. may relax rule on employe benefits in captive

By JERRY GEISEL

WASHINGTON—Within the next few months, corporations may find it a lot easier to purchase employe benefit policies from their domestic subsidiary insurance companies.

Next spring, the government plans to issue its long-delayed and eagerly awaited final rule amending the pension reform law to lower barriers that prevent companies from insuring employe benefits in their subsidiaries.

Currently under ERISA a subsidiary can insure a parent company only if the subsidiary is wholly owned by the parent and if less than 5% of its insurance revenues come from the parent company risks.

A number of major corporations which use their domestic insurance subsidiaries to issue policies to employes of the parent—including John Deere & Co. of Moline, Ill., and Field Enterprises of Chicago—were unable to meet the 5% test and petitioned the government to boost the percentage allowed.

Last May, the Labor Department and the Internal Revenue Service recommended that the wholly owned requirement be reduced to 50% ownership and that up to 50% of the subsidiary's revenues could come from the premiums of policies purchased by the parent from the subsidiary.

As a result, a corporation with an

Captive & Self-Insurance

insurance subsidiary domiciled in the U.S. and writing a substantial amount of outside business would be able to place benefits in the captive. (A Colorado captive could not be used since that state does not permit employe benefits to be written by captives.).

Some companies, however, complained to the government that the 50% test is unnecessary. Field Enterprises, said its insurance subsidiary, World Book Life Insurance Co., is licensed in 42 states and the District of Columbia. As a licensed U.S. insurer, World Book is subject to numerous state regulations that protect policyholders, making the 50% of premium test superfluous, World Book vp and general counsel Thomas G. Bostetter contends.

But government sources indicate that the 50% outside business requirement is very likely to remain in the final rule. "It shows that the insurance company is in the business of selling insurance to the public. . .and hasn't been set up only to sell insurance to the parent's employe benefit," a Labor Department spokesman said.

Some firms asked the government to permit offshore or non-U.S. insurance company subsidiaries to underwrite or reinsure benefit policies for the parent.

Cleveland attorney Thomas Jorgenson said excluding foreign insurance subsidiaries is "unnecessary, unreasonable and arbitrary." Foreign insurers are subject to the same type of regulatory requirements as U.S. insurers and it is unfair to assume that they are "somehow inferior" to their U.S. counterparts, he suggested.

But Business Insurance learned that the IRS and Labor will not liberalize the final rule to allow offshore captives to get into employe benefits arena. The government is opposed to use of offshore captives, considering them difficult to regulate and not as safe as domestic insurance companies, sources said.

However, the government still has not come to grips with whether a corporation's insurance subsidiary can enter into "fronting" arrangements with other unrelated insurance companies.

"The fronting question is the main problem at the moment," said one source. "It is an extremely complex issue and I'm afraid there are no easy or quick answers."

Under a "fronting" arrangement, insurance policies are usually issued by a well-known, licensed insurance company. The licensed insurer then reinsures a substantial portion of the risks with the parent company's insurance subsidiary.

The government's May proposal did not come out and say that fronting and reinsurance arrangements are prohibited under ERISA. However, a footnote attached to the proposal said: "This proposed class exemption is not intended to cover such reinsurance arrangements to the extent they are prohibited transactions."

Attorney Mr. Jorgenson has described the footnote as an innuendo that condemns "a multiple of legitimate reinsurance arrangements which are in the best interests of plan participants and beneficiaries."

Under reinsurance arrangements the primary insurer does not have to absorb the full burden of the loss, Mr. Jorgenson said. "This protects the assets and financial stability of the primary insurer and therefore increases the likelihood that the participants will receive their benefits," he maintained.

Government officials say they understand Mr. Jorgenson's reasoning, but fear blanket approval of reinsurance arrangements could lead to self-dealing between a parent and its subsidiary.

The issuance of a final rule, which has been delayed by staff shortages in the IRS and Labor Department, will cap a four-year battle by corporations to liberalize the "5% ERISA rule."

When ERISA was being drafted in 1974, the bill's architects originally proposed prohibiting any employe benefit transactions between a parent and its insurance subsidiary to prevent possible self-dealing.

However, the outright prohibition was replaced with the 5% limitation on subsidiary revenues from insuring its parent's risks so Sears, Roebuck & Co. could continue to insure its employe benefit plan with Allstate Insurance Co., its insurance subsidiary.

Sears was able to meet the 5% test with ease since more than 95% of Allstate revenues come from insuring non-Sears risks. However, other companies could not meet the 5% test and started pressing for a higher percentage test.

Once the final rule is issued, corporations insuring employe benefits in subsidiaries will be given one year to comply. ■

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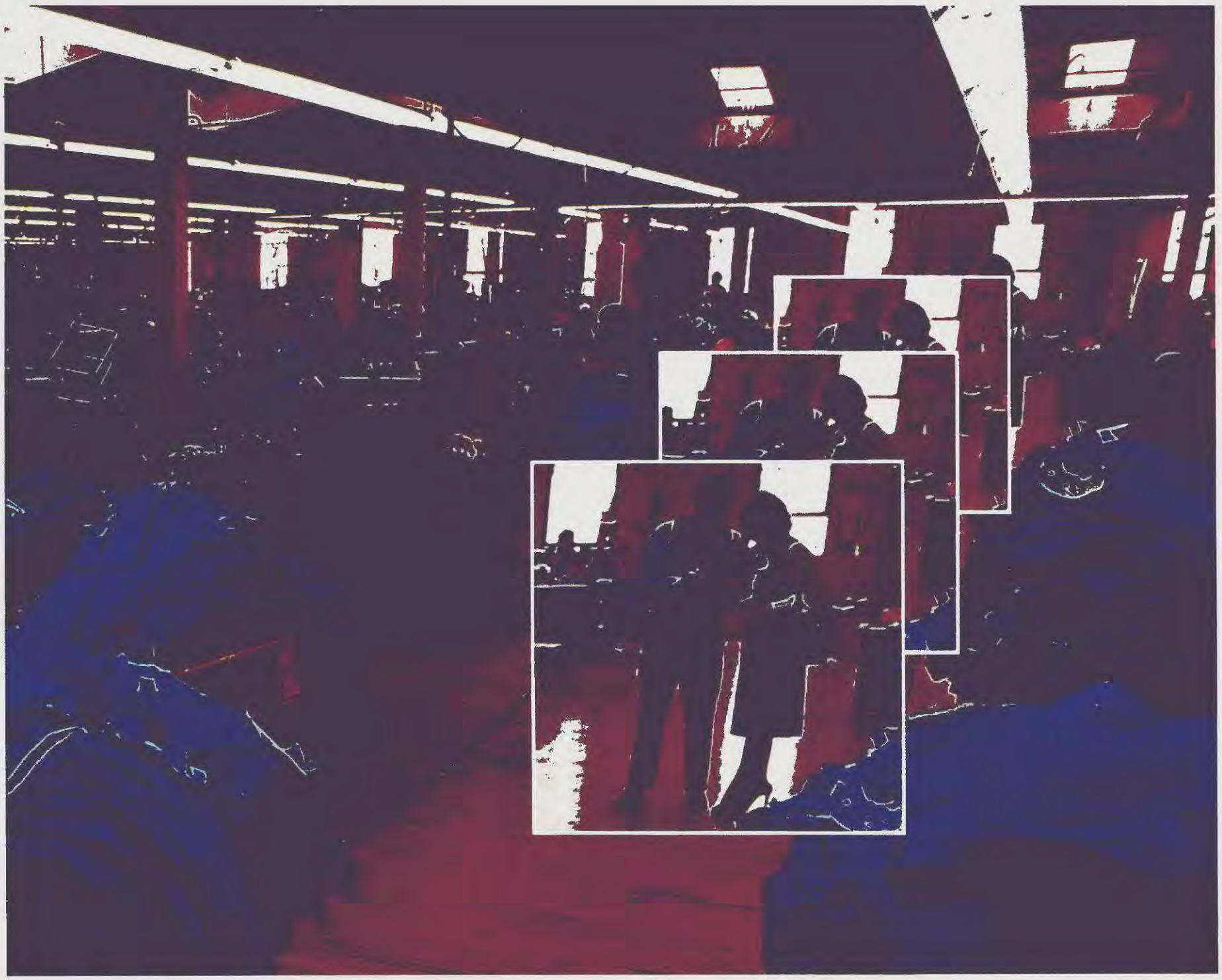

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State officials covet captive insurer development

By JOHN MAES

CHICAGO—State laws authorizing formation of captive insurance companies will likely be on the minds of insurance officials in at least three states as they begin the new year.

In Minnesota, a state senator plans to introduce a bill to the new legislative session that would make Minnesota the third state to pass a law designed to stimulate the growth of captive insurance companies.

In Colorado, whose 1972 law is considered to be the model of state captive legislation, captives will now be able to reinsure third-party risks since the state attorney general recently advised insurance officials such reinsurance is legal without legislative amendments.

Meanwhile, Tennessee officials have chartered and licensed the state's first operating captive for Hospital Corp. of America and hope to begin reaping the fruits this year of their Colorado-style bill passed in 1977.

Otherwise, it doesn't appear that legislators across the country will heed the advice of David D. Holbrook, president of the National Assn. of Insurance Brokers, who recently told a conference of lawmakers that they should push for captive insurance laws as an answer to the scarcity of product liability insurance.

Officials in Washington, California, New York, Michigan, Pennsylvania and Connecticut—states

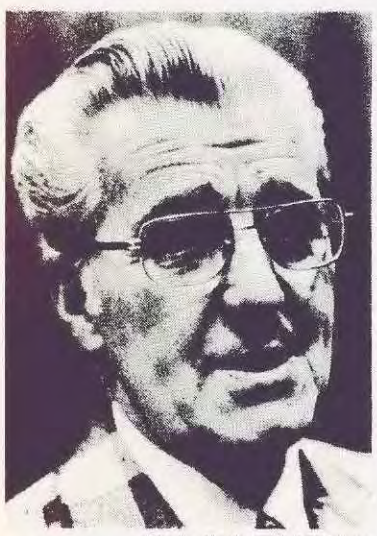


Photo: Kathryn J. McIntyre

Third-party business can't be a Colorado captive insurer's main business, says J. Richard Barnes.

mentioned as possible entrants into the captive market—say they know of no legislation being planned for their states dealing with captive insurance companies.

In Pennsylvania, Benn Prybutok, special assistant to the insurance commissioner, said developing a captive insurance company domicile is a low priority item when compared with product liability and the problems of inner-city residents buying insurance.

Carl Brakensiek, chief counsel for California's finance, insurance and commerce committee, said a captive insurance company bill is apparently not on the agenda for this year, but may be in 1980.

Michigan insurance officials say their state's existing law encourages growth of captive companies by foregoing taxes on premiums paid for Michigan risks and decreasing tax liability on the amount of investment income.

Ford Motor Co. and Dow Chemical Co. have formed Michigan captives, the department said.

An insurance department spokesman in New York said no captive insurance laws have been recommended while lawmakers gear up for discussion on bylaws and the constitution for the New York Exchange.

State Senator Jerome O. Gunderson of Minnesota said his legislative proposal is almost the same as the Colorado law, but is stricter in that it would require companies entering the captive market to back up a letter of credit with a certain amount of money.

"We'll need to have money to back it up," the senator said. "We can cover some of it, but we'll have to have something to back it up to protect the public."

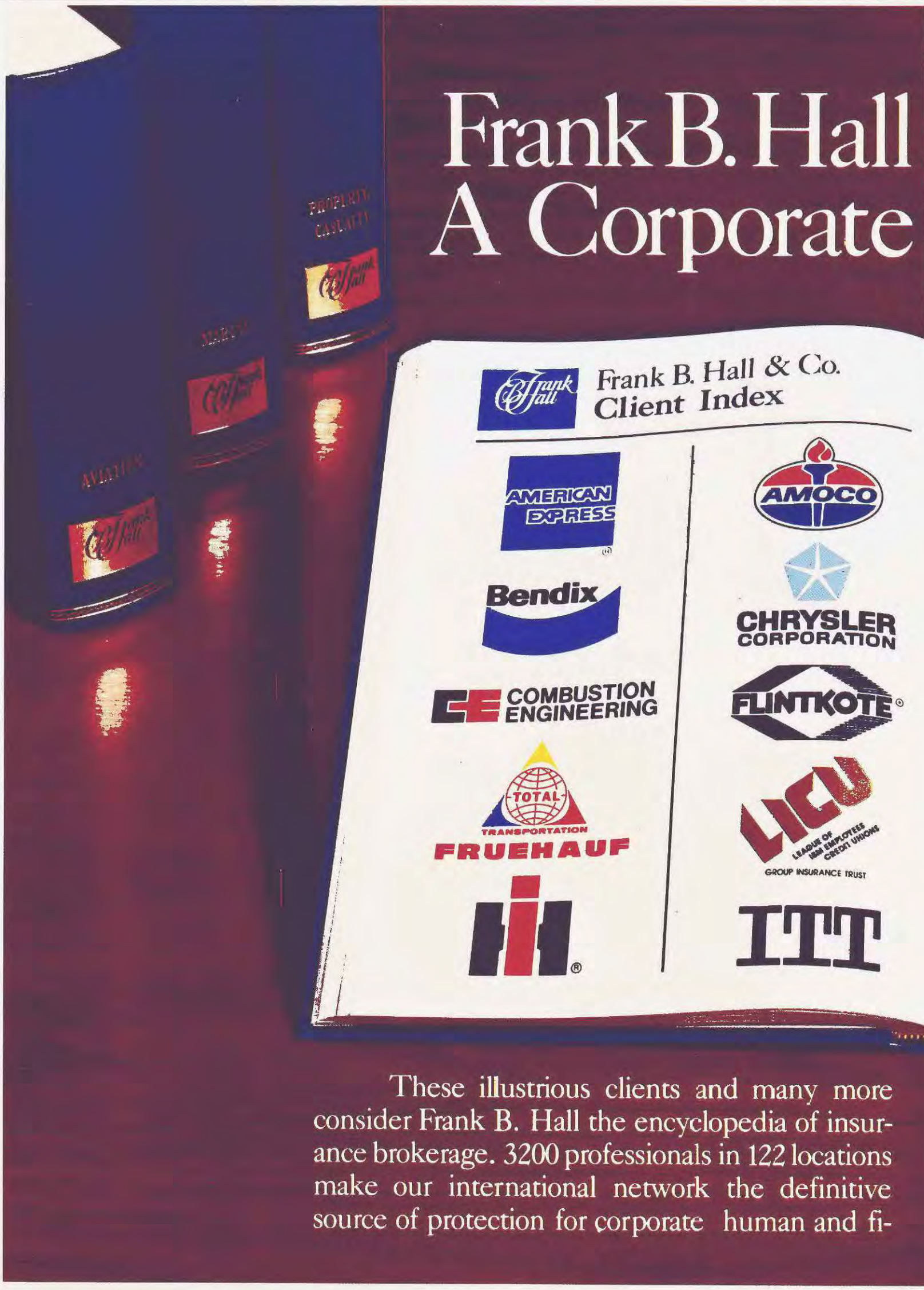
Captive & Self-Insurance

Senator Gunderson wants a Minnesota captive law so the state can attract and regulate the captives and to prevent the state government from losing premium taxes that might otherwise be carried to offshore captives. "We should have that privilege in our own state," he said.

Sen. Gunderson became interested in captive legislation when he learned that the University of Minnesota had formed a captive in Bermuda. He was concerned others may follow suit, taking money out of Minnesota.

St. Paul Fire & Marine Insurance Co., the state's largest insurance company, indicated they are "interested" in the legislative proposal, but have stopped short of committing total support to its passage, according to the senator.

The insurer will "neither support nor discourage" a captive law in Minnesota, said a company spokesman, but would provide



counseling through its risk management subsidiary to companies seeking to set up a captive insurer.

The proposed exemption for captives from contributing to the cost of compulsory residual market mechanisms is "something we're concerned about," the spokesman said, but company officials can live with the bill.

Sen. Gunderson predicted there will be some controversy over the bill, especially from agents and brokers who might see it as a threat to their businesses. "It's foreign to Minnesota and some people are wary about what it's not going to do," he said.

"There are some agents who will probably think it's the craziest thing they've ever heard of. It will give them the impression that it's all right for everyone to have their own insurance company," he said.

Although optimistic his bill will eventually become law, Sen. Gunderson said challenges to the outcome of elections in the Minnesota House of Representatives may push some of the legislature's business over to the 1980 session.

In Colorado, insurance commissioner Mr. Barnes said the state attorney general's office has advised him that captive insurers can do third-party business through reinsurance under existing law.

Reinsurance of risks unrelated to the parent firm is an "indirect form" of third-party business, said Mr. Barnes. The state's 29 captives will be eligible to apply for authorization to conduct the business and the commissioner said each request will be reviewed individually.

However, the captives will not be allowed to make third-party reinsurance risks their primary source of business and firms may be required to put up additional capital and surplus before being allowed to enter the market, he added.

The only lines of reinsurance to be allowed are those that the captive is allowed to write for the parent company, which excludes personal lines and employe benefits.

Mr. Barnes had told a conference of the Captive Insurance Companies Assn. last October that it was unlawful for captives to take on third-party business but that he would not oppose any amendments to the law that would allow them to do so.

He had to explain later that he was referring in his speech only to non-parent reinsurance business as being illegal and was not suggesting he would allow Colorado captives to write third-party business directly.

But Mr. Barnes' comments at the conference still caused some concern among executives of the captive firms apparently surprised that non-parent business was unlawful, according to Reginald G. Hobday, managing vp of Anistics Inc., a subsidiary of Alexander & Alexander. "It caught a lot of us by surprise—they were not aware they couldn't write non-parent business," he said.

After the conference, a group of captive managers met to discuss the situation and decided to ask for an opportunity to comment on guidelines governing premiums and the nature of risks to be allowed, Mr. Hobday said.

Mr. Hobday said he and others in Colorado are satisfied with the new interpretation of the existing law and will not push for amendments. "We don't want to become full-fledged insurance companies," he said.

Tennessee, the second state to invite captive insurers through legislation, now has its first captive, Parthenon Insurance. The subsidiary of Nashville-based Hospital Corp. of America, which had been doing business in Denver under the auspices of the Colorado law, is incorporated in Tennessee.

Paul J. Tidwell, assistant insurance director for Tennessee said one other firm is awaiting the green light to begin operating and a third company is in the application process.

"And we get a lot of inquiries," he said. "We're getting five to six a week and a lot of people are coming in to sit down and talk."

Although only a few firms have done anything more than apply for licensing, Mr. Tidwell said, "we're exactly where we thought we'd be" in efforts to induce captive growth in the state.

Since the passage of the law, Mr. Tidwell's office has been publicizing it, but officials were not expecting an immediate rush of companies seeking permission to operate there.

"We based our expectations on the Colorado situation and found that law laid out there for three years before anything happened," he said. "Things didn't take off out there until the later part of 1976 and into 1977."

But now that Tennessee's law has been on the books for a while, Mr. Tidwell predicts as many as six captives will be set up in 1979 and more in years to come. Anticipating that situation, Mr. Tidwell said he plans to ask for $44,000 in budgetary outlays for advertising to attract new captive operators.

The plan is part of a larger effort by the Tennessee Industrial Development Board, which is trying to draw new industry into the state. ■

New office for surplus lines

LOS ANGELES—Towers, Perrin, Forster & Crosby's reinsurance division last month opened a reinsurance-surplus lines office here. The Los Angeles office will serve as a production and servicing satellite of TPF&C's San Francisco reinsurance office.

While the Los Angeles office initially will only have a surplus lines capability, TPF&C also plans to offer property/casualty facultative reinsurance services here during the first half of 1979. ■

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SINCE 1967

May not be told

Employes don't notice self-funded health plan

By ESTHER KUNTZ

Captive & Self-Insurance

CHICAGO—Many companies that implement self-funded benefit plans inform their employes about the change, while others prefer to keep the matter quiet.

Those that are straightforward about it say the most negative response they receive is indifference. Most employes are pleased with self-funding, especially if the employer administers the claims.

Alan Jeffery, benefits manager for Security Pacific National Bank, says, "We can turn a claim around a lot faster than an insurance company. Employes are aware of this advantage and favor the program."

The service an employe gets from his own company is better and more personal, said Judy Smith of the Bank of America. But because of that, employes expect more from their own company and sometimes have trouble accepting the bank's decisions to limit payments. "If we were an insurance company, people might not tend to question our decision," she said.

Perhaps that is the reason some companies prefer to have an insurance company administer the claims. Then experienced claims managers take responsibility for the payments and employers can choose not to inform employes that they are funding the programs. Because employes receive payment from the insurance company, they assume it insures them as well.

One benefits manager, who makes it a point not to inform employes that their health benefits program is self-funded, defended his position by saying, "The employe sees it the same way because the insurance company is paying the claim whether it comes out of our bank account or their premiums. It really makes no difference to the employes."

Some employes apparently are indifferent to the manner in which their benefits are funded while others simply remain unaware. "Even though it says Security Pacific Health Care Plan on the forms," Mr. Jeffery said, "not everyone has made the connection. The plan has been in effect for three years, but some older employes still assume they are covered by an insurance company."

At the bank of America, new employes are told the plan is self-funded when they are hired, said Judy Smith. But those who were hired before the plan became effective still identify their coverage with Occidental Life Insurance Co. "It's obvious when they call about their claims, though, that they are talking to us," she said.

Benefits manager Robert Deitmeyer summed up the attitude of Abbott Laboratories employes toward the self-funded plans as, "We're guaranteeing the programs. The employes don't care where the benefits come from as long as they are there." ■

OPIC honors Taiwan policies

WASHINGTON—The Overseas Private Investment Corp. (OPIC) will honor all existing political risk insurance policies it issued to U.S. companies that have overseas facilities in Taiwan even though diplomatic relations between the U.S. and Taiwan have been severed.

OPIC and State Department officials, however, are now discussing whether OPIC will continue to offer new policies to U.S. companies investing in Taiwan. Generally, OPIC policies only are available in foreign countries that maintain diplomatic relations with the U.S.

OPIC is the federal agency that offers political risk insurance to protect U.S. private investment in developing countries against political risks.

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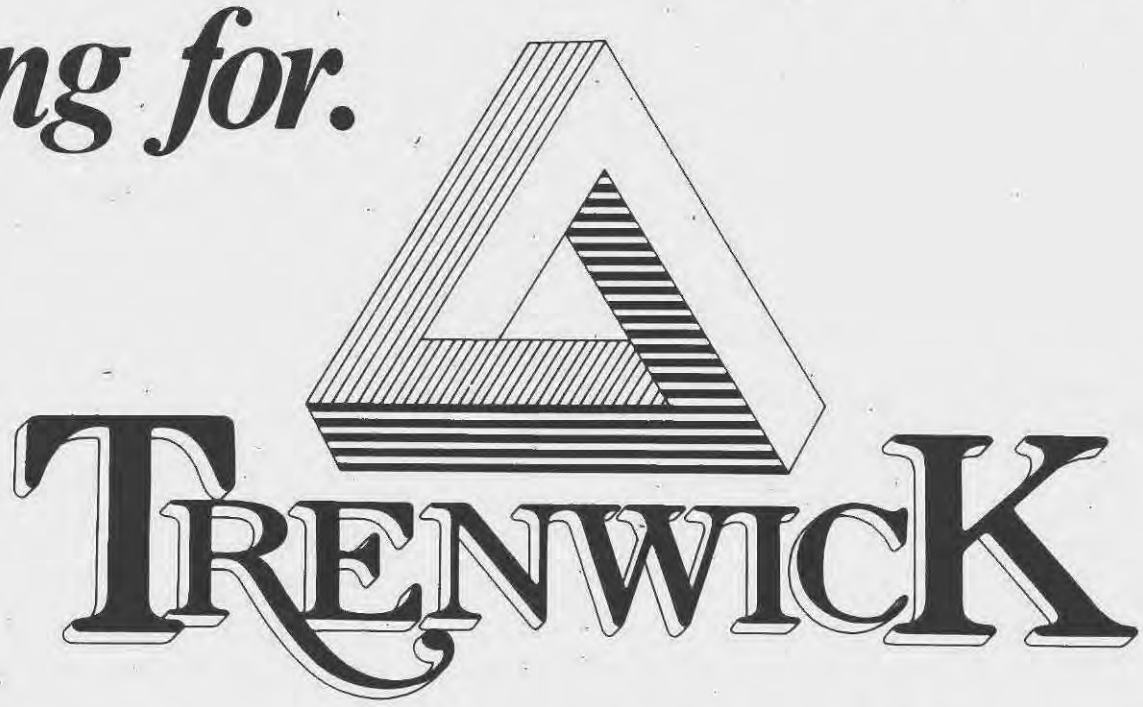

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Is that diving haven or tax haven?

When is a vacation spot not a vacation spot? When it's the meeting site for the board of directors of an offshore captive insurance company.

But can one blame captive executives for succumbing to the warm, sunny climate, picturesque beaches and various other tourist attractions of locations such as Bermuda?

Yes, said several risk managers whose companies have captives.

"People who combine business with pleasure by having captive meetings at exotic resorts ought to be hung out and dried," said the northern California risk manager who's president of a captive domiciled in Bermuda.

"That's what caused a lot of trouble with the Internal Revenue Service," he said. On the other hand, "if your captive is in Bermuda, and your managers and bank are there too, there's no reason not to meet in Bermuda. Just don't have a great time while you're there," he added.

Directors of an offshore captive insurance company must meet outside the U.S. to conduct the captive's business, lest the captive be found engaged in U.S. trade or business and invite immediate taxation.

After Bermuda, Toronto was mentioned by several risk and captive managers as a popular meeting spot. "It's outside the U.S., convenient and cheap," said one.

"There really are few incidents of vacations disguised as captive meetings," said an insurance consultant.

But one wonders how typical is the reply given by the U.S. risk manager of a captive domiciled in Grand Cayman. When asked why his company chose that location, he said quite candidly, "Because it has one of the best underwater diving places in the world."

Caymans grow popular

Captives pick a home from a host of options

By MARGARET LeROUX

Captive & Self-Insurance

GEORGETOWN, Grand Cayman—Bermuda has Leslie Dew, but Grand Cayman has Harvard; Guernsey may soon have 3M Co., and one authority predicts renewed interest in the Bahamas as domiciles for captive insurance companies spatter the globe.

With more than 700 captives registered in Hamilton, Bermuda is still the choice of most offshore captive insurance companies. "Probably 99.5% of all captives are in Bermuda," said Gerald Brown, vp of Alexander & Alexander risk management services. "There's no advantage for a legitimate company to set up an offshore captive in any place other than Bermuda."

The management of Controlled Risk Insurance Ltd., the captive of Harvard University and 11 affiliated hospitals, would disagree. The hassles involved in applying to establish a captive in Bermuda made the Cayman Islands look very attractive to the board of directors of Harvard's captive, according to manager Dan Creasey.

Harvard's directors were considerably irritated at the probings by Bermuda's Adhoc Committee which scrutinized all applications by malpractice captives. "We were looking for a location, not a business partner," Mr. Creasey said.

So even though Bermuda eventually approved Harvard's application, the $22 million captive was domiciled in Grand Cayman, a decision the board of directors intended to show their anger at the Bermudians.

Since Harvard's application, the Adhoc Committee has redefined its duties and changed its name. Now all captives with a long tail exposure are reviewed by a group known as the Insurance Review Subcommittee.

"Just what we need, another IRS," commented Thomas Duffield, risk manager for Archer-Daniels-Midland.

That company has two captives domiciled in Grand Cayman, Agrinational Ltd. and ADM Insurance Co. Ltd. "But we had other business operations there before we established them," Mr. Duffield explained. "It wasn't a case of not wanting to be in Bermuda.

"Since we've been in the Caymans, we've seen a lot more captives being established there," he said, estimating 50 there now.

"There's been a tremendous increase in the number of captives coming to Grand Cayman," said John Ray, general manager of Cayman Underwriters Services Ltd., the oldest captive management firm on the island.

"We've added eight captives this year," Mr. Ray said, bringing the total to 23 managed by Cayman Underwriters. "Within the next two years, the Caymans will be a force in the market," he predicted.

Although the Caymans don't measure up to Bermuda in communication facilities, with no direct dial telephone service, the financial services available in the Caymans are superior to those in Bermuda, several captive managers said.

With more than 200 banks leading the list of exempt companies doing business in the Caymans, "you could say it's the Bermuda of the financial industry," Mr. Duffield observed.

"The banking environment is more secure in the Caymans than in Bermuda," Harvard's Mr. Creasey said, "because the banks (in the Caymans) operate as branches, not subsidiaries of the parent banks such as Citibank of New York and the Bank of Nova Scotia.

"The banks in the Caymans have the full faith and credit of the parent institutions, while in Bermuda all banks are 60% locally owned," he said.

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Captive homes . . .

Continued from page 34

rest, the Bermuda government could freeze the banks and subsidiaries could be cut off from their parent institutions. But branch banks couldn't be cut off if a similar situation occurred in the Caymans.

Another advantage to doing business with a branch bank is a certificate of deposit from the Cayman Island branch bank could be cashed in any other of the bank's branches.

Several sources involved in captive management noted that the Caymans have overcome their former shady image of a tax dodge. "The location of Harvard's captive there had a favorable effect," Mr. Duffield said.

According to Harvard, their captive made the Caymans prestigious. A former member of that institution's board of directors said in a speech at the university, "The Caymans are respectable by virtue of the fact that Harvard's captive is there."

A further step towards respectability, the passage of insurance legislation is expected in the near future. Captive expert Sidney Pine, attorney with the New York firm of Trubin, Sillcocks, Edelman & Knapp told *Business Insurance* he had been asked by the Cayman government to comment on the proposed legislation.

His advice was to wait until the Bermuda government works out some of the more controversial aspects of its new law.

The financial future of the European Economic Community played an important role in 3M Co.'s plans to establish a captive on Guernsey, one of the Channel Islands.

"We hope at some point in the future the EEC will ratify insurance treaties and at that point it would be to our advantage to have our insurance subsidiary in existence," said 3M insurance director Howard Weber.

"It's speculative at this point," Mr. Weber said, "but if it does happen, it would be a tremendous advantage to have direct access to the reinsurance market in Europe."

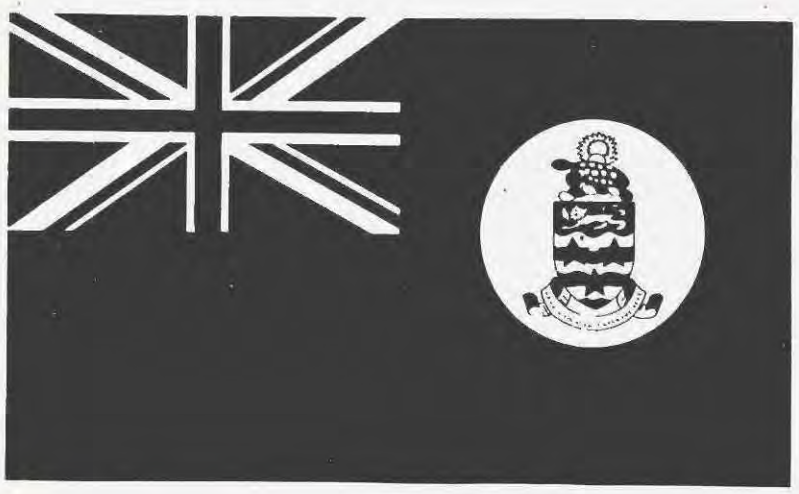
A spokesman for a Midwest-based electronics firm that founded a Guernsey captive in 1976 said, "We've been told by several consultants that Guernsey is the right place at the right time.

"If the EEC ever agrees on the commodity status of insurance, there will be grandfather clauses written into legislation," said the risk manager, who requested anonymity.

Not many U.S. firms are among the estimated 100 captives licensed in Guernsey, but some experts expect to see more interest.

The Bahamas will also see action in captive development, attorney Mr. Pine said. "The government there has recently amended its insurance regulations and is making a real effort to encourage captive business." For example, a 10% premium tax will no longer be applicable to insurance business done by captives in the Bahamas.

The Netherlands Antilles is another potentially hot area for captive growth, according to Mr. Pine. That government reduced the tax on captives to 6% of underwriting income with allowable deductions for all reserves. ■



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Savings take time

Big risks force small firms into captive insurance

By ELLIS SIMON

Captive & Self-Insurance

SAVANNAH—What does Savannah-based Southeastern Maritime Co., a stevedoring firm with $20 million annual sales, have in common with industrial giants such as Ford, Union Carbide and 3M Co.?

A captive insurance company.

Surprising? It shouldn't be, because the ability of a corporation to set up a captive has little to do with it's size, but rather its exposure and the size of the premiums it would have to pay to protect itself, say captive experts.

In Southeastern's case, casualty premiums were running close to $1 million when the captive, Anchorage Fire & Casualty Insurance Co., was set up in Bermuda in 1975, said Mike Winnett, vp-risk management and president of Anchorage.

Workers compensation represented the greatest casualty exposure. As a stevedoring firm, most of Southeastern's employes come under the U.S. Longshoremen's and Harbor Workers Act and are eligible for the lucrative disability benefits provided under the act. Premiums for the insurance in the states served by the firm range from about $8.50 per $100 of payroll in South Carolina to just over $26 in Florida.

With payroll representing 80% of the costs for a firm like Southeastern, it is easy to see the tremendous impact of workers compensation premiums on the total operation. "At the end of 1972, substantive changes to the U.S. L&H Act substantially increased benefits," Mr. Winnett noted. "We felt it would be quite a while before the benefits paid would catch up with the rate increases. That proved true for us, but it may have not been true for others."

In addition to workers compensation, Southeastern uses its Bermuda-based captive to write general and auto liability and on occasion strike insurance. The captive also provides direct access to the buffer layer excess and reinsurance markets, Mr. Winnett noted. In addition, Anchorage Fire & Casualty handles third-party business and is considering expansion in this area.

Southeastern may not be the smallest single entity in the U.S. operating a captive; Mr. Winnett believes one or two other stevedoring firms of similar size could be operating captives. However, firms doing less than $100 million annual sales and operating captives are not that uncommon.

How many firms fit that criteria is unknown. Both Risk Planning Group Inc., which publishes Captive Insurance Company Reports, and Thomas Duffield, president of the Captive Insurance Companies Assn., have no idea, since neither organization keeps records on the size of parent firms.

However, industry experts note that the size of premiums paid, not annual sales of the parent firm, is the determining factor whether or not a captive is feasible for a company. Generally, they say a $500,000 standard premium on a single line of insurance is the minimum requirement for starting a captive, although some say $1 million is a safer level.

At $500,000, a captive would just about break even, assuming a 100% loss ratio. The minimum capitalization requirement in Bermuda is $120,000. The captive would write three times that in premium and management fees would run at least $20,000, noted Bill Yeargan, assistant vp of J.H. Blades & Co.

Assume the rule of thumb that insurance premiums run 1% of sales for a normal risk company and 3% of sales for a high risk organization. Under the $500,000 minimum premium standard, a standard risk company would have to have at least $50 million in sales and a high risk organization $17 million in sales before a captive would be feasible.

Several firms with less than $100 million sales are operating captives. For the most part, the captives are special purpose operations handling problems such as product liability, builders risk, hospital malpractice or in the case of Anchorage, high exposure workers compensation.

Often, a captive is set up where there is no alternative insurance solution, said Joseph Smetana, president of AIG Risk Management Inc. "It's a question not of being successful, but setting up a mechanism to fund contingent liability losses. In effect, it's the same as going bare, but earning income as the result of investment."

"What counts is whether there is a potential for underwriting profit, how big that potential is, the anticipated investment income and how they compare with the expense of operating a captive," said Peter Densen, president of Alexander & Alexander's Anistics division. Since captives require capitalization, if a company can get a better return on investment elsewhere, it should not set up a captive, he added.

"It's feasible for a company to set up a captive provided the company is committed to risk and loss control, is well financed and is able to withstand losses up to a substantial level," said Robert Godfrey of SCOR Risk Management. "These losses should be somewhat predictable and the company should be able to maintain adequate levels of reinsurance at reasonable cost."

Recently, Mr. Godfrey's firm set up a Cayman Islands captive for Allied Products Co., an Alabama concrete products manufacturer with around $50 million annual sales. Prior to setting up the captive, Allied's casualty premiums were running $550,000 annually.

Allied had good loss experience in workers compensation during the past few years, but had been paying a high insurance rate because of problems several years earlier, said William Stephenson, vp-finance. In addition, the firm could not obtain product liability coverage for its concrete pre-stressed railroad crossties.

Mr. Stephenson expects the captive to break even over the first two years and then produce savings in future years, although he made no predictions on the size of the savings. "We're right at the size where

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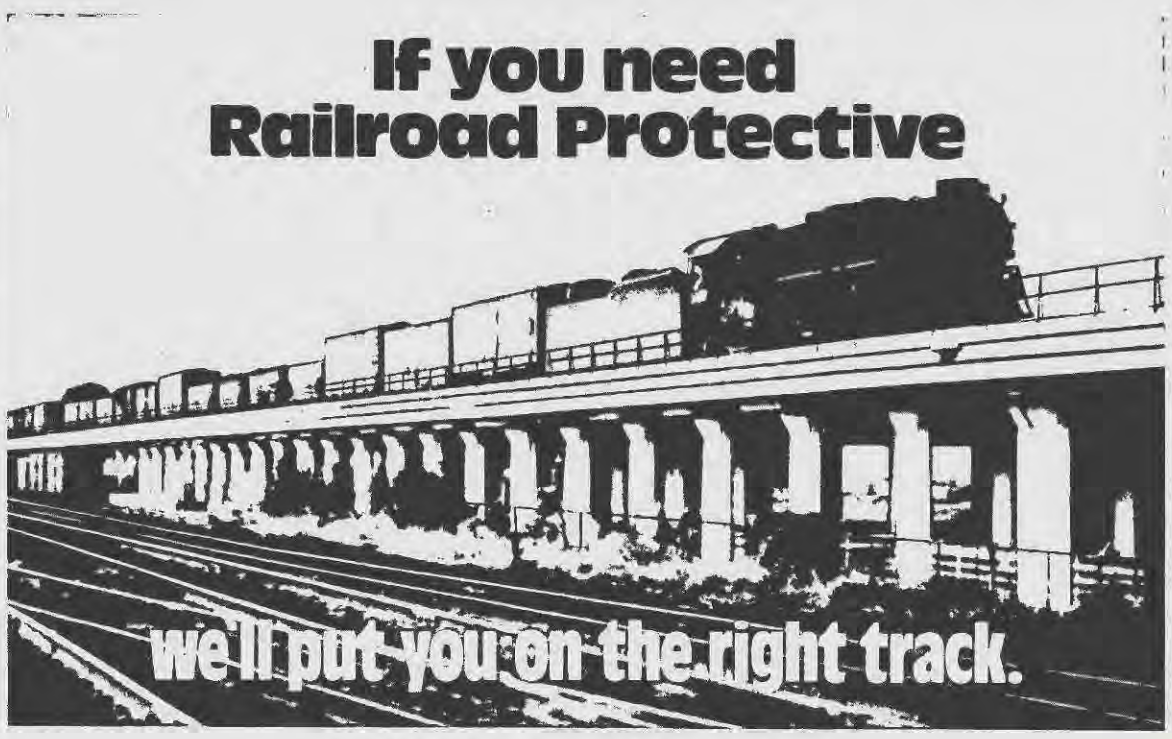

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Small firms' captives . . .

Captive & Self-Insurance

Continued from preceding page
we can't expect savings until premiums would be larger than they are now," he added.

Newpark Resources Inc., a New Orleans-based energy products and marine transportation holding company with $59 million in sales in 1977, formed a Bermuda captive this year because it was having difficulty finding an underwriter to handle a newly consolidated casualty program.

But at levels much below a $500,000 premium, captive feasibility is limited. "With small premiums, the amount you save doesn't justify going through the rigors of a captive," said Arthur Deters, executive vp of American Risk Management Inc., a captive services firm. Mr. Deters and other experts suggested smaller firms join group captives as an alternative to forming their own wholly owned subsidiary.

Even two or three companies that size could band together to form a successful captive, he said.

"A company with a $400,000 premium could set up a captive, but I'm not sure the expense would justify the end result," added Jack Morrison, president of INA Special Risk Facilities.

"The point of forming a captive is to put back as many dollars as possible into less payments and not expense payments. At some point, capitalization costs become too great for captive formation," added SCOR's Mr. Godfrey.

Gurrentz International, a meat importer in Pittsburgh, operates a captive with less than a $500,000 premium volume. But neither Gurrentz nor the Nassau, Bahamas, management firm of J.S. Johnson & Co. Ltd. would discuss the captive GINCO's operations.

SCOR's Mr. Godfrey said he had heard of a group captive operating with a $250,000 premium volume because it had no market for insurance, but he was not aware of a single entity of such size operating a captive.

Captive ownership offers the same advantages to a small firm as a large one. "The same principles that apply to Ford and Exxon can be applied to someone who's not that big," Mr. Godfrey said.

Single owner captives give the owner control over investment programs, but they are more expensive to operate than a group captive, said Mr. Yeargan of J.H. Blades.

Where there is homogenous participation in a group captive, the captive is in a better position to deal with the reinsurance markets, he said. The single owner captive is purchasing facultative reinsurance for one account, while the group captive is treated more like a treaty reinsurance buyer since there is more premium and a greater spread of risk, Mr. Yeargan explained. ■

Insurer offers auto dealers new program

SAN FRANCISCO—Fireman's Fund Insurance Cos. is marketing a new liability and physical damage policy for automobile dealers and service operations.

The garage policy offers a revised liability and collision rating system, expanded coverage, more physical damage options and simplified language and format, said vp Joel V. O'Neal. Exposures insured by the new policy include liability, auto medical payments, garage operations medical payments, uninsured motorists, garagekeepers and physical damage insurance.

The liability rating method for auto dealers is based upon auto usage rather than payroll classifications, eliminating the inequities that resulted from charging two dealers with the same inventory the same premiums even though one had more demonstrators on the road and was therefore more likely to have a loss, the company said.

Previously excluded perils—losses due to structural alterations, escalators, vacant premises, war and liquor liability—are now covered under the new garage policy. ■

Captive fever still burns hot in trade group associations

By JERRY GEISEL

Captive & Self-Insurance

WASHINGTON—When the huge Chemical Specialties Manufacturers Assn. formed a Bermuda insurance company last summer, CSMA president Ralph Engel was optimistic that the captive would help solve members' product liability coverage problems.

What Mr. Engel did not anticipate was the deluge of requests for more information from other trade associations after a profile of the captive, called Chem-Spec Insurance Ltd., appeared in *Business Insurance* and later in another business publication.

"I've already spoken to more than 30 different groups and there are so many other invitations that I could spend almost every day for the next nine months discussing Chem-Spec before other trade groups," Mr. Engel says.

The interest in Chem-Spec is evidence that the relative improvement in the property/casualty insurance market hasn't cooled associations' captive fever.

The number of association captives is now estimated at between 35 and 45, double the figure of only two years ago. Some experts, such as Michael Bott, president of Risk Treatment Services of Bermuda, are forecasting half again as many will be formed in the next few years.

"I think the future is very bright for association captives, particularly if the underwriting situation takes another adverse turn," says William Kersten, president of Glendale Risk Management Inc., a Denver captive management company.

"For small manufacturers that have a serious coverage problem where the market seems to have overreacted, an association captive is the name of the game," says Peter Godfrey, senior vp in Reed Shaw Stenhouse's Boston office.

Captive experts agree, however, that associations' interest in a captive to handle property coverages has waned recently due to the softness in that market.

The high price of comprehensive general liability coverages, particularly product liability, as well as the lack of capacity for certain liability risks, continue to be the raison d'etre for most association captives, said Mr. Bott of Risk Treatment Services, a Bermuda captive management company.

In the last year, trade associations representing greyhound race track operators, oil jobbers, chemical manufacturers and tuna boat operators formed captives. Now, Michigan tavern owners are forming a Cayman Island-based captive that will provide coverage for tavern owners against suits brought under the state's strict dram shop liability law. That law lets customers sue a tavern owner if they suffer injuries as a result of having too much to drink in his bar.

A diverse group, these associations all represent members who believe the insurance premiums they were being charged had little, if any, correlation with their loss experience.

For example, one chemical manufacturing company's insurance premium soared to $149,000 from $7,900 even though the company had not suffered a loss in over five years, Mr. Engel observed.

"The experience of members just didn't reflect the rates that were being laid upon us," agreed Richard Bartlett of the National Oil Jobbers Council, a trade group that recently helped members establish a Colorado captive.

The National Pest Control Assn. of Leesburg, Va., the first trade group to form a captive in 1979, began to explore a group program in 1976 when premiums for general liability coverage for pest control operators began to soar.

Members with an insignificant number of claims suddenly found it difficult to obtain coverage at a reasonable price, said Jefferson Keith, executive director of the association. "One pest control operator's premium leaped to $35,000 from $3,500 even though no losses had been incurred," he said.

The association retained Euclid Services Inc. of New York to find an answer to soaring premiums. Members submitted insurance costs, company sales and loss experiences to see if a group program was feasible.

After 28 months of a "hell of a lot of time and effort," the National Pest Control Assn.'s Bermuda insurance subsidiary, Pestco Insurance Co. Ltd., is ready to offer trade group members $1 million of general liability coverage.

Pestco is paying a fee to Mutual

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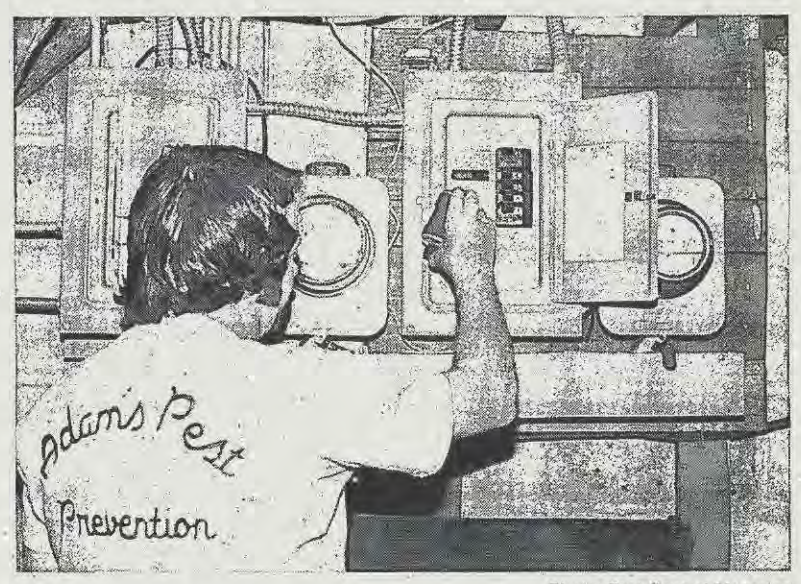
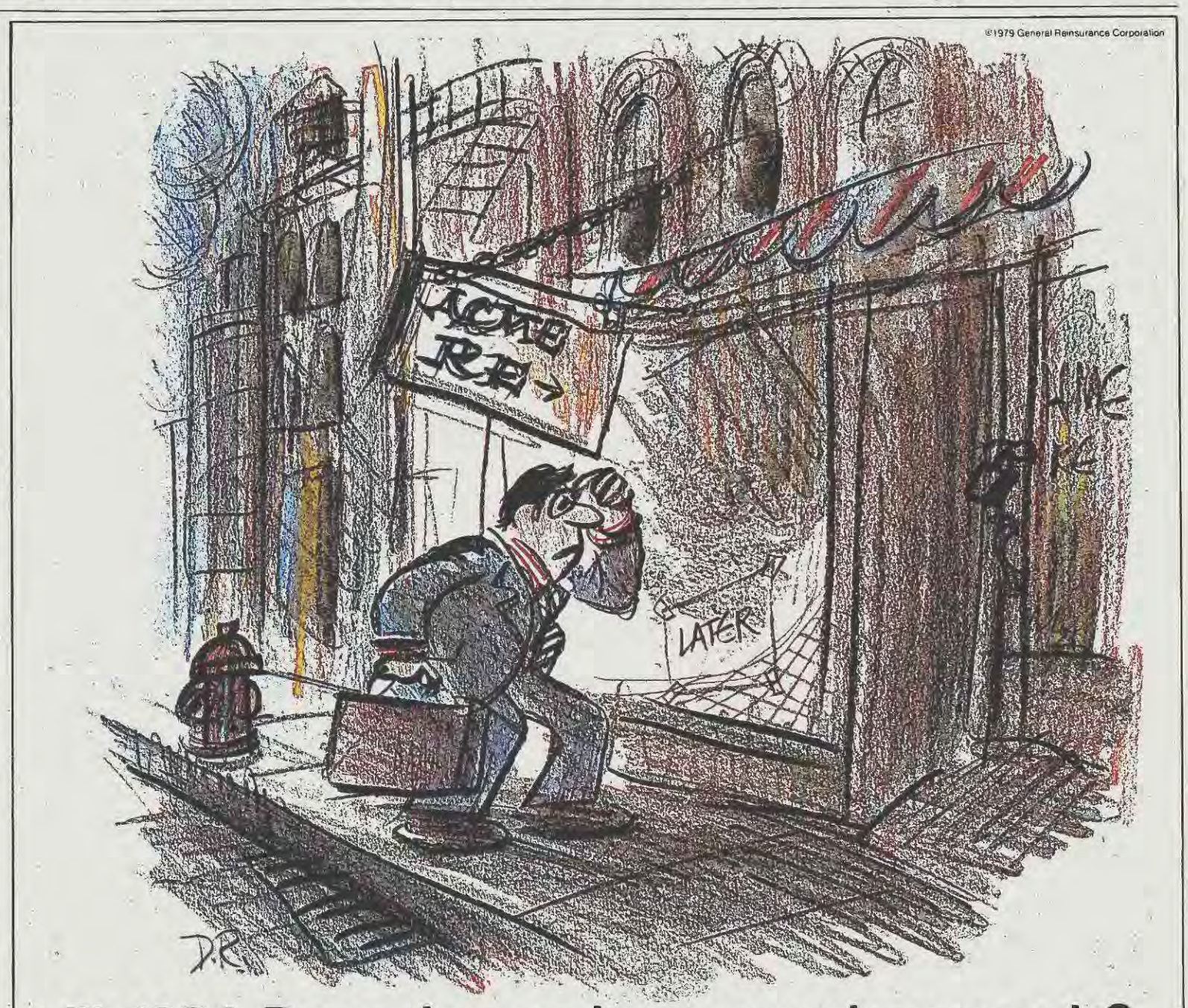


Photo: Pest Control Magazine

Liability insurance to rid clients of pests was getting irritating for the pest control operators. Their trade association has organized a Bermuda insurer to offer $1 million of liability insurance.



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Association captives . . .

Continued from preceding page

Fire Marine & Inland Insurance Co. of Philadelphia for writing the insurance policies. Mutual Fire & Marine is not sharing in the risk.

Deductibles will range from $200 to $2,500 on each loss. The size of the deductible will depend on the amount of sales of a member. Above that, Pestco will provide up to $250,000 of coverage on a per occurrence basis with a major reinsurer picking up the next $750,000.

The rate for coverage will be $1.10 per $100 of sales. Members had been charged 93 cents to $2.90 per $100 of sales by insurers.

After the first two years of the program, rates will be adjusted to reflect individual companies' loss experiences. Mr. Keith believes that Pestco's premium flow during its first full year of operation will be about $990,000 covering members whose sales total $85 million.

Captive & Self-Insurance

Eventually, Pestco has the potential to attract up to half of the trade group's 1,900 active members. "Right now, my phone is ringing off the hook from members who have been hit with huge premium increases at renewal time and who now want to join Pestco," Mr. Keith said.

Meanwhile, the National Fertilizer Solutions Assn. of Peoria, Ill., is on the verge of establishing a Colorado captive to provide members with probably up to $500,000 of coverage for a broad range of liability risks.

Mr. Kersten of Glendale Risk Management anticipates that the captive would have an annual premium flow of $2 million after the first full year of operations.

The fertilizer solutions trade group began considering alternative insurance programs when some members began having difficulty obtaining product liability coverage while others were hit with "exorbitant" premium increases, Mr. Kersten said.

"Premiums in some cases jumped 500% or 1000% in one year," he noted. "Based on extensive studies of members' loss experiences there is no justification for that kind of a premium increase."

The 35 to 45 association captives now in operation represent only a minute fraction of the estimated 20,000 trade groups in the U.S., experts observe. But due to the size of some of the associations—the 417 corporate members of the Chemical Specialties Manufacturers Assn. represent some $19 billion in sales—the trade association captives could become a significant factor in the insurance market. ■

Benefits plans

Self-insured firms ask: Can we service claims?

By ESTHER KUNTZ

CHICAGO—Many companies that self-insure their employe benefits programs are now analyzing their use of an insurance company to administer the claims against taking over the administration themselves.

Rohr Industries Inc. is planning to switch to an entire in-house program over the next few months. The company is adding five full time people to the staff to handle inquiries and to administer claims and anticipates a 20% reduction in costs with the self-administered plan, said benefits manager Doris Ramsey. "We also hope to give our employes better service," she added.

But 3M Co. benefits manager Donald Kissack says because 3M is a national corporation, it would be impractical to add staff to administer claims for offices from Puerto Rico to Hawaii. Besides, it would be difficult for a central office to keep up with the usual, customary and reasonable fee schedules for medical care in different localities, he explained.

"We use a number of Equitable offices throughout the country to do it. This has worked out very well for us. We have access to some expert claims officers," Mr. Kissack said.

The company wouldn't save money by administering claims itself, Mr. Kissack believes.

What the company might lose by not retaining an insurance company to administer the claims in keeping with local fee schedules might offset any savings, he explained. And there is the cost of additional people, Mr. Kissack said. With the self-insured program administered by the insurance company, 3M has been able to cut its benefits staff.

Benefits manager Donald Shovein of Control Data Corp. says he hasn't really investigated the possibility of reducing costs through self-administration because of its disadvantages. He prefers the buffer effect and expertise of a third party in administering claims.

Charles Nappi of Chase Manhattan Bank prefers to have an insurance company's medical director or a member of his staff determine the extent of disability or the length of a leave. He does not think the bank's staff could make such a decision with integrity.

But the Memphis Light, Gas and Water Division of the City of Memphis has found that it can give its employes better service by self-administering claims under its health care plan. "We can counsel our employes better than an insurance company because we know our own plan very well," said benefits manager Ruth Ann Harris. "Besides, it takes us only about one week to turn over a claim, which is much faster than an insurance company."

Ms. Harris says her four claims adjusters find it easier to keep up to date on fee schedules because the company is local. But the company does retain an outside consultant to audit claims and arbitrate claim disputes, the benefits manager noted. ■

Railroads pay for unsafe ways

WASHINGTON—The nation's railroads were slapped with $7.5 million in fines for safety violations in fiscal year 1978, more than double the amount collected in the previous year.

The $7,559,439 in fines also exceeded the total amount of fines collected by the Federal Railroad Administration from 1967-1976, by $110,000.

"We are not proud of this huge increase in fines for it shows that the railroads are not complying with minimum safety standards," said Federal Railroad adminstrator John M. Sullivan. "But we must use every means at our disposal to protect the public against possibly disastrous accidents," he explained. ■

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Universities talk in circles about forming a captive

NEW YORK—Eleven Eastern universities are delaying plans to establish a group captive insurance company because of a "Catch 22" quandary that developed at a December meeting to finalize the group's captive feasibility study.

Some universities won't make a commitment to use the captive until the feasibility report is complete. But, the report can't be formalized until all the universities make a decision on the captive so it can be set up with coverages tailored to each university's needs.

"It's quite a challenge for the

Captive & Self-Insurance

consultant to come up with a model" for the universities, said Stanley Tarr, director of risk management at Rutgers University.

Johnson & Higgins was hired to conduct the feasibility study for setting up a captive to write buffer layers of insurance for the universities.

Mr. Tarr, who has spearheaded the universities' efforts, is "anxious to make another pitch" to the universities when they meet January 17 to again discuss setting up the captive. "We'll have to have it implemented soon."

"I never understood how complicated it would be, but that's the problem with any group," Mr. Tarr said. ■

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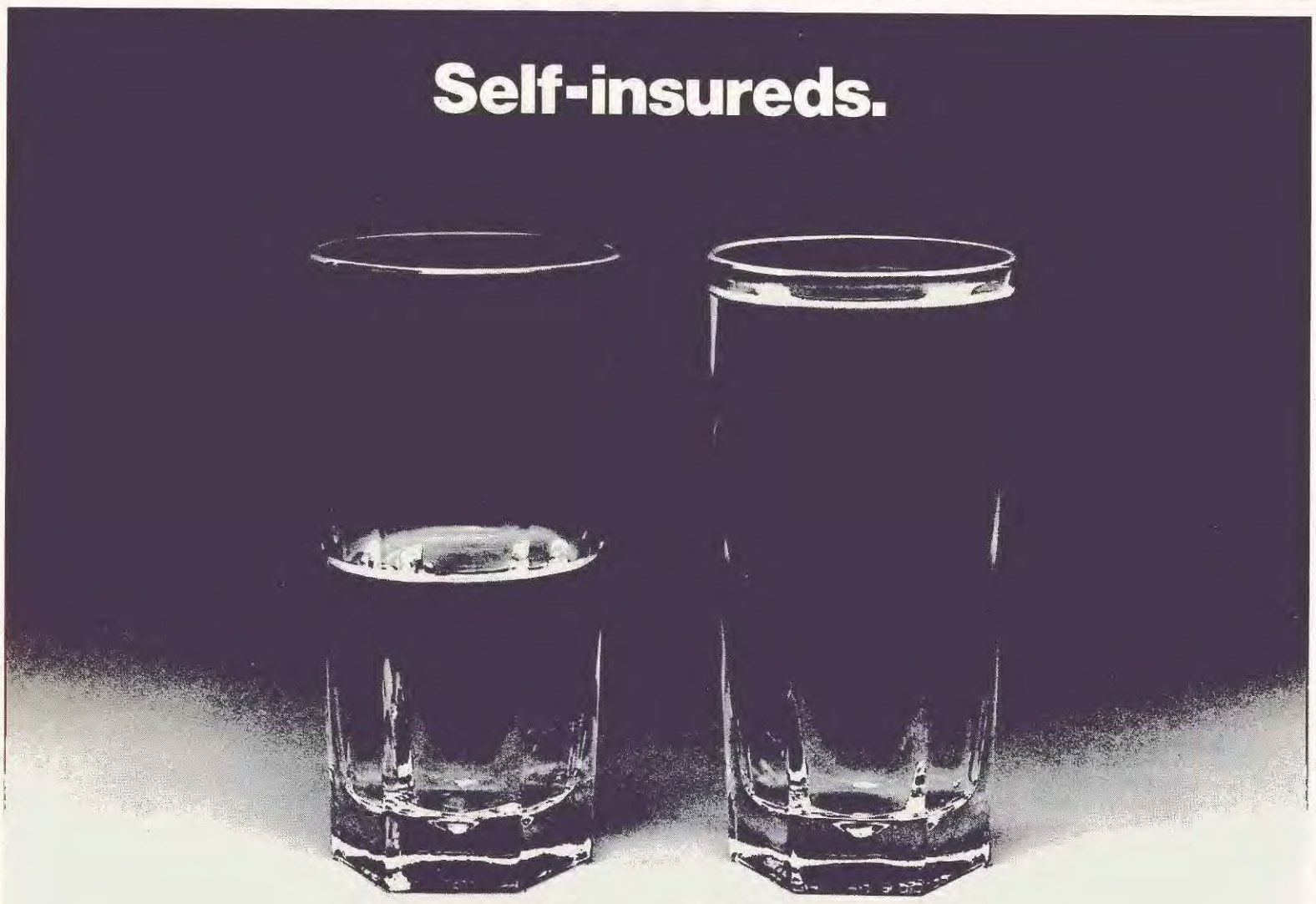

Don't think of them as business lost.

It's no secret, many firms these days are electing to insure themselves. At least for primary limits. Instead of looking at these accounts as the proverbial glass that's become half-empty, smart agents and brokers see them as a glass ready to be refilled. Ready prospects for Excess of Self-Insured Retention (SIR) coverage.

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dates for buyers

JAN. 16-17. RCI Communications Inc. will present an advanced seminar in San Francisco on the **reduction of construction insurance costs.** Workshops will cover new material such as preparations for premium audits, rating plans for competitive proposals, management for professional liability, captives and self-insurance funding, determining insurance costs for construction bids, the London market and workers compensation guaranteed cost plans. Cost: $395, team fees available. Contact RCI Communications Inc., Suite 350, Building V, 10300 North Central Expressway, Dallas, Tex. 75231; phone 214-363-9656.

JAN. 17-18. How to profit from the London market by improving coverage and lowering costs is the title of a RIMCO seminar to be held in San Francisco. The program will cover an introduction to Lloyd's, the other London companies, security, role of the Lloyd's broker, role of the surplus lines broker, collecting a loss, role of a Lloyd's agent and how to present a risk for a London placement. Cost: $395, team fees available. Contact RCI Communications Inc., Suite 350, Building V, 10300 North Central Expressway, Dallas, Tex. 75231; phone 214-363-9656.

JAN. 22-25. Executive Protection is a workshop and exhibition sponsored by Indiana University to be held in Phoenix, Ariz. This is just one of many programs planned this year by the university's center for public safety training. The workshop will be repeated **April 30-May 2** in Indianapolis. Cost of the workshop is $200. Contact Indiana University, Center for Public Safety Training, ISTA Building, Suite 400, 150 W. Market St., Indianapolis, Indiana 46204; phone 317-264-8085.

JAN. 22-28 The Cardio-Metrics Institute and the Human Performance Laboratory are the sponsors of a symposium on **health and preventive medicine in the corporate setting** to be held in Hollywood, Fla. The symposium will cover the role of industry in the control of preventable disease and health abuse with particular emphasis on the areas of stress, nutrition, physical activity, heart disease and alcoholism. Current research findings will be presented and discussed by medical authorities and selected corporate health programs will be reviewed. Cost: $475. Contact Cardio-Metrics Institute, 295 Madison Ave., New York, N.Y. 10017.

JAN. 23-25. The Risk Research Group is offering a course on how to establish, operate and manage a captive at the Marriott Hotel in Amsterdam. Feasibility studies, underwriting, selection of location, accounting and taxation, loss control and claims, reinsurance and methods of management are topics to be covered. Contact Gillian Morley, Risk Research Group (London) Ltd., Bridge House, 181 Queen Victoria St., London, EC4V; phone 01-236-2175.

JAN. 28-31. The insurance and protection division of the American Bankers Assn. is sponsoring a **risk and insurance management in banking** seminar at the Hilton Palacio Del Rio in San Antonio, Tex. The seminar is designed to provide executives responsible for a bank's insurance program with knowledge of risk and insurance management techniques with special emphasis on loss control methods, minimizing insurance broker and company service and the bankers blanket bond. Other topics include properly insuring against losses arising from directors and officers liability, ERISA and other fiduciary liabilities and electronic funds transfer system participation. Cost is $225. Contact Nancy Krakover, Registrar, Insurance and Protection Division, American Bankers Assn., 1120 Connecticut Ave. N.W., Washington, D.C. 20036; phone 202-467-4049.

JAN. 29-FEB. 1. Financial Costing in Risk Management is an advanced seminar to be offered by The University of Dallas. The seminar will examine the impact and timing of risk management accounting decisions with an emphasis on the identification of accounting decisions in self-

insurance and captive operations, the allocation of risk management costs to various divisions and the building of a risk management operating budget. Cost is $345 for RIMS deputy members and $375 for others. Contact Professor Bruce Evans, The University of Dallas, Management Laboratories of America Inc., Irving, Tex. 75061; phone 214-438-1123 ext. 360 or 214-438-5765.

FEB. 1-2. The Wharton School of the University of Pennsylvania will sponsor a two-day seminar on dealing effectively with **change in a complex organization** in Chicago. The seminar will emphasize the importance of analysis and evaluation techniques in the change process, offer ways to combat resistance to change within the company, finding the right approach to change for your company and examining why some changes fail and others succeed. The seminar will be repeated in **New York on April 2-3.** Contact Heidi Kaplan, Dept. 20NR, Wharton Conference Center, 360 Lexington Ave., New York, N.Y. 10017; phone 800-223-7450.

FEB. 5-6. The THEOREM Institute is offering a seminar on **workers compensation costs** at the Holiday Inn in Downtown Atlanta tailored to the problems facing law enforcement agency managers, personnel directors and city/county government managers. The two-day course will stress the practical aspects of evaluating workers compensation program administration with an emphasis on alternative approaches. The seminar will also examine cost effective procedures, program modifications and the self-insurance v. insurance issue. The afternoon sessions will include workshop case studies and evaluations. Cost is $200; groups of three or more entitled to a 20% discount. Contact Michael O'Neill, President, THEOREM Institute, 1737 N. First Street, Suite, 590, San Jose, Calif. 95112; phone 408-294-1427 or 800-538-6896.

West Coast firm seeks excess risks

SEATTLE—SAFECO Insurance Co. will increase its excess and special risks underwriting as a result of an underwriting management agreement with EASI Insurance Services Inc. of San Francisco.

SAFECO has written excess and special risks policies on a limited basis. Now agents representing SAFECO can have excess and special risk coverages issued on a SAFECO policy, said assistant vp John Gettles.

The insurer had excess capacity and now has a facility to handle this business, said SAFECO president Bruce Maines.

Most of SAFECO's commercial business currently comes from the "Main Street mercantile market," Mr. Gettles noted.

EASI specializes in underwriting excess coverages, including umbrella excess and layered excess policies, according to president Garrett Redmond.

The firm also had underwriting management agreements with Lumberman's Mutual, Excess Insurance Co. of London, Sarpo Mutual of Finland and Canadian General Insurance Co. of Toronto. These companies reinsure policies written by each other, Mr. Redmond said.

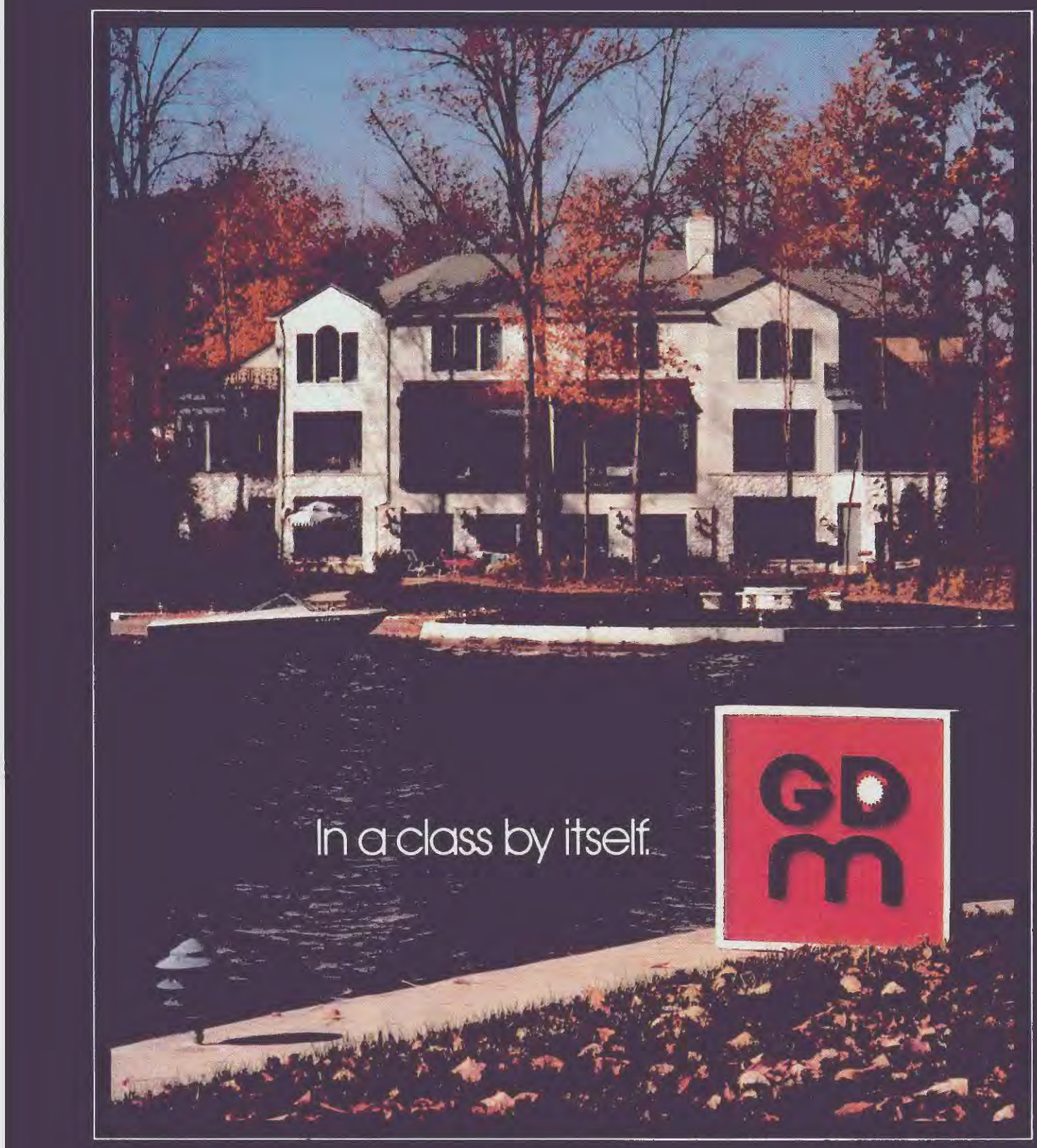
In addition to its San Francisco headquarters, EASI maintains a branch office in Los Angeles and plans to open offices in Seattle, Cleveland and other principal markets. ■

FEB. 7. The International Foundation of Employe Benefit Plans is offering a comprehensive one-day program examining **current problems and important issues in the employe benefit field** in Seattle, Wash. Future programs will be held in San Francisco, **Feb. 8;** Columbus, Ohio, **Feb. 28;** Pittsburgh, **March 1;** St. Louis, **April 25;** Chicago, **April 26;** Milwaukee, **July 18;** Bloomington, Minn., **July 19;** Buffalo, **Aug. 1,** and Boston, **Aug. 2.** The program will cover the end of mandatory retirement, effective benefit communication programs, legislative and regulatory developments. Cost is $90 for members and $115 for non-members. For more information on locations contact The International Foundation of Employe Benefit Plans, P.O. Box 69, Brookfield, Wis. 53005; phone 414-786-6700.

FEB. 15-17. Union Planters National Bank is holding a second **fidelity bond claim seminar** which will be held at the Tamarron in Durango, Colo. It will examine executive fidelity, bond claims and related matters. Seminar participants will be shown how to file and pursue a claim, possible consequences of the claim, the insurer's part in the claim, legal strategies if a claim is not paid and steps to reduce fidelity bond claims. Cost is $495. Contact Union Planters National Bank of Memphis, James A. Cook Jr., Special Assistant for Financial Affairs, 67 Madison Ave., Memphis, Tenn. 38174; phone 901-683-1985.

MAR. 12-16. The American Society for Industrial Security will present an **assets protection course** at the Davidson conference center at the University of Southern California. The course will review the fundamentals of loss prevention and will provide principles, practical plans and techniques for cost effective security and asset protection. Cost is $475 for members and $525 for non-members. Contact The American Society for Industrial Security, 2000 K St. N.W., Suite 651, Washington, D.C. 20006; phone 202-331-7887.

MAR. 20-22. The third international **captive insurance** company conference sponsored by the Risk Planning Group Inc. will be held at the Princess and Bermudian Hotels in Hamilton, Bermuda. The program will review important events in the captive insurance industry during the past year, the growth and development of captives and IRS tax rulings. Funding employe benefits through captives and developing "outside business" for captives will also be examined. Contact Micki Briskin, Conference Coordinator, Risk Planning Group Inc., 722 Post Rd., Darien, Conn. 06820; phone 203-655-9791.



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The Widening World

Simplified placement of insurance, cost benefits, and the availability of professional management services are all factors behind the continuing growth of captive insurance companies.

A brief review by INA of an insurance topic of interest to business executives.

For a growing number of American companies, the insurance subsidiary or "captive" is an idea whose time has arrived.

There are now at least 1,000 captives, both individually and group owned, operating worldwide. Over a hundred have been formed in the last two years alone. Moreover, with costs continuing to escalate for full risk protection through conventional policy coverage, captives are expanding both the volume and scope of their underwriting activities.

Most captives were originally formed to write insurance for the parent company or group only, but as they grew in experience (and in capital surplus) some began to accept risks from unrelated outside companies. This makes the captive more of a full-fledged insurance company, with possibly important tax consequences.

At one time, a captive was considered feasible only for the very large company or trade association, and the capital outlay required may still rule out a wholly-owned captive for many companies. But many captives are now being formed by groups and medium-sized firms.

The Bermuda angle

Many captives today – about 700 of them – are based in Bermuda, where capitalization requirements are less stringent and investment and financial reporting rules more relaxed. American multinational companies that do not restrict their captives to doing business with the parent company find Bermuda particularly advantageous, since income derived from overseas insurance operations is not taxable until the funds are repatriated.

With the advent of the captives, Bermuda has become a world insurance center, handling as much as two billion dollars in premiums each year. Of this, as much as $500 million is outside business not related to the captives' sponsors.

What has led companies to establish captives? Essentially, a captive represented an extension of the self-insurance trend – a

# of Captive Insurers

reaction to situations in which commercial coverages for certain risks had become either unavailable or prohibitively costly.

Lower expense ratios

Today, however, with commercial insurance less restricted, the motives are largely financial.

When insurance is placed directly with the captive, a company may be able to realize a savings of the commercial insurer's overall administrative costs. On the other side of the ledger is the cost of executive time, as well as any fees for the captive's management.

In addition, retention of premium reserves by the captive instead of an insurance company can have important cash flow advantages for the parent company. Such funds may be legally available for company investments that otherwise might have to be financed through bank loans. And the fact that a captive can reinsure a large part of its risks can mitigate against the disastrous loss – at reinsurance rates that can be lower than those for primary insurance.

Backing and fronting

Reinsurance, in fact, can play a key role for a captive, since many parent company risks are too large for a captive to handle without the backing of another insurer.

In one arrangement, the parent company pays premiums directly to the captive for primary insurance, but a large amount – say 80% – of the risk is immediately transferred to a reinsurance company. Or, in another arrangement called "fronting," the parent pays all premiums to a primary insurer, which then cedes perhaps 50% of the risk to the captive as the reinsurer. In some cases the captive handles part of both the primary and reinsurance coverages.

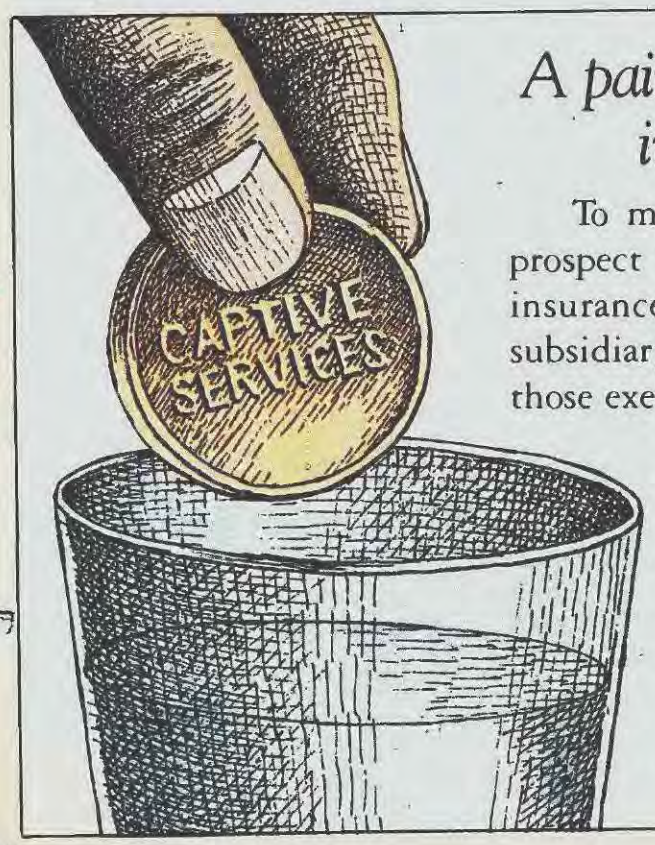
All of these arrangements involve some major tax considerations. In general, the IRS today disallows the tax deduction of premiums paid to wholly-owned captives, except to the degree that the risks are shared by other insurers, on the ground that such captives are merely a form of self-insurance. Challenges to this IRS ruling are now in the courts. If, however, the premiums go to a captive organized by a group and not dominated by any one company, they are likely to be deductible.

A decision about setting up a captive can be difficult. The first step should be a comprehensive survey of the company's risk exposures and insurance coverages, together with all other relevant factors such as cash flow and financing considerations. If the study suggests that a captive is advisable, insurance brokers and some insurance companies – including INA – can be instrumental in its creation and management.

* * *

The Insurance Company of North America was founded in 1792 in Independence Hall, Philadelphia. Today it is the largest component of INA Corporation's international network of insurance and financial service companies. In property and casualty insurance and risk management services, life and group insurance, health care management, and investment banking, INA and its affiliated companies offer a unique combination of products and services to business and industry around the world.

INA insurance products and services are available through selected independent agents and brokers. For an informative booklet on current trends in captive insurance, write INA, 1600 Arch St., Philadelphia, Pa. 19101.



A painless way to acquire insurance experience

To most company executives, the prospect of sudden immersion in the insurance business via an insurance subsidiary is not an enticing one. For those executives, some insurance companies and brokers have a solution: working with the risk manager, they can provide all the management services needed by a captive – including underwriting, financial management, loss control and claims handling.

INA

The Professionals

Self insurance isn't exactly a new idea.

At NWNL, we were involved with self insurance protection of all kinds almost from the beginning. Now we'd like to tell you a few of the things we've learned. So we've drafted a booklet that explains why—and under what conditions—you should consider self insurance for employee benefits.

It explains the risks, the costs, and the codes of conduct influencing this trend to self protection, as well as the variety of plans available. For your copy of the booklet, just send the coupon or write on your letterhead.

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PERSPECTIVE

Captive insurer movement develops a sense of history and opportunity

Special from The Economist
Dec. 2, 1978

WHEN THE TANKER Amoco Cadiz went aground last summer, spilling oil all over Brittany's beaches, Shell lost oil worth $23 million. It claimed damages from an obscure outfit in Bermuda called Petrol Insurance Ltd.

When Ford's European parts warehouse in Cologne burned to the ground last year, the insurance check, for over $200 million, came from another small Bermudian company, called Transcon Insurance.

Why did Shell and Ford entrust their immense risks to tiny and unfamiliar insurers rather than to the giants of the world's insurance business? Because Petrol Insurance and Transcon belong to Shell and Ford themselves.

Along with 1,000 other "captive" insurance companies in tax havens like Bermuda, Grand Cayman and Guernsey, they were established as part of their multinational parents' never-ending struggle with taxmen and foreign exchange authorities.

"Captives" are simply insurance companies set up by large industrial companies (and more recently other institutions ranging from skate-board parks to universities) to insure their own risks. They have existed since the 1920s, when companies such as ICI, BP, Unilever and British American Tobacco—or their forerunners—all set up insurance subsidiaries. In the past few years in America, captive formation has grown from an exotic tax-avoidance technique into a major part of many large industrial companies' corporate strategy.

Few companies paying more than $500,000 in insurance premiums have not considered forming a captive. The list of distinguished corporate names with insurance subsidiaries in Bermuda now includes over 600 companies, ranging from Exxon and Boeing to Colgate-Palmolive and Levi Strauss. These Bermudian captives have assets of close to $1 billion.

Groups of American doctors, lawyers, accountants and even soil engineers, appalled by soaring liability premiums, have also jumped on the captive bandwagon.

Americans have been in the vanguard of the captive movement, but innovative European companies, including Beecham, Glaxo, Fisons, Tesco, Philips, Ciba-Geigy and Electrolux have not been far behind.

Captives are created for a complex collection of financial and fiscal reasons. Tax inspectors regard them as just another tax avoidance ruse, while risk managers praise them as an essential part of their insurance arrangements. Both are right, from their different points of view.

To begin with the manager's: Self-insurance saves money. Less than 70% of the average insurance premium is recovered in claims. The remaining 30% is absorbed by brokerage, the insurer's overheads and profit margin. So it is a waste of money for a company to buy insurance for the sort of small losses that it can absorb as a working expense, without ruffling its profit and loss account.

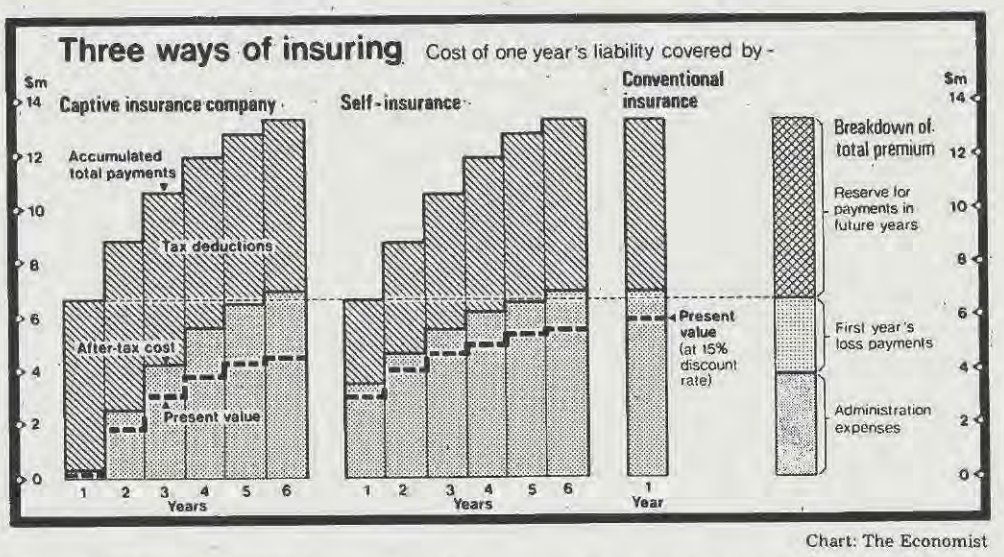


Chart: The Economist

Companies with better-than-average loss control can save more than the average 30%. Some companies consistently have very low ratios of losses to premiums, because insurers do not recognize that they are safer than other companies in the same industry.

Self-insuring can actually help to reduce losses. "The insurance will always pay up" is a less comforting thought when the insurer is a senior executive at head office, who will be looking for someone to blame if he has to pay out. A company may decide to divert money that has gone on insurance premiums into loss control measures.

Although most companies that set up captives have better than average loss experience, the average company can also benefit from self-insurance of the kind of risks that take years to investigate and settle, such as the side effects of a drug or the consequences of an error in engineering design.

Continued on page 52

Speaking Out

Safe underwriting: A bromide and insight

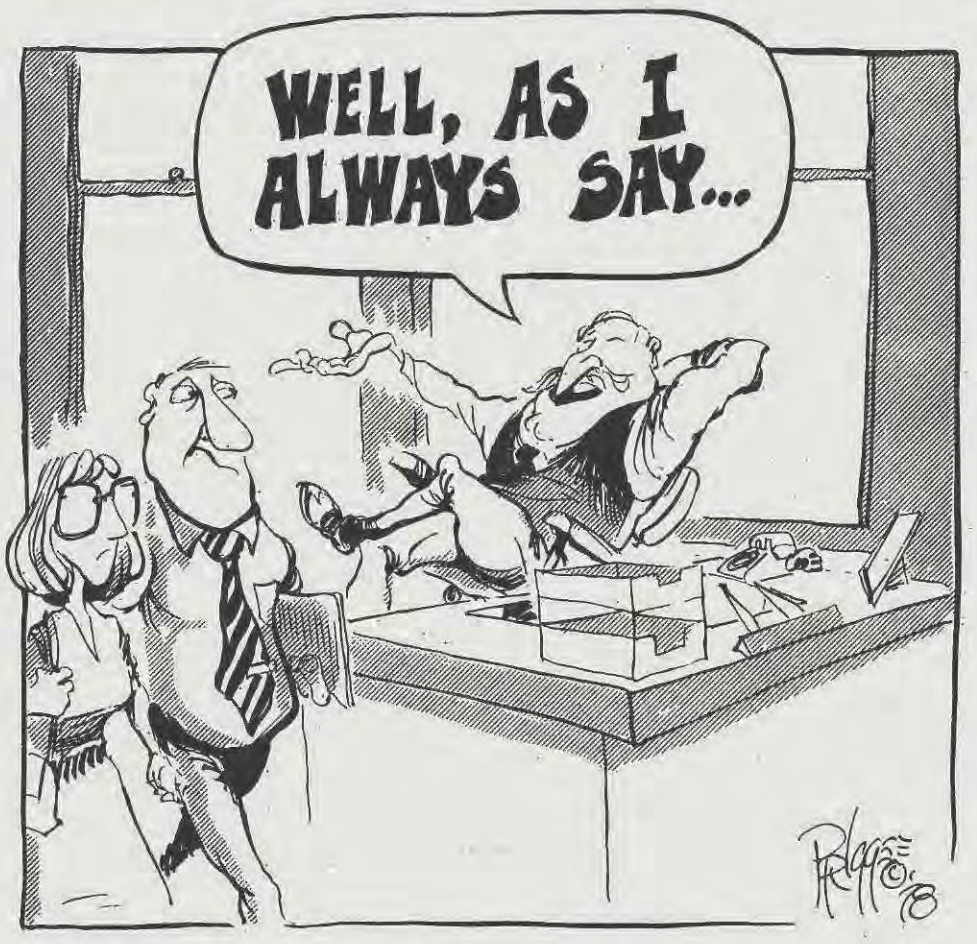
By Peter Downes

AN EMPLOYER OF MINE in my London days had a fund of truisms, cliches and bromides which he would trot out with almost predictable frequency. The amusing part of it was that he would sometimes be a mite careless and would verbalize bromide A when he really meant to use cliche B. Based on this element of uncertainty, we used to bet on what he would actually say, losers paying for morning coffee.

For instance, we had a lot of business from religious institutions on our books. Anytime a piece of such business passed over his desk he would almost invariably remark, "Church people may be good, but there is nothing good about churches—fire traps every one of them." Then came the morning when he was told that a Pentecostal chapel had burned down and we all waited expectantly for the inevitable. But he surely must have had something else on his mind because his actual comment was, "Like I always say, there is no good business to be found in bars." I bought the coffee that morning.

I was reminded of him while I was reading a news item reporting that the American Insurance Assn. had recommended improvements in the "Early Warning System" which would make early identification of financially troubled insurers that much more effective.

My old boss, in common with Winston Churchill, whom he much admired, was a one-page man. If you could not come up with a summary of any problem or method in one page or less, the first thing you would hear would be bromide number 26, "If you cannot say it in one page or less, it is not worth saying in the first place," or number 32, "Anything complicated which cannot be said simply is not worth a damn."



He would have approved of the American Insurance Assn. recommendations. Like the rest of us, he had no use at all for rate regulation and as a Lloyd's broker deplored insurers who did this voluntarily. "Underwriters who subscribe to tariffs don't know the first thing about underwriting." He did nevertheless approve of financial regulations and solvency requirements and as might be expected had an aphorism ready at hand which dealt with the matter: "Anybody who goes bankrupt cheats his customers as well as himself."

He often complained that so far as insolvencies were concerned there was no foolproof way of detecting danger signals in advance and that all published accounts did were to tell us what had happened after the event. "What we need," he used to say, "is a system which will tell us the status of companies and underwriters on a daily basis, but I cannot see it happening in my lifetime." He was right about that too, since he died not long after computers and CRT's came on the scene.

We once pointed out to him that even if a Lloyd's syndicate went under, the guaranty fund would take care of the problem and as for insurance companies, at that time there had not been a bankruptcy for more than 20 years. There was a short pause while he mentally located the appropriate piece of wisdom for the occasion, "Children should be seen and not heard; a guaranty fund should be there and not used." So what if it was a nonsequitur; he knew what he meant, and I guess we did too.

As for insurance companies, I well remember the occasion when he stopped at my desk and told me that under no circumstances was I to place any more business with a certain insurer and to withdraw anything already placed as soon as possible. He was the boss, of course, and I would do as he told me, but I wondered why and asked him. He hemmed and hawed and started this explanation and that, none of it making any sense. Finally, he snorted impatiently, "Because they smell funny, that's why!" Three or four years later the British Commercial Insurance Co. went down the drain with a noisy gurgle.

It seems in retrospect as if his instincts

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Peter Downes, manager of insurance for the American Trading & Production Corp. in Baltimore, is the most prolific contributor to the Speaking Out column on these Perspective pages.

PERSPECTIVE

Underwriting Agencies Handling Third-Party Business for Captives

	ALLIANCE REINSURANCE	BLADES GROUP	BERMUDA FIRE & MARINE	PRUDENTIAL REINSURANCE MGMT. UNDER. FAC. (MUF)	KEMPER RE. BERMUDA
Type of Facility	Quota Share Retrocession	Underwriting Agency	Underwriting Agency	Quota Share Retrocession	Quota Share Retrocession
Years in Operation	4	7	1	2	1
No. of Participants — 1978	13	7	14	40	5
Minimum Capital Preferred	$1 million	$2.5 million	$2 million	$2 million	$5 million
Total Premium Written	$3,500,000	$30 million	$5 million	$15 million	$10 million
Est. Premium/Captive	$350,000	Avg. $3 to $4 million	$300,000 avg.	$300,000	$2 million
Guarantees or LOC's	Required for smaller captives	None	Required upon withdrawal	Required for unearned premiums and loss reserves	No
Type of Business Underwritten	U.S. Property Excess Catastrophe	Worldwide Book All Lines	London Reinsurance Property & Casualty	U.S., Canadian & P.R. Excess	Primarily U.S. & Canada Book of Business Some direct business written in Bermuda market
Senior Underwriters	Jim Lyons Joe Sheehan	Robin Spencer Arscott AlanTaft	Joseph Sutton	Prudential Reinsurance Dryden & Co. • Paul Ingrey • Ross Cowan	Kemper Re. U.S. • Frank Alderidge Ted Koeh H. L. Kennicott
Catastrophe Protection	Yes	Yes	Yes	No	No
Retrocessions Permitted	Not prohibited	Yes	Yes	Discouraged	Not prohibited
Premium Reserves	Yes—Held by fronting carrier	None	None	No	Held by Kemper Re. for premium & loss reserves
Other Reserves	None	None	None	IBNR reserve held	No
Interest on Reserves Held	None paid	—	—	No	Full investment income less .25% management fee to Kemper Financial Services
Fees: Fixed	2% fronting 4% agency fee on premium	4% on net premium	5% property 7.5% casualty	Treaty = 14% of gross premium Facultative = 6.5% of net premium	
Profit Sharing	No profit sharing	15% of underwriting profit	None	25% after participants have earned 7.5% Unlimited carry forward	Not available
Foreign Exchange Exposure	None	Managed by Blades Group	Captive responsible	None	None
Minimum Participation Period	1 year	None	None	None	Expect long-term relationship
Withdrawal Notice	120 days	90 days	60 days	180 days prior to next underwriting year	90 days
Information Contact	John Lepire	Joe Blades	Cyril Rance	Ross Cowan	Ted Hoeh H. L. Kennicott

Prepared by Joseph A. Destein, president, Risk Science Group Inc., Santa Monica, Calif.

CORROON & BLACK/ ALEXANDER COCKBURN	BRITAMCO	ALEXANDER UNDERWRITING AGENCY (AUA)	BACCALA & SHOOP	AIG AIM/SUMIT	BELLEFONTE	UNION INDEMNITY INSUR. CO. OF NEW YORK
Underwriting Agency	Underwriting Agency	Underwriting Agency	Quota Share Retrocession	Quota Share Retrocession	Retrocession	Quota Share Retrocession
4	1	1	4	AIM-3 SUMIT-1	5	1
5	4	7	1/1/79 20	9 plus AIG	6	8
$2.5 million	$5 million	$1.5 million dedicated	$3 million	$5 million	Not specified	$1 million
$11 million	Over $100 million	$25 million	$10 million	$10 million	$180 million	$4 million
$2 million avg.	—	$3 to $4 million	Minimum $1 million Maximum 2 x capital	$1 million	Maximum 3 x capital	$200,000
No	Letter of credit required upon withdrawal	Letter of credit required for premiums released	Letter of credit for unearned premium and loss reserves	Letter of credit for premium released	Required	Letter of credit for unearned premium and loss reserves
Worldwide, Non U.S. Treaty 1979 will enter U.S. business	Worldwide all lines 75% U.S.	London Reinsurance	U.S. Property and Casualty	Worldwide Property & Casualty AIM excludes U.S. SUMIT includes U.S.	Worldwide	U.S. 15% Property 85% Casualty Excess & Catastrophe
Alex Cockburn John Harris	Leslie Dew Peter Foley James Parkinson Ralph Bailey	Jack Carpenter Charles Seymour	Harry Petru James Keegan Bill Whiteford	AIG Worldwide Source Underwriting	Bellefonte London with C. G. Heath Bellefonte U.S. Treaty Underwriters	J. R. Wiedeman
Yes	Yes	Yes	Available if requested	AIM—Yes SUMIT—Not yet	Yes	Yes
Based on circumstances	Discouraged	Yes	Yes	Discouraged	Yes	Discouraged
No	None	Released by letter of credit	Released by letter of credit	None	Yes	No
Working balance reserve	None	None	None	None	None	No
Yes—Totally	—	—	—	—	N/A	—
4.5% of gross premium	4.5% average fixed fee	2.5%fee 3% estimated expense charge on net premium	9% on net premium	2.5% treaty 5% facultative	N/A	2.5% treaty 5.0% facultative 10.0% direct
15% on underwriting	25% of underwriting profits	15% of underwriting profits	20% on property underwriting profits	25% of underwriting profits		20% of all lines
Yes—Managed by agency	Company monitors	Captive responsible	None	Captive responsible	N/A	No
Expect long-term relationship	3 years	3 years	None	3 years	1 year	2 years
6 months	12 months	6 months prior to renewal	105 days	6 months	90 days	90 days
Alex Cockburn John Harris	Leslie Dew	Robert Gielow	William Baccala	Richard Williams	Rick Rodgers	J.R. Wiedeman

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PERSPECTIVE

Captive opportunities . . .

Continued from page 49

While the lawyers argue, premiums are being accumulated by the insurance company, which may not have to pay out for up to 10 years. With self-insurance, the company, not the insurer, has the use of this money.

All these are reasons for large companies to shun the conventional insurance markets and to rely on self-insurance. But why convert straightforward self-insurance reserves into full-fledged insurance companies?

- Captives have a big technical advantage over self-insurance funds. They have access to the wholesalers of the insurance business, the reinsurance companies. Because reinsurers deal only with proper insurance companies, they often provide cover much more cheaply and on more flexible terms. Even the largest captives reinsure themselves against really big losses or let direct insurers share part of their risks as coinsurers. In the Ford warehouse fire, for example, Transcon collected all but $5 million of its losses from reinsurers and coinsurers. Sometimes the captive acts as reinsurer. The company insures with a local insurer which then reinsures anything up to 95% of the risk with the captive. Such "fronting" arrangements enable the company to satisfy local insurance requirements without losing the benefits of self-insurance.
- Setting up a proper insurance subsidiary makes managerial sense. It may help to prevent insurance reserves being raided for other purposes.
- Most importantly, captives offer tax advantages. Insurance premiums are tax-deductible. But only in Holland and Scandinavia are the taxmen willing to treat contributions to self-insurance reserves in the same way. Elsewhere, companies get tax deductions only when they actually pay out for a loss.

IRS evasion

But even if a captive is taxed like an ordinary insurance company it still has a problem. If the captive does not have a very wide spread of risks, it may find that its underwriting profits swing widely from one year to the next. When the parent company has a lucky year, with few losses, the captive makes big profits and is heavily taxed, making it harder to build up reserves for the unlucky years that will eventually come. An ordinary insurer with a very wide spread of risks should not have this problem.

In the 1950s a group of lawyers and insurance brokers in America found a way round this handicap which also enabled companies with captives to save tax and not just to defer it. They simply told their clients to base their captives in tax havens. A captive in Bermuda, which received more premiums from its parent than the losses it had to pay out, could accumulate tax-free underwriting profits and investment income out of tax deductible insurance premiums. Its accumulated reserves could then be used by the parent for investment round the world.

In the early days, a captive's very existence was shrouded in secrecy, in the hope of avoiding challenges from the tax inspector. But the United States Internal Revenue Service (IRS) soon caught on and started to look for legal principles with which to attack the captives.

In 1962, it declared that captives which insured risks situated in the United States would be taxed as domestic companies, wherever they were based. The other prong of the early IRS attacks on captives was to challenge the levels of premiums they charged their parents.

IRS attacks

In the early 1970s, the Exxon and Mobil Oil captives agreed to reduce their premiums to below the level charged by open-market insurers because of their lower administrative costs and better loss experience. For standard types of risk few captives would dare to charge their parents exorbitant premiums today. But for unusual risks such as confiscation, strikes or libel it is hard for the IRS to prove that the captive is charging too much.

Meanwhile the IRS was developing a more powerful theory, which it formally produced last year. Britain's inland revenue, which has been watching the action fairly quietly, would no doubt like to destroy captives' tax advantages if the IRS showed the way.

In effect, the IRS asserted that captives are not insurance companies at all. Genuine insurance, argued the IRS, requires the spreading of risk: Paying a premium to a wholly-owned subsidiary that insures only its parent's risks is simply transferring money from one corporate pocket to another. There is an "economic identity" between captives and their parents and no risk spreading can take place. So:

(a) premiums paid to a captive will not be tax deductible;

(b) premiums paid to a captive by a foreign subsidiary will be regarded as "constructive dividends" to the American parent;

(c) loss payments by the captive to the parent will be regarded as dividends or capital repayments.

This blanket condemnation has been followed not by the collapse of the captive movement, but by its expansion. In Bermuda, the number has grown by 30% since mid-1977, for three reasons:

- Many companies are now convinced that captives can be profitable even if the IRS treats them as cruelly as self-insurance reserves.
- Some tax experts in New York simply do not believe that the IRS position will survive a challenge in the courts. The first court decision, on a case brought by Carnation Co., is expected in the next month or so.

The IRS position was first stated, informally, back in 1972. But there has never been a court ruling, because both companies and the IRS have preferred out-of-court deals. Companies find their captives are convenient bargaining counters.

- The IRS's theory applies only to a very "pure" type of captive—one which is wholly owned by one company and insures only that company's risks. Two obvious ways of circumventing the ruling are for several companies to set up a "group captive" or for a single-parent captive to start insuring outside risks.

This autumn the IRS published a ruling which recognized a company called Oil Insurance Ltd. (OIL), formed in Bermuda by 31 oil companies to cover their pollution liabilities, as a genuine insurance company. Since the parents were not economically related, the IRS agreed that risk-shifting was taking place. Would this not apply also to a captive with only two parents?

More dodging

Another loophole is available for captives prepared to insure risks not related to their parents. The consensus in Bermuda is that a captive that derives 20% of its premiums from risks unrelated to its parent should certainly skip through the IRS net.

There is even a feeling among captive managers that the IRS attitude has given their business a major boost, since some of them have been urging their clients for years to start covering outside risks. They have argued that this can increase a captive's stability, make better use of the vast amounts of capital that some of them have accumulated over the years and reduce management costs.

At the moment there are 70 to 100 captives insuring outside risks, mainly through pools organized by one of the captive management companies in Bermuda. But some captives have taken a braver course and have started independent underwriting. The largest of these, Belefonte Insurance, owned by Armco Inc. had premium income of $207 million in 1977 and is no longer regarded as a captive. Gulf Oil's subsidiary, Insco, which recently hired a deputy chairman of Lloyd's to be its underwriter, is moving the same way.

With enough capital already to support over $2 billion of insurance premiums, the captive insurance industry seems destined to grow into a major force in world insurance. ■

Cap health claim costs in self-funded programs

By Steve Lockwood

IN RECENT YEARS the rise in health care costs has forced many firms to look for alternative methods of funding their employe benefits programs. Two of the more popular vehicles have been administrative-services-only (ASO) contracts and self-insurance through third-party administrators. One of the basic reasons why these forms of funding have not been more widely accepted is the open ended liability that the employer could face.

Recently many domestic insurance companies have developed stop loss coverage, but most require supporting lines which could disturb the entire benefits program. But it is still possible to obtain both specific and aggregate stop loss coverage (Lloyd's is one market along with some U.S. carriers) without any other accompanying coverages.

The specific coverage is intended to provide protection against any one claim adversely affecting the experience of the program. Deductibles, for example, can range from a minimum of $10,000 per claim up to $100,000 depending on the particular program design and need for the group. The amount of coverage available in excess of the deductible can vary from $100,000 to $1 million. These can be tailor-made to fit a particular program.

The aggregate stop loss coverage is intended to protect the employer from adverse fluctuation in the total claims paid in a given year. This coverage is designed to attach above a certain percentage of the expected claims during a given plan year. For example, if the expected claims for the 1977 to 1978 plan year were $500,000, underwriters might provide 100% reinsurance with an attachment point ranging from a minimum of 115% to a maximum of 150% depending on the merits of each case. Limits of $1 million or $2 million in excess of the attachment point are available.

Both specific and aggregate are available independently or can be purchased in combination with each other.

Steve Lockwood is a principal of Boston-based Lockwood, Dipple & Green Inc., specialty risk underwriters in excess-surplus lines.

Bromides and insight . . .

Continued from page 49

were always sound. He had such a feel for what was going on that he would know things without being able to articulate why he knew them. At the same time, however, he longed for objective criteria with which to measure his subjective judgments.

There would have been no point in explaining that by using multiple variate discriminant analysis techniques, a set of significant ratios would be produced. He would probably have remarked that all that nonsense could be left to the technical wallahs and in any event, what could they tell us? We would have told him, and I can imagine the responses he might have made.

First of all, we would have said, they show a two year operating ratio. ("Should be three years, same as Lloyd's.") We would have gently said that it was not the same thing at all but in addition the system would show the ratio of liabilities to liquid assets. ("They've got to show that now.") And besides that, any change in policyholders' surplus ratio. ("That's an absurd concept to start with.") Then net premiums written to loss and loss adjustment expense reserve ratios. ("That may help, but crooks will always lie and fools will always be with us.") And finally, changes in liability mix ratio. ("You mean if somebody writes something too heavy.")

After some heavy thinking, he would have wondered what the difference really was. The main difference, we would have told him, is simply that it is now possible to get a continuous update on these items so that we can learn how everybody stands, on a daily basis if necessary. We would further explain that the computer enables us to do this. Thereupon he might have asked, "How long have computers been around?" About 20 years, we would have told him. "Took their time getting around to it, didn't they?"

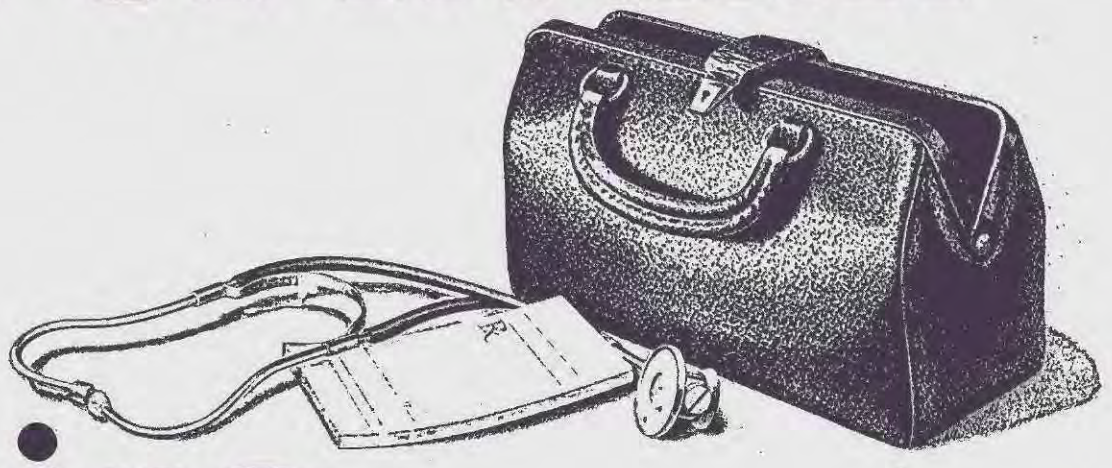
Thereupon if some wiseacre had then said that there would never be any doubt on such matters in the future, he would have stomped all over him. Indeed, he would have wholly approved the comment by American Insurance Assn. that their recommendations were no more than a tool and not a substitute for good judgment, to which he would probably have added, "Any more than an aperitif followed by an aperient is a substitute for a good meal." Just to ram the point home, he would have said, as he often did, "A saw is not a piece of furniture, just something that is useful in making a chair or table. In the same way, bookkeeping records are not the business, just something that may show what we have been up to."

Notwithstanding his habitual use of platitudes, he was nobody's fool and I remember him both with respect and affection. No doubt this episode would have ended as so many did, when I stopped by his office for a chat before leaving for the day. Frequently, I would find him gazing out the window at the trains entering and leaving London Bridge Station; they seemed to have a soothing effect on him. And he might have said, "There are days, admittedly rare, when bookkeepers actually contribute something useful to the world."

"You mean systems managers don't you?"

"Same thing!" ■

How to hold down the cost of health care claims processing



–and still be quick, fair, and accurate with settlements

For employer and insurer alike, the cost crisis is here—today. It takes more income, more profit to provide the benefits package and to process the group claims. Many cost inflators are squeezing companies now—and none is more visible than those affecting employee benefits. No longer can we be content with "explaining" these away. Many are concerned about cost containment—but MCAUTO is one of those doing something about it. Right now.

Experts agree that a well designed and operated computer-based information system is one of the methods offering the greatest potential for cost containment. MCAUTO has proven systems. Ones that will combat soaring benefit costs and ensure timely processing for medical, dental, and vision claims—without duplication or overpayment. We are operating these systems today—for a worldwide manufacturer with 100,000 employees. And for companies in the insurance industry. We can do the same for you.

To learn more about our Employee Benefit and Group Claims Processing Systems, write to Mr. W. R. Vickroy, MCAUTO, Dept. KK-500, Box 516, St. Louis, MO 63166. Or phone him at (314) 232-8021.

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info for buyers

• Are you confused about **self-insurance?** If so, a promotional brochure from Jeff Brougher, consultant for Lloyd's brokers and Thompson, Graham & Co., Ltd., may be what you need. The brochure answers the most commonly asked questions about self-insurance. For a free copy of this brochure write 1 in the box on the reader service coupon.

• The Risk Planning Group Inc. is offering a booklet of papers presented at the second international **captive insurance company conference of 1978.** The articles cover topics ranging from legal, tax and financial requirements relating to captives in various domiciles to a broad overview of the current captive scene and a discussion of where captive insurance companies may be heading. For a free copy of this booklet write 2 in the box on the reader service coupon.

• Are you thinking about forming a captive as the answer to your insurance needs? If you already have a captive, are you dissatisfied with the results? If so, AIG Risk Management is now offering a brochure entitled **Going the Captive Route: It Isn't "Business As Usual,"** which may solve your problems. The brochure outlines AIGRM's insurance management capabilities in the captive field. For a free copy of this brochure write 3 in the box on the reader service coupon.

• **Employe benefit self-funding** is becoming increasingly attractive to employers. In response to this trend Jefferson National Life Insurance Co. has compiled a self-funding administrators kit. The kit is designed to give a brief overview of self-funding, an explanation of the variety and flexibility of the company's stop loss products and a checklist for establishing a new self-funded plan. For a free copy of this kit write 4 in the box on the reader service coupon.

• Equifax Inc., an independent firm serving the risk management market, is offering a brochure describing its new **Risk Management Support Services** program. The brochure outlines the complete package of self-insurance services in the program—multiple line adjusting, safety/loss surveys, audits and valuation, health screening, claims investigation and a motor vehicle record system. For a free copy of this brochure write 5 in the box on the reader service coupon.

• **The PMI Mobile Facility Comes Right To Your Door** is the title of a brochure describing a health screening facility offered by Physical Measurements Inc. For a free copy of this brochure write 6 in the box on the reader service coupon.

• **When Employment Screening is Vital** is the title of a brochure outlining an employe screening program, tailored to meet the needs of the nuclear energy field, available through Equifax Services. For a free copy of this brochure write 7 in the box on the reader service coupon.

• Are you a **risk management** firm serving the self-insurance market? Gay & Taylor, insurance adjusters, has a new package of services for you. It includes automated reporting of loss statistics, claims management, claims adjusting and loss control services. A descriptive brochure and sample statistical reports are available free. For a free copy write 8 in the box on the reader service coupon.

• **1978 directory of facilities** of Gay & Taylor Inc., insurance adjusters and a subsidiary of Equifax Inc., is now available. The directory lists Gay & Taylor branch offices according to state. For a free copy of this booklet write 9 in the box on the reader service coupon.

• The Landmark Insurance Group Inc. has updated its kit detailing **The Captive Insurance Concept** for risk managers and insurance agents. Discussions include structuring of insurance to suit particular needs, financial advantages, the ability to offer unusual coverages not normally available and tax flexibility. Havens available for the formation of captives both on and

Continued on page 57

The end of the 4-wastebasket, 93-cup insurance meeting.

Shaping up your own insurance program eats up time. And even after all those meetings, today's tight insurance market may saddle you with expensive coverages and limited liabilities.

Insurance Management loosens your time bind. We study your needs, not just survey them. We pick the best alternatives for management of your risks, out of total familiarity with all coverages available.

When regular coverages prove inadequate, we're old hands at setting up and managing a "captive" insurance subsidiary for your company. You gain needed coverages, *plus* access to the worldwide insurance market.

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Info for buyers . . .

Continued from page 54

offshore are covered. Also the advantages of working with a Bermuda-based affiliate management corporation are outlined. A guideline for application to form Bermuda companies writing product liability coverage and sample management and underwriting agreements are provided. For a free kit write 10 in the box on the reader service coupon.

• **SICK** is a Self-Insurance Claims Kit prepared by Johns Eastern Co. The claims adjusting firm explains its philosophy and how it handles claims. For a free copy of this booklet write 11 in the box on the reader service coupon.

• A promotional brochure describes Hewitt, Coleman's services in workers compensation, general liability and self-insurance—**A Dialogue for Decision Makers.** For a free copy write 12 in the box on the reader service coupon.

• **Self-Insurance** and **Captive Insurers** are two 13-page brochures, part of INA's program of review of insurance topics for business executives and the insurance profession. The topics surveyed in "Self-Insurance" are why self-insure, choosing risks to retain and financing. In "Captive Insurers" the advantages of a captive, determining the need for a captive, association captives, domiciles and taxes are outlined briefly. For free copies write 13 in the box on the reader service coupon.

• Do you want to improve your cash flow and economize your operations in funding **group medical benefits**? IDS Life Insurance has a 10-page brochure describing the concept of self-funding and the five most common approaches to medical insurance plan funding. For a free copy write 14 in the box on the reader service coupon.

• **Unlock Your Capital with Self-Insurance** is a promotional folder from Hewitt, Coleman outlining their self-insurance program and advantages. For a free copy of this folder write 15 in the box on the reader service coupon.

• Gates, McDonald has put together a promotional kit describing their cost **control services to self-insurers for workers compensation.** Included are pamphlets to assist in compliance with OSHA, description of services for reducing accident costs, self-insurance for workers compensation plans and answers to questions on self-insurance. For a free copy write 16 in the box on the reader service coupon.

• **ERMCI: A Participative Management Approach to Your Hospital's Insurance Program** is a promotional brochure available from Ebasco Risk Management Consultants Inc. The firm's two key services—claims administration and risk control—are pinpointed for the risk control manager interested in self-insurance for his hospital. For a free brochure write 17 in the box on the reader service coupon.

• Employers Save Money by **Self-Insurance** is the title of a promotional brochure from Employe Service Inc. The company is a third-party employe benefit claim administrator. For a free copy write 18 in the box on the reader service coupon.

• **Is Self-Insurance Answer to Rising Costs?** is the title of an article reprinted from Health Care Week. The author, Ralph Carnesecchi, a senior consultant with Ebasco Risk Management Consultants Inc., discusses establishing a self-insurance program, prefunding, the excess market and the advantages of commercial insurers and self-insurance. For a free reprint write 19 in the box on the reader service coupon.

• American Insurers Administrators Inc. offers a promotional brochure describing its **claims administration program** for insured and self-insured companies. For a free copy write 20 in the box on the reader service coupon.

• A promotional brochure describes **All Risk Management Services Inc.'s** background and capabilities in assisting self-insurers. For a free copy write 21 in the box on the reader service coupon.

• A promotional brochure outlines the services of **Venture Management Ltd.** The company offers management services to Bermuda-domiciled insurance companies. For a free copy write 22 in the box on the reader service coupon.

• Two promotional brochures describe Self-Insurers Service Inc.'s **third-party administration services** for occupational and non-occupational benefit programs. For a free copy write 23 in the box on the reader service coupon.

• The revised edition of **Section 501(c)(9) Programs,** a Kwasha Lipton booklet, is now available. The booklet summarizes the provisions of this IRS code governing self-funded trusts. It details background, types of benefits, restriction on membership, program structure, advantages, disadvantages, financing, tax exemption and consequences and state insurance laws. For a free copy write 24 in the box on the reader service coupon.

• A new program providing international benefits for as few as three employes working overseas, **Third Country National Group Trust,** is described in a promotional booklet from American International Life Assurance Co. For a free copy write 25 in the box on the reader service coupon.

• Scarborough and Co., Chicago-based insurance counselors to banks, has updated **Insurance and Protection Handbook.** The 20-page handbook provides a description of services, rules for buying financial institution insurance and highlights of policies available through Scarborough. A loss prevention index has been added that lists many causes of loss, cites the insurance coverages designed to cover them and suggests operational safeguards to reduce risks. For a free copy of the handbook write 26 in the box on the reader service coupon.

• Johnson & Higgins has prepared a promotional brochure on its **nuclear loss control** technical service. The guide attempts to dispel some misconceptions about risk management of nuclear facilities, clarify some basic problems and tell about J&H's services in this unique environment. For a free copy write 27 in the box on the reader service coupon.

• **Building a Result-Oriented Control Program** is an article reprinted from Risk Management magazine that explains the conditions of possible trade-offs of risk control and risk financing as it relates to hospital professional liability coverage. For a free copy write 28 in the box on the reader service coupon.

Continued on following page

Tolley Knows

how to pay claims . . . in one day

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Info . . .

Continued from preceding page

• **Risk Management,** Some Professional Considerations is a 12-page brochure review of the topic by INA. Among the areas of concern considered are identifying the risks, risk measurement, risk handling techniques, selection of specific techniques, retention versus transfer and periodic evaluation. For a free copy of the brochure write 29 in the box on the reader service coupon.

• Are you a risk manager, insurance consultant, broker or company in need of an independent fire protection consulting service? **Creative Property Loss Prevention Engineering** is a promotional brochure that describes such a service for self-insurers offered by RM/i Consultants Inc. For a free copy write 30 in the box on the reader service coupon.

• RIMCO tells how to **Analyze Risks to Get Better Insurance at Less Cost** in the construction field, for both highway and heavy construction contractors. Two reprints of articles are offered free. How to request bids, how to get coverage in monopolistic states and cash flow arrangements are some of the topics covered. For a free copy write 31 in the box on the reader service coupon.

• When revenue unexpectedly stops for a business because of insured damage to its physical plant, business interruption insurance can pay out a fixed amount to compensate for each day lost. For a discussion of this form of insurance, INA has prepared a 12-page booklet—**Business Interruption:** Some Professional Considerations. For a free copy write 32 in the box on the reader service coupon.

• **Standard Dwelling Property Service,** a total inspection reporting system of underwriting property lines insurance is detailed in a promotional brochure from Equifax Services Inc. The 24-page brochure includes many sample reporting forms and stresses the value of inspection reports. For a free copy write 33 in the box on the reader service coupon.

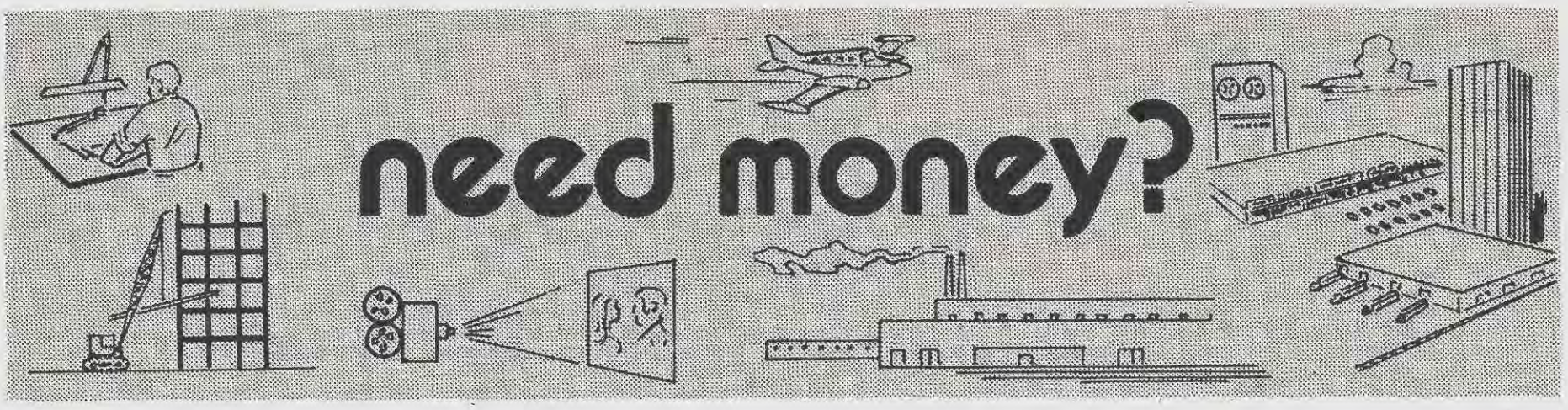
• If you're a member of the United States aerospace industry, you may be interested in a promotional booklet from the **Aircraft Builders Counsel.** Written in conjunction with J.H. Minet & Co. Ltd., the publication presents answers and questions about the ABC program of coverage. For a free copy write 34 in the box on the reader service coupon.

• **The Merritt Co.,** publisher of reference manuals, services and study and training aids for insurance and business managers is offering a four-page brochure describing all its products and services. For a free copy write 35 in the box on the reader service coupon.

• **When You're Not Sure if Your Construction Site Will Be in a Friendly Territory,** Johnson & Higgins says it can help. The pamphlet outlines the complexities facing U.S. contractors with overseas commitments and describes the company's "all risk" and political risk insurance. For a free copy write 36 in the box on the reader service coupon.

• A detailed brochure describing the **analytical services** of Clayton Environmental Consultants Inc., a technical service of Marsh & McLennan, is available free. Some of the analyses that the consultants

Continued on page 60



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Continued from page 58
offer are gas chromatography, atomic absorption and emission spectrophotometry, x-ray diffractometry, microscopic analysis and method development. Write 37 in the box on the reader service coupon.

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• **Detour Alcoholism Ahead** is a 16-page booklet from the Kemper Insurance Cos. designed for supervisors and others who require a basic understanding of alcoholism. The booklet will help your people identify problem drinkers and suggest sources of help. Up to 50 copies may be obtained without cost. For a free copy write 40 in the box on the reader service coupon.

• A monograph titled **Self-Insurance:** A Risk Management Alternative contains articles discussing how self-insurance is a successful tool to deal with workers compensation, FASB-5, banker's blanket bond, medical malpractice and product liability problems. Other topics covered in the monograph are controlling self-insurance costs, investment management and insurance subsidiaries. Cost is $10. Write The Society of Chartered Property & Casualty Underwriters, Kahler Hall, Providence Rd., Malvern, Pa. 19355.

• Are you a risk manager in need of evaluating the effectiveness of your **public agency's self-insured workers compensation program?** G. David Marceau and Associates has prepared a 23-page manual from a total risk management point of view. The review is presented in outline form and costs $11.95. Write David Marceau, G. David Marceau & Associates, 8294 Gould Ave., Los Angeles, Calif. 90046.

• Want to establish or evaluate your library insurance program? Whether you are employed by a small or large library, **Insurance Manual for Libraries** is a how-to-do-it reference that should help you put together the essential elements of an appropriate insurance program. Suggestions are given for appraising costs for all library items. A glossary of insurance terms is included. Copies are $5 each. Write Order Dept., American Library Assn. 50 E. Huron St., Chicago, Ill. 60611.

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Business Insurance is seeking items relating to international insurance for the Info for Buyers column in the special International Insurance issue. The Info for Buyers column provides BI's readers with easy access to explanatory brochures, studies, reports and other sources of information helpful to their jobs. The items must either be free or for a nominal cost (less than $10). Persons wishing to submit material should send a copy of the brochure, information on where it may be obtained and the cost to Mary Ellen McKee, *Business Insurance*, 740 N. Rush St., Chicago, Ill. 60611 no later than Jan. 25.

• The Machinery and Allied Products Institute has prepared a 33-page booklet **Company Programs to Reduce Product Liability: Some Matters to Be Considered.** The institute says this booklet is the product of 17 years of MAPI involvement in the growing problem of product liability. Single copies are available for $5 for institute members and $8 for nonmembers. Write Machinery and Allied Products Institute, 1200 Eighteenth St. NW, Washington D.C. 20036

• A new manual, combining available information along with analysis and explanations of **workers compensation,** is now available from RIMCO. The manual is written in layman's language and designed for use by insurance buyers, agents, underwriters and auditors. Cross-referenced with both numerical and alphabetical listings, the manual contains rules, classifications and interpretations for all states except monopolistic fund states. For a free brochure describing this $75 manual write William Beck, RIMCO Inc., 10300 North Central Expressway, Suite 180, Dallas, Tex. 75231.

• The defense of medical malpractice cases is the subject of the recently published **Medical-Legal Monograph** offered by the Defense Research Institute. A collection of five articles provides observations regarding the investigation and preparation of medical malpractice litigation, the medical standard of care, the statute of limitations and informed consent. An appendix outlining a strategy of discovery for the defense, an annotated bibliography and case references to nearly 90 briefs are included. Each copy of the monograph costs $7.50. Write William H. Kotlowski Jr., Information Director, Defense Research Institute, 1100 W. Wells St., Milwaukee, Wis. 53233.

• A monograph titled **Products Liability—An Area of Growing Concern** contains articles discussing the problem and explaining no-fault, consumer product safety, malpractice and tort reform. Cost is $6.95. Write The Society of Chartered Property & Casualty Underwriters, P.O. Box 566, Media, Pa. 19063.

• **Workers Compensation and Employers' Liability Experience Rating,** by John R. Stafford, covers the National Council on Workers Compensation experience rating plans. Eligibility, jurisdictions and single-state, interstate and exception-state calculations are included. The major 1977 revision of the plan is also explained. Prepaid cost is $6.95, otherwise $7.20. Write J&M Publications, Dept. B, P.O. Box 338, Palatine, Ill. 60067.

New ISO chairman

J. Roy Nicholas, president and chief executive officer of Royal Globe Insurance Cos., has been elected chairman of the board of directors of the Insurance Services Office. He succeeds Waverly G. Smith, president and CEO of the St. Paul Companies Inc.

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These programs range from screening programs for hypertension to health information programs (like one in use by Armco).

In addition, an amazing number of companies have begun on-the-job fitness programs. These programs range from exercises employees are encouraged to perform at their desk, to workouts at nearby YMCAs, to medically supervised fitness activities at extensive company facilities (like those provided for their employees by Xerox and Kimberly-Clark).

These bold and imaginative companies realize that preventive medical programs have the potential of returning enormous dividends in greater health and happiness for their employees. And greater productivity from them.

It also stands to reason that if your company can institute a program that is actively designed to keep your employees healthy and well, your company's health care costs can possibly be lowered.

As you know, Blue Cross and Blue Shield Plans are fighting a nationwide battle to keep costs from running away.

Programs such as second surgical opinion, medical necessity programs, home care, health maintenance organizations, same day surgery, pre-admission testing and the like are in use in many Plans with positive money-saving results. As successes are achieved, the results are shared so that knowledge gained by solving local problems can be applied on a wider basis.

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around the states

Ill. lets workers seek punitive damages

SPRINGFIELD—The Illinois supreme court has ruled that workers can seek punitive damages if they are fired for filing a workers compensation claim against their employers.

Previously, workers who were victims of retaliatory firings could only seek compensatory damages for the amount of wages lost and not punitive damages.

The decision concerned Marilyn Jo Kelsay who injured her thumb while working for Motorola Inc. in Pontiac and claimed that the company fired her because she had filed a workers compensation claim.

The trial court ruled in Ms. Kelsay's favor and the jury awarded her $749 in compensatory damages and $25,000 in punitive damages.

On an appeal by Motorola, the appeals court threw out the award. On Ms. Kelsay's appeal, the state supreme court said punitive damages were incorrectly awarded to Ms. Kelsay, but maintained that a worker could seek punitive damages in cases brought for retaliatory firings.

Meanwhile, Employers of Wausau, Aetna Life & Casualty, USF&G and Kemper, major insurers of workers compensation in Illinois, refused to comment on the decision, but said that they would watch it very closely to see its effect on an already troublesome line of business.

Malpractice rates cut

INDIANAPOLIS—The Indiana Residual Malpractice Insurance Authority, a state operated insurance company, slashed medical malpractice professional liability insurance premiums for all health care providers by 25% on Jan. 1. Malpractice insurance premiums for hospitals were lowered by 12.5%.

The premium reduction was possible because fewer malpractice claims had been filed than the state expected, according to Indiana insurance commissioner H.P. Hudson.

Liability limit struck

GLENDALE—A California superior court judge has struck down as unconstitutional the state's $250,000 limit for pain and suffering damages in medical malpractice awards.

The limit was included in the state's Keene Act passed in 1975 to relieve physicians from skyrocketing professional liability insurance rates.

In holding the limit unconstitutional, Glendale superior court judge Robert P. Schifferman said the ceiling was an unconstitutional denial of equal protection under the law. Limiting the recovery available to a person injured on the operating table but not, for instance on the highway, was "arbitrary," the superior court judge explained.

Sex-based benefits

NASHVILLE—A Tennessee circuit court judge has ruled as unconstitutional a provision of the state's workers compensation law that required separate standards for awarding benefits to widows and widowers.

Under the state law, widows were entitled to receive 50% of their deceased husband's income, but widowers only could receive 20% of their deceased wife's income and had to prove dependency.

Excess/surplus lines

SOUTHFIELD—Michigan insurance commissioner Thomas C. Jones said legislation will be introduced this year to make it easier for commercial insurance buyers to purchase excess/surplus lines of coverage.

The legislation will call for faster state approval of insurance companies located outside the U.S. Currently, Lloyd's of London is the only insurer writing excess/surplus lines coverages in Michigan.

The bill Mr. Jones expects to have introduced will also recognize and regulate the brokerage function in surplus lines; establish conditions under which purchasers may seek coverage in the surplus lines market; include safeguards for insureds, and provide for the establishment and supervision of associations of surplus lines insurers and the establishment of guaranty funds to pay claims if an insurer becomes insolvent.

"Commercial purchasers of surplus lines are sophisticated enough to need somewhat less regulatory protection and a great deal more latitude in finding a market for special or large risks," Mr. Jones said. "Regulation should be more flexible where purchasers are more knowledgeable."

Product liability survey

ATLANTA—Insurers of product liability in Georgia must file extensive annual reports on their business in Georgia and elsewhere with the insurance commissioner by March 1 of each year.

A prescribed form for reporting under the new mandate requires insurers to disclose their business practices regarding product liability insurance in Georgia and in other states.

Insurers must disclose where they write product liability insurance, their marketing plans for it, their restrictions on the kind of risks or amount of insurance they will write, exclusions in their policies and their loss and profit history on the business.

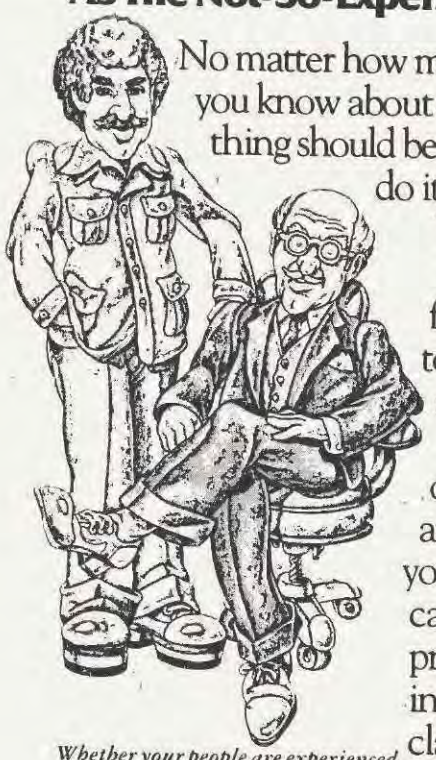
Skiers' liability

TRENTON—The New Jersey legislature gave final approval to a measure that is expected to hold down rising liability insurance premiums for the state's ski industry by giving lodge operators a defense against liability if a skier's own negligence contributed to an accident.

Similar legislation has been enacted in New York, Massachusetts, Pennslyvania and New Hampshire and in those states liability insurance coverage costs half of what it is in New Jersey, claimed state Sen. Wayne Dymont Jr. The bill now goes to Gov. Brendan Byrne, who has not taken a position on the legislation. ■

How To Keep S From Being So

A Guide For The Experienced As Well As The Not-So-Experienced.



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If you're new to self-insurance, choose a company that isn't. (If you're an old hand, do the same.)

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We can help you set up a program. Or help support your existing one.

Lloyd's clears Willis Faber in Fiat fire claim case

By JOHN H. MILLER

LONDON—A Lloyd's board of inquiry has cleared Willis Faber Dumas broking group of charges that it brought undue pressure on reinsurers to pay more than $500,000 on a controversial claim for fire damage to a shipment of Fiat automobiles in 1974.

A massive report issued by the board of inquiry goes beyond this incident in which charges of claim fraud were levied to establishing guidelines for brokers handling claims in which fraud is suspected.

The board maintained that as long as insurance brokers notify their underwriters that a claim is suspicious, they have completed their duty to the market and should not hinder any further decisions to pay it.

That opinion is essentially an endorsement of Willis Faber Dumas' action as the new broker on the account to see the claim paid and a rebuff of efforts of the Pearson Webb Springbett group as the original broker to see that the claim was resisted.

The clash between the two broking groups took on a David versus Goliath appearance. Pearson Webb Springbett, with $5 million in brokerage business, charged the giant Willis Faber Dumas group, with an annual premium volume of more than $1.5 billion a year, had brought undue pressure to settle the claim.

There were suspicions that salvage losses on Fiat auto cargo damaged by fire while en route to the U.S. in 1974 had been inflated by some senior executives of the big Italian Fiat auto group (*BI*, April 17, 1978).

Details of the clash first excited the London insurance market last March when British M.P. Jonathan Aitken charged in Parliament that Lloyd's had paid out large sums even though fraud had been committed in Italy.

The affair became known as the "Savonita case," named after the auto-carrier owned by a Norwegian shipping group. The Savonita caught fire off Savona, northern Italy, in November 1974.

It returned to port where the 301 Fiat autos destined for the U.S. that had been damaged in the blaze were unloaded onto the dock and written off as being almost valueless.

Claims for the cargo loss were initiated by an Italian insurance company named SIAT, Societa Italiana Assicurazioni Transporti, in which Fiat held a large commercial stake. It had reinsured the cargo in the London market, and wanted reimbursement since it had been called on to meet losses of close to $1 million.

But inquiries by London insurers, through a leading loss adjusting firm Graham Miller & Co., suggested that some of the autos had been sold to a Naples dealer, Signor Dotoli, for 15% of their value and that he had then resold them for 80% or more of their value, possibly with the aid of some unnamed Fiat executives.

Issues of payment began to worry the insurance market and were taken up by Pearson Webb Springbett, the reinsurance brokers for SIAT, which had placed the cargo risks on this and other Fiat auto shipments to the U.S. for some time.

A similar claim for damaged cargo on another vessel, the Toronita, which had caught fire in U.S. waters, was also under scrutiny at the time.

The Lloyd's report reviews the classic four-year trail of events recalling that the reinsurance for SIAT that covered the Savonita affair was placed in London on Jan. 1, 1974. When SIAT claimed $711,643 from London underwriters after meeting its own claims to the Fiat group, the leading Lloyd's underwriter, Roy Hill, called for survey reports and found they did not satisfy him. But the point was made on behalf of SIAT that under the policy in force the reinsuring underwriters were contractually obliged to follow its settlement.

Preliminary inquiries on behalf of Lloyd's Claims Office suggested that the amount of loss had been grossly inflated, and a complete inquiry in Italy was started.

By then, Malcolm Pearson, in what Lloyd's calls a "crusading spirit," had talked about parts of the SIAT account to executive directors of the much more powerful Willis Faber Dumas group, who already held brokerage rights for other SIAT business, such as hull

Continued on following page

Another fire

In addition to the well publicized Savonita case, the SIAT group made another large claim for fire damage to a shipment of Fiat cars aboard the cargo ship Toronita in 1975.

The claim was settled by Willis Faber Dumas for the full amount of $2 million, about 70% of which was placed in the London market. A P&I Club (protection and indemnity) is thought to also have an interest in the Toronita.

Despite the two fires on the Savonita and Toronita, underwriters made an overall profit on the SIAT account for the reinsurance on Fiat automobiles shipped to the U.S. from Italy, said Willis Faber Dumas broking group.

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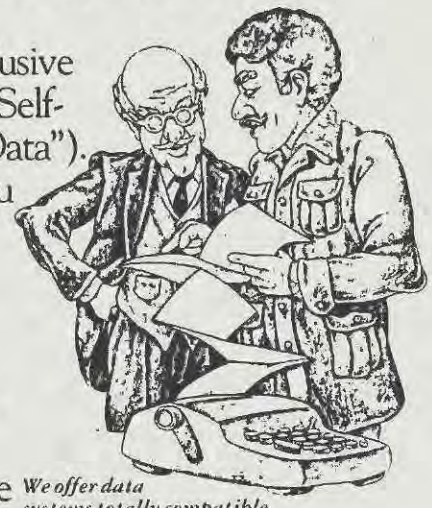

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Fiat fire claim . . .

Continued from preceding page
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They considered him a potentially serious competitor to their own position, especially as he knew the head of the Fiat corporation, Signor Agnelli. Willis Faber thought of buying Pearson Webb and bringing it within their own group ownership.

But Mr. Pearson's comments about SIAT caused concern and were passed on to Willis Faber's deputy chairman, J.O. Prentice, who was also on SIAT's executive board.

Both Mr. Pearson, of the broking group, and Mr. Hill, the lead underwriter, later saw then Lloyd's chairman Sir Havekock Hudson to tell him of the position.

But in April 1976, SIAT replaced Pearson Webb Springbett with Willis Faber as brokers for the Savonita account and instructed them to proceed to settle the claim.

With this in mind, the Willis Faber group arranged a meeting with leading marine underwriters, even though Mr. Pearson was still encouraging Mr. Hill to resist any settlement.

"It was a very stormy meeting at which feelings ran high on both sides, and out of it came the feeling that Willis Faber Dumas were prepared to use the weight of their account to get the claim settled," the Lloyd's report says. "There was evidence, which was not denied, of robustness by Willis Faber Dumas in the presentation of their case to some of the reinsuring underwriters."

Further developments took place when attorneys retained by Mr. Pearson gave their opinion there had been fraud. Lawyers for the underwriters decided the provision in the reinsurance contract to "follow all settlements" of the ceding company, SIAT, could not be effectively challenged. Furthermore, the lawyers said those facts that could be proved in court were not enough to justify resisting the claim under the circumstances.

So in the end the underwriters accepted their lawyers' advice and paid out $543,000 in February 1978, representing $183,000 from Lloyd's and $360,000 from U.K. company underwriters.

Then the storm broke when Mr. Aitken raised the matter in Parliament and declared there were some doubts about other Italian insurance losses which had been paid in recent years.

Lloyd's felt it should establish whether any undue pressure had been put on the market to settle the Savonita claim.

The board of inquiry was headed by Clifford A.L. Clark, chairman of the London Court of Arbitration, and included two Lloyd's underwriters, Frank Barber and Charles Skey, and two Lloyd's brokers, Ivor Binney and Peter Miller. They heard more than 50 witnesses.

Thirty underwriters were among the witnesses. The hearings lasted over 100 hours and 2,300 items of documentary evidence were considered, including a statement from A. Tarazi, U.S. surveyor for SIAT. Some of the witnesses were entitled to have lawyers present.

Written evidence was received from Italy from Signor Umberto Agnelli, vice chairman of the Fiat auto group, and from insurance men there.

The report, which was hedged with legal safeguards before release, was published in full in Lloyd's List. Its findings include the following conclusions:

• The board of inquiry is satisfied that Willis Faber Dumas did not seek to use the weight of its account in order to persuade reinsuring underwriters to settle the claim, although at one meeting the behavior of their personnel was robust beyond the normally acceptable standards of broking conduct.

Reinsurers settled the claim because they were advised by leading attorneys that the chance of challenging SIAT's contention that they were obliged to "follow its settlement" of the claim was only 50-50. Even if they had succeeded on this legal point, it was believed they would be unlikely to discharge the burden of proof which rested on them if they challenged the claim as tainted by fraud.

• The board believes there is a continuing duty of disclosure on a broker in the presentation and negotiation of a claim. In the event a broker becomes aware of circumstances which give rise to suspicions of fraud, that duty requires him to report his suspicions both to his client and to the underwriters. Thereafter he should either pursue the claim against the underwriters, or inform his client that he is not prepared to continue to act and withdraw.

Brokers Pearson Webb Springbett quite correctly informed reinsuring underwriters of their suspicions, but not their client. Instead of pursuing the matter, they actively mounted investigations for the purpose of persuading the underwriters that the claim was fraudulent.

• Considering all the evidence available to reinsuring underwriters regarding the allegation of fraud coupled with the legal advice underwriters received, the board accepts that despite undoubtedly unsatisfactory aspects to the claim, the conclusion the underwriters reached was correct.

• The duty of any leading underwriter, when informed of suspicions of fraud in connection with a claim, is to ensure that all underwriters following him are aware of the circumstances. The board would not expect a leading underwriter to settle a claim in such circumstances without an investigation.

Leading underwriter Roy Hill investigated the facts as far as he was able, and sought legal advice on the construction of the reinsurance contract. Based on this advice, instructions were given to reinsuring underwriters' lawyers to settle.

On the attitude taken by Pearson Webb Springbett, the board comments: "Malcolm Pearson is young, able and ambitious. He has developed a successful insurance brokerage business in a very short period of time. His own flair is commercial rather than insurance, but he has ensured that his directors and staff are well experienced."

But the board was critical of his "crusade and campaign" about suspected fraud after reporting his suspicions to the underwriters.

Mr. Pearson later told *Business Insurance*: "I do not feel I should be criticized for what I did. It is not correct that I failed to tell my client of my suspicions, as I reported the matter to various persons. Furthermore, I consulted one of Britain's leading lawyers in the course of my inquiries, and hope to be able to publish his views on the whole affair in the near future. I feel my side of the story has not yet been fully told, and hope there will be equal publicity when I am in a position to release it."

John Prentice, deputy chairman of Willis Faber Dumas, said, "We accept the report, and that goes for the board of inquiry's opinion that we were robust on one occasion. I don't really look upon that as criticism, for we're in a competitive market and surely most clients would like robust presentation for their case." ■

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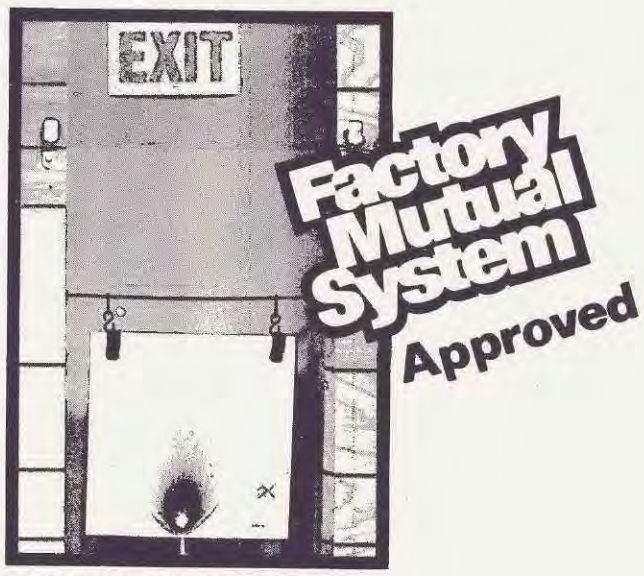

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Small firms fall short on insurance purchases

By JOHN MAES

CHICAGO—More than half of the small businesses in the U.S. carry no group insurance plans for their employes and 10% have no property/liability coverage despite average annual sales of $500,000, a study shows.

The study of 10,000 small businesses across the country was sponsored by U.S. News & World Report magazine and the Life Insurance Marketing and Research Assn. to illustrate the insurance needs of the small business community and to point out its potential as an insurance market.

Of those surveyed 45% of the firms were run by a sole proprietor, 44% were corporations and 11% were partnerships. All the firms had 50 or fewer employes with an average of eight workers per firm. The principal owners averaged salaries of $40,000 yearly.

Fifty-six percent of the businesses carried no group insurance. Among companies doing less than $100,000 annually in business, 81% did not offer group coverage and among small businesses with annual sales volumes of more than $500,000, 19% had no group plans.

Also, 17% of the companies without property/liability insurance had less than $100,000 in yearly sales, while only 6% of those firms without it had $500,000 in annual sales.

Of the firms questioned, 97% said they did not give their employes dental coverage, while large majorities reported being without group surgical, major medical or group hospital plans.

All but 4% said they had no group permanent life insurance and another 78% indicated they provided no term life coverage to their workers.

In addition, nearly nine out of 10 employers participating said they were without temporary and long term disability or accidental death and survivor/income policies.

Of the companies reporting they did offer group insurance plans, 60% and 70% bore the entire premium burden with the exception of group survivor plans where 56% of the employers paid all the premiums. The other exception was with health maintenance organizations, for which just 33% of the employers paid the whole cost.

And small companies paid healthy premiums for employe coverage, the study showed. The average total premium for all group insurance plans was $5,900 per year, while business life insurance cost an average $2,100 yearly and disability income insurance averaged $1,400 in annual premiums.

Those employers buying property/liability insurance paid an average of $4,500 in annual premiums.

Of the 90% of the firms buying property/liability coverage, 70% had workers compensation, 67% had comprehensive general liability, 53% had commercial auto/truck, 50% had fire and allied lines, 46% had burglary/theft, 33% had a multi-peril package, 29% had product liability, 22% had business interruption, 20% had glass coverage and 17% had professional liability.

Only 12% of the firms buy surety bond and 10% or fewer of the firms buy boiler and machinery coverage, an employe fidelity bond, inland marine insurance, officers and directors liability insurance.

The survey also found that 70% or 2.38 million of the nation's 3.4 million small businesses don't buy business-related life insurance, 75% are without disability income insurance, 56% did not have a formal plan for transfer of ownership and 67% did not have a tax deductible retirement plan.

Small business proprietors gave insurance companies and agents, for the most part, only average marks in the way they attend to insurance matters, the study also found.

For instance, while 13% of the responding companies feel they receive good policies at reasonable rates, 53% gave only an average rating to insurers on that issue and 25% rated insurance at its current price as a poor value.

Twenty-nine percent said insur-

Continued on following page

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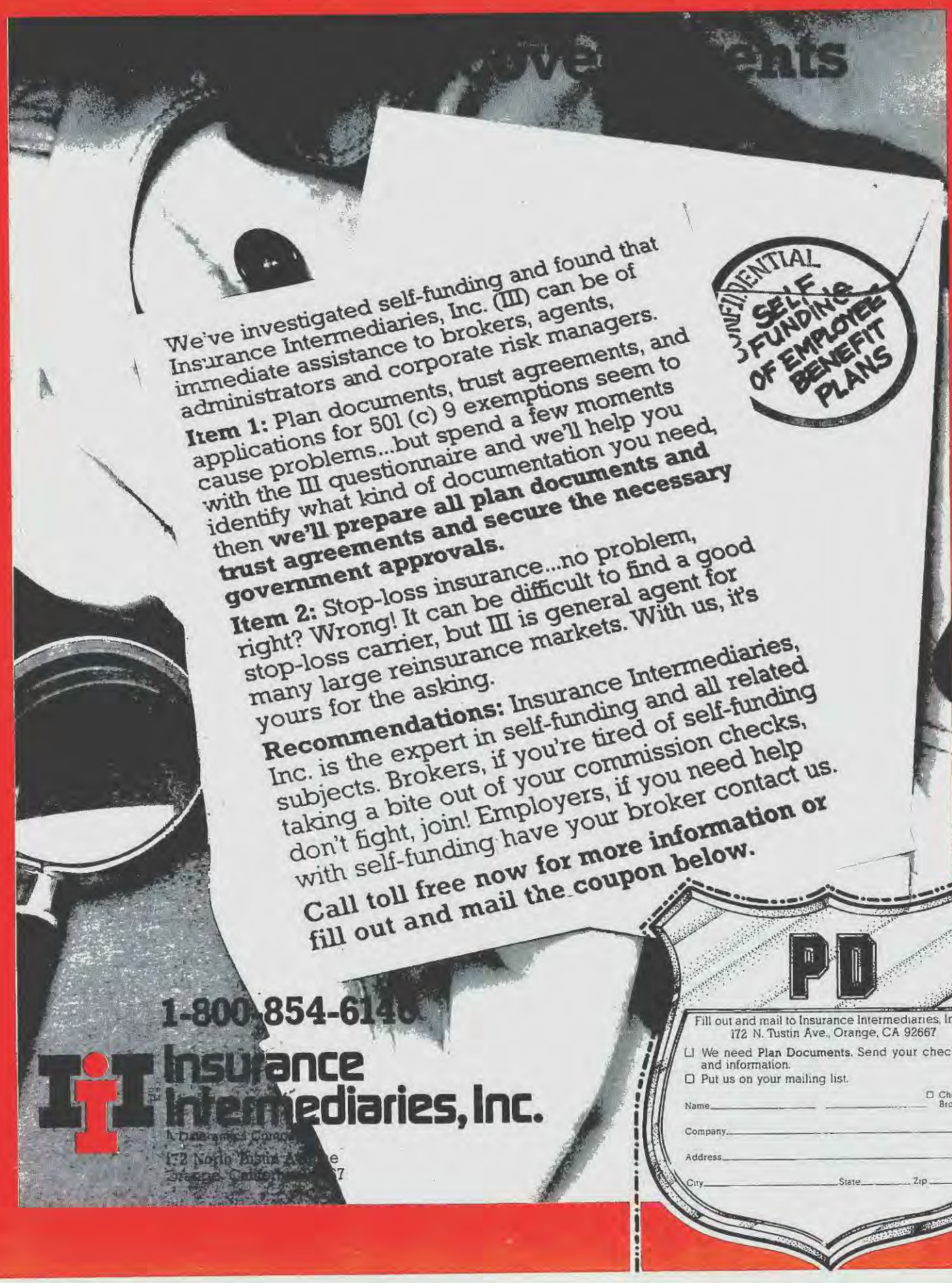

Small firms . . .

Continued from preceding page

ers do a good job of being open and honest with their policyholders but 45% indicated the job was only average in quality and 17% said it was poor.

In offering policies that are understandable and free of "fine print," 44% said insurance companies do a poor job, 36% said it's average and 11% said it's a good job.

Forty percent of the companies said insurers do a poor job of helping them find ways to reduce the cost of their insurance, 37% said they do an average job and only 13% said they do a good job. The performance of insurers in keeping red tape and paperwork to a minimum was rated good by only 21%, average by 42% and poor by 27%, according to the study.

But 42% of the surveyed firms said insurers do a good job of answering correspondence courteously, 38% said they do an average job and 8% said insurers handle the matter poorly.

Insurers are rated as generally good in handling claims. Thirty-four percent of the firms said insurers pay claims fully and promptly, 40% said they do an average job handling claims and 20% said they do a poor job.

Rating insurance agents, 46% of the firms said agents have only an average knowledge of insurance, 38% said they know it well and 8% complained agents' insurance knowledge is poor.

In addition, 47% of the firms gave agents an average rating at making it a point to know the business and insurance needs of the client, 28% gave them a good rating and 17% a poor rating.

Thirty-five percent of the proprietors said agents do a good job of avoiding complex and technical language when talking about insurance, 45% said they do an average job and 12% said they do a poor job. In openly and honestly describing the policies, options and costs, 36% of those surveyed said agents do a good job, 42% called it average and 13% found them to perform poorly.

The performance of agents avoiding high-pressure sales talk is rated good by 37%, average by 38% and poor by 17%. Twenty-nine percent of those questioned said agents do a good job of keeping in touch with policyholders between renewal dates, 31% said they do an average job and a like 31% said they do a poor job.

Also asked whether insurance agents are helpful in dealings with an insurance company, 39% indicated agents do a good job, 38% said they do an average job and 15% said they do a poor job. ■

Wrap-up insurance plan works for Ariz. utility

By JOHN MAES

PHOENIX—A wrap-up insurance program and a low loss ratio have saved the Arizona Public Service Co. $2.9 million in the form of returned premiums on a massive power plant and transmission line construction project.

Norm Cocanour, risk manager for APS, said the wrap-up project was the first of its kind in the state. The concept is being used currently on one other project, a hotel, and will be used next year on another APS job involving a nuclear power plant in Farmington, N.M., he added.

The saving will figure in rate calculations which could lead to lower bills for APS's' 350,000 electric power customers, Mr. Cocanour said.

The wrap-up package covered workers compensation and general liability exposures in the construction of the APS Cholla and West Phoenix power plants as well as a 500,000-volt transmission line, the Cholla-Saguaro, running 206 miles from Tucson to the city of Holbrook, Ariz.

The bulk of the premium return, approximately $2.25 million, stemmed from a policy that covered construction of three units of the Cholla plant near Joseph City and the Cholla-Saguaro transmission line. Another $650,000 of the return came from insurance dividends on policies covering all three projects, according to APS.

Mr. Cocanour said the $2.25 million was returned on $3.8 million in premiums paid to Argonaut Insurance Co. of Menlo Park, Calif., for a year-long policy covering all the contractors associated with the job for workers compensation and general liability. Between 15 and 30 contractors and 2,000 workers were involved at one time or another.

There were a few minor liability claims and a somewhat larger number of compensation claims, Mr. Cocanour said. Some of the compensation claims were termed "serious" by Mr. Cocanour, but there were no fatalities.

"Our loss ratio was very good—20% or about one-fifth of the total premium," he said.

The policy was set up so that if APS loss ratios were less than those which insurance companies estimate for comparable projects, APS would be eligible for a return on its premiums, said Mr. Cocanour. "The crews bettered the industry average by more than 30%."

"Safety awareness" and accident prevention were emphasized to the workers by the contractors, the insurance company and APS. In addition, "there was constant monitoring of safe work practices," the risk manager said. The wrap-up policy eliminated multiple insurance contracts, duplicate coverage and cross-claims and counterclaims that can occur on large-scale construction projects, "especially if you have a lot of contractors," Mr. Cocanour explained.

The wrap-up insurance program was used by APS because it saw the concept had been used successfully in other areas by utility companies.

"It's been kicked around in the utility industry for a number of years," according to Mr. Cocanour. "If you're involved in the industry, you hear about it.

"Many utilities that have major construction projects are involved with wrap-ups," he said. ■

Democrats ask for national plan

MEMPHIS—The Democratic Party officially endorsed at its mid-term convention here the enactment of a national health insurance program during the next congressional session.

Adoption of the NHI resolution is viewed as a mild blow to the Carter Administration which favors a phase-in period in which NHI would be gradually ushered in. ■

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benefit tax slants

Consider other options for pension programs

By JOSEPH S. ROBINSON
Attorney-at-Law

MANY CLOSELY HELD corporations find employe qualified retirement plans burdensome and time consuming. What's more, sponsors of such plans are increasingly fearful of their personal responsibility as fiduciaries. Consequently, and as a result of the new tax law, many companies are contemplating a switch to the so-called simplified pension plan.

Beginning in 1979, the rules permit employers to provide retirement benefits for employes by making contributions to the employe's individual retirement plan (IRA) instead of maintaining their own qualified plan.

Under such an arrangement, each employe sets up and maintains his or her own individual account which will be governed by existing IRA rules regarding distributions, withdrawals and the like.

Such contributions are deductible by the employe up to the lesser of $7,500 or 15% of earned income. However, these new rules apply only when the company pay-ins are made pursuant to a written formula.

This formula must provide nondiscriminatory contributions for each employe over age 25 who has worked for the company during any part of three out of the five preceding calendar years. Contributions under the formula must not discriminate in favor of any employe who is an officer, a more than 10% shareholder, self-employed or highly compensated.

Another approach which requires no IRS approval and, in addition, permits the company to select its participants, works as follows:

Instead of contributing money into a formal Treasury-approved pension, the company gives an annual bonus to selected employes which equals the premium of a participating insurance policy on the life of each selected employe. The employe owns the policy and names the beneficiary. Consequently, the premium dollars are taxable to the latter. But that's not so bad inasmuch as the tax free policy dividends (which belong to the employe) will partially offset the extra income tax which the employe must pay. In the meantime, the company takes a deduction for the premium just as it would when making contributions to a qualified pension (I.R.C. Sec. 162 (a)).

Split-dollar plan

A recognized executive extra which companies offer to key employes is the so-called split-dollar plan, a vehicle by which the lion's share of life insurance premiums is borne by the corporation through, in effect, interest free loans to the executive.

Some tax experts questioned the success of obtaining estate tax clearance on a typical split-dollar setup for a controlling stockholder—one who owns more than a 50% interest. These "tax mavins" base their concern on current Treasury regulation section 20,2042-1(c)(6), which states that a corporation's incidents of ownership in an insurance policy will be attributed to a sole or controlling shareholder to the extent that proceeds are payable to someone other than the corporation.

And in a recent case, the tax court concluded that a controlling shareholder and a sole shareholder both have the power to control a corporation and therefore possess the corporation's incidents of ownership in split-dollar insurance policies.

Here are the facts:

When Milton Levy died, he owned 80% of the outstanding voting stock and 100% of the outstanding nonvoting stock of Levy Brothers Inc. Levy Brothers owned two split-dollar policies on Milton Levy's life, both with face

Continued on following page

Some different approaches to surplus lines.

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CU RISK MANAGEMENT

Benefit tax slants . . .

Continued from preceding page
amounts of $128,500. Each policy paid $103,350 to Milton Levy's widow, and approximately $850 to Levy Brothers. (The value of the policies was reduced by substantial policy loans.) At all times, Levy Brothers had the right to assign, modify and borrow against the policy, as well as to change the beneficiary of the death benefits. Milton Levy had no incidents of ownership in the policies, except for his company stock interest.

The tax court ruled that the $200,000 which Mrs. Levy received in insurance proceeds was included in her deceased husband's estate for estate tax purposes. *(Levy 70 TC No. 80)*

Life insurance transfers

Many executives who are covered by group life and/or split-dollar insurance plans often assign their interest in the policy to their beneficiary in an effort to shelter the proceeds from their taxable estate. In 1976, the Treasury clarified the gift and estate tax impact:

(a) An employe's transfer of his interest in a group policy has no ascertainable value at the time the policy is transferred because the employer could have simply failed to make future payments. Therefore the transfer is not a taxable gift.

(b) The employer's payments of policy premiums are added compensation to the employe (whether taxable or not to him), and later viewed as a taxable gift by the employe, subject to the $3,000 exclusion. *(Rev. Rul. 76-490)*

Subsequently, the Tax Reform Act of 1976 permitted gifts to anyone in the amount of $3,000 per year which would be excluded from gift or estate tax.

The Revenue Act of 1978 explains the rule with regard to life insurance further. If the insured-transferor of a life insurance policy with a cash value of $3,000 or less or a term policy with a paid-up premium of $3,000 or less dies within three years of the transfer of the policy the entire policy proceeds will be included in the insured's gross estate.

However, if incidents of ownership were relinquished more than three years before the date of death, no part of the proceeds is included in the gross estate. But according to committee reports, premiums paid by the decedent for a donee, after the assignment and within three years of death, are fully includable if they exceed $3,000 in a calendar year. *(IRC Sec. 2035 (b) amended by Revenue Act Sec. 702(f)*. See also *(Rev. Rule 71-497)*. ■

Consultant says

Public employers try to cut health plan costs

SAN DIEGO—Public entities and their employes are looking at changes in health benefit plans and alternatives to traditional insurance coverage to help them cope with rising health care costs.

Like private corporations, the public sector has found itself faced with steady cost increases in providing health care benefits for its employes. The reasons are the same too: inflation, advances in medical technology and hikes in contract benefits brought on by collective bargaining.

That was the message of Bernard Handel, president of the Handel Group Inc. of New York, during a conference last month in San Diego of the International Foundation of Employe Benefit Plans.

Mr. Handel said that efforts to cut costs include changing means of funding, revising benefit structures, changing methods of paying benefits and adopting alternative approaches to providing benefits.

In some cases, local governments and municipal workers have begun a welfare fund approach, in which the governmental agency contributes to a fund that is used to help pay health care costs for its employes.

Under this method, workers become more closely involved in selecting a plan and its insurance carrier and the government is committed to provide a certain budgetary amount during a given period, stabilizing its costs, according to Mr. Handel.

Plans should also be expanded to provide for "second opinions" from physicians on voluntary surgery and extended diagnostic testing, both of which may help ward off future cost increases by cutting down on plan utilization by employes, he added.

Stricter coordination of benefits with other insurance policies, deductibles and co-insurance, along with pre-approval for dental treatment would also deter excessive use of benefit plans, Mr. Handel said.

Another money-saving method for benefit plans would be to establish competition for services by calling for review of doctors' charges and trying to negotiate the rates, Mr. Handel suggested. Such procedures may involve substantial costs but would eventually save on future reimbursements to hospitals which could be based on previously negotiated rates.

Governments and public employes should also be more aggressive in looking at educational programs that would instruct workers on ways of preventing diseases and health problems, suggested Mr. Handel.

Using the analogy that it is cheaper to attack air pollution than treat emphysema, Mr. Handel said money would be saved in the long run if workers' programs would deal with such areas as smoking, weight control, physical fitness, accident prevention, alcoholism, drug abuse, hypertension control, first aid and cardio-pulmonary resuscitation.

"Joint government-public employe programs could be innovated which may achieve the greatest long-term degree of medical cost containment," he said.

"Health plan decision makers should aggressively seek means of modifying annual cost escalation other than merely attempting to raise sufficient taxes to defray such costs," he urged.

Mr. Handel cautioned however that before restructuring plans, plan administrators should study changes carefully and should seek professional advice. ■

La. storm losses

Insured losses of $25.6 million are estimated from a storm that swept through parts of Louisiana, Arkansas and Mississippi last month. Nearly all the damage occurred in Louisiana. The storm has been assigned castastrophe number 70 by the Insurance Services Office.

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legal briefs

Discrimination awards are insurable: Court

The abstracts published in this column were prepared by Cases Unlimited Inc., Evanston, Ill.

DOES AN INSURANCE policy that insures an employer against losses resulting from racially discriminatory practices violate public policy? In a pioneer case, a federal district court in Georgia ruled that it did not.

The Union Camp Corp. (Union) carried an umbrella excess coverage policy with the Continental Casualty Corp. (CNA). The policy covered "discrimination except that committed by, at the direction of, or with the consent of the insured."

In 1971 a class suit was brought against Union claiming discrimination against its black employes. CNA denied coverage and refused to defend Union. Subsequently, Union settled the class suit which included $800,000 in back pay. Union then brought this suit against CNA seeking recovery of the back pay and attorneys' fees incurred in defending the class suit.

CNA's basic argument was that an insurance contract is unenforceable if it is injurious to the public or contravenes some established interest of society. According to CNA, permitting the writing of such insurance would undermine enforcement of the strong public policy of equal treatment of all persons.

The court concluded that the proposition that insurance taken out by an employer to protect against liability for civil rights law violations would encourage violation of the laws was "based on an assumption that is speculative and erroneous." The court said that it "is only in clear cases that contracts will be held void as against public policy. . .This is not one." *Union Camp Corp. v. Continental Cas. Co.*, United States District Court for the Southern District of Georgia, June 27, 1978 (BI/02/F.-$4).

Fidelity bond

A bank sued two bonding companies to recover on fidelity bonds. The Supreme Court of Wisconsin held that the bonding companies would not be subrogated against the bank's officers and directors for ordinary negligence in supervising the affairs of the bank and in supervision and control of a defaulting employe.

The First National Bank of Columbus (First) carried a fidelity bond with a $300,000 limit issued by Capital Indemnity Co. insuring it against losses resulting from the fraudulent and dishonest acts of employes. The Fidelity and Deposit Co. of Maryland issued First a similar policy for an excess of that amount not to exceed $1 million.

First sustained losses of over $900,000 as the result of dishonest and fraudulent acts of its executive vice-president. First filed claims with the insurers which were denied. First sued both insurance companies and they, in turn, brought a countersuit against the officers and directors of First. The trial court dismissed the countersuit.

On appeal, the insurance companies argued that since the bank had a right of action against its officers and directors for loss caused by the dishonest and fraudulent acts of an employe resulting from the officers' and directors' negligent supervision and control, upon payment of this loss on the bond, the insurers were entitled to be subrogated to that claim. However, the court said that the insured would not be so subrogated unless the equities in favor of the insurer were greater than those of the person against whom subrogation was invoked. "Lack of ordinary care by the directors and officers of the insured," the court said, "does not give the fidelity insurer, who is

Continued on following page

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Legal briefs . . .

Continued from preceding page
paid to assume this risk, an equitable position superior to that of the officers and directors of the bank." *First Nat. Bank of Columbus v. Hansen*, Supreme Court of Wisconsin, June 30, 1978 (BI/03/F.-$4).

Jewelers block

A federal appellate court has upheld a decision reported earlier in this column that the terms of a jewelers block insurance policy did not provide coverage for a loss sustained by an insured by theft of goods from a store other than the one named in the policy.

Treasure Craft Jewelers Inc. (Treasure Craft) sustained a $94,000 loss in jewelry and merchandise stolen from its Southampton, Pa., store. The Jefferson Insurance Co. of New York (Jefferson) had issued Treasure Craft a jewelers block insurance policy covering jewelry in its Levittown, Pa., store. The policy had a $25,000 limit with respect to property elsewhere. A policy endorsement limited coverage also to $25,000 for property in custody of named personnel away from the premises.

Treasure Craft submitted a claim for $25,000 to Jefferson asserting the jewelry stolen was in the custody of the company president who was named in the policy. Jefferson denied the claim. A trial court ruled against Treasure Craft.

On appeal, Treasure Craft's principal argument was that the policy terms were ambiguous as to the scope of coverage of the merchandise that was stolen from Southampton and conflicted with the limitation of coverage provisions. The court concluded that the policy excluded any losses sustained by theft of goods stored in any location other than the Levittown store.

"In a policy for insurance against burglary," the court emphasized, "the specified location of the insured's property is crucial to the insuring company's assumption of the risks involved. The coverage of its policy should not extend to losses that occur in different places." The court was also satisfied that Treasure Craft was aware of the policy limitations. *Treasure Craft Jewelers Inc. v. Jefferson Insurance Co. of New York*, Aug. 14, 1978 (BI/04/F.-$4).

Bankers blanket bond

A California appellate court has ruled that false invoices submitted to a bank by a borrower in connection with its accounts receivable financing agreement with the bank were not "counterfeited" or "forged" documents within the meaning of a bankers blanket bond.

Fireman's Fund Insurance Co. (Fireman's) issued to Liberty National Bank (Liberty) a standard form bankers blanket bond which agreed to indemnify the bank against losses resulting from counterfeited or forged documents. The word "counterfeited" was defined to mean only an imitation of a security or document intended to deceive or to be taken as an original.

Liberty sustained substantial losses arising out of an accounts receivable financing agreement it had entered into with the customer. The losses were incurred when Liberty relied on several false or inflated invoices submitted by the customer. Liberty sought recovery from Fireman's for the losses but lost in the trial court.

On this appeal, Liberty contended that the false invoices constituted documents proven to be counterfeited within the meaning of the policy. Fireman's argued the word "counterfeited" was not ambiguous and, in fact, was specifically defined in the policy. The court agreed with the insurer emphasizing that fictitious invoices and accounts receivable, such as those involved here, have not been considered counterfeit. "Falsity," the court said, "lies in the representation of facts contained in the invoices and not in the genuineness of their execution." *Hinkson v. Fireman's Fund Insurance Co.*, California Court of Appeals, Aug. 24, 1978 (BI/05/F.-$4).

Workers compensation

The Court of Appeals of Oregon has upheld the constitutionality of a section of the workers compensation law that permits an unmarried cohabitant to collect benefits only if her relation with the decedent had resulted in children.

Darlene Kempf (the claimant) applied for benefits under the statute. She established that she and a worker, who was killed in an industrial accident, had been cohabiting for several years before the latter's death. The claimant acknowledged they had never married and that they had no children.

The Workers Compensation Board denied her claim. The claimant contended that there was no rational basis for the distinction between surviving partners with children and those without children, and that, therefore, the classification was invalid as a violation of the equal protection clause.

The court said there was no equal protection infirmity because that clause "does not mandate that the legislature treat unmarried couples the same as couples who have chosen to formally alter the legal aspects of their relationship by getting married." The court also believed that the legislature can extend a right that marriage would involve to some but not all unmarried couples.

"The legislature," the court said, "was entitled to reason that the surviving partner of a substantial relationship was more likely to be financially dependent than the surviving partner of a casual relationship." The birth of children and cohabitation for more than one year were, according to the court, appropriate tests for distinction between the substantial and the casual. Consequently, the court held the claimant did not satisfy the living-children requirement. *Matter of Lacey*, Court of Appeals of Oregon, June 20, 1978 (BI/01/F.-$4).

•

Copies of the entire decision may be obtained by sending a check for $4 made out to Cases Unlimited to Business Insurance, *740 N. Rush St., Chicago, Ill. 60611. Please list the number for each opinion.*

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Award upheld in embryo death

NEW YORK—A $50,000 award to a Florida woman for her mental anguish following the destruction of her test tube embryo was upheld by a Manhattan federal judge last month.

U.S. district judge Charles Stewart upheld a jury's award to Doris Del Zio against Raymond Vande Wiele, Md., Columbia Presbyterian Medical Center and the Columbia University College of Physicians and Surgeons.

In the lawsuit, brought last summer, Mrs. Del Zio and her husband sought $1.5 million in damages, alleging Dr. Vande Wiele had maliciously and wantonly destroyed a culture of eggs and her husband's sperm.

The federal judge found the jury's award "reasonable and fair," when asked to dismiss the verdict. The doctor's liability is $25,000 and the two institutions are each responsible for $12,500. ■

Equifax consolidates self-insurance services

By MARY ELLEN McKEE

ATLANTA—Equifax Services is consolidating its risk management services into one package for self-insurers and will begin marketing the product to brokers, agents, administrative service organizations and consultants in the Southeast.

The program, named Risk Management Support Services (RMS), is designed to bring the self-insurer to one place and one person for assistance at each step of the risk management process—identifying, measuring and reducing a risk and funding and monitoring a program.

This self-insurance services program is designed to cut back on manpower and paperwork and channel all available resources within various Equifax divisions into the proper and efficient administration and management of a self-insurance program, said John Olive, director of the new program.

With this consolidation, Equifax Services will become the largest independent servicing facility for the risk management market, Mr. Olive claims.

Risk Management Support Services offers self-insurers a broad range of expertise "at their fingertips" and individual attention, Mr. Olive emphasized. "These two points are the strongest features in the risk management services program and will provide the major thrust of the marketing campaign for the product which will be launched at the end of this month," Mr. Olive added.

The areas of expertise that will be available to the self-insurer include multiple line adjusting, statistical reports, safety and loss control, occupational health screening, claims investigation, rehabilitation surveys, employment security investigations and easy access to a computer system from which to obtain driving records. "There are a lot of companies that may provide various parts of our risk management package, but no company combines so many services in one sweep," Mr. Olive boasted.

Another novel aspect of the program is that a client will deal exclusively with one "account specialist" who will oversee every aspect of the risk management process in that specific self-insurance program. "Two things are accomplished by enforcing this one-to-one interaction between a client and an Equifax employe," Mr. Olive explained. "One, the Equifax employe gets to know every aspect of the self-insurance program and is then better able to evaluate the needs of his client. And the client as he begins to develop a good working relationship with the Equifax representative, will be more eager to consider the suggestions of the Equifax account specialist more carefully."

The idea for the risk management services program first surfaced last January when a group of Equifax executives were setting 1978 marketing directions for the company. At the meeting these executives made self-insurance a top priority market, Mr. Olive explained, due to the tremendous growth in self insurance.

A task force of key people from each Equifax division and corporate planning was formed to study what kind of services would best complement the self-insurance industry.

Gay & Taylor Inc., Atwell, Vogel & Sterling Inc., Physical Measurements Inc., Equifax Claims and Dataflo Systems are the Equifax divisions participating.

Gay & Taylor Inc., according to Mr. Olive is set up to design a program for each account, handle all claims administration details from required regulatory filings to writing checks for claimants, assist in recovery efforts (salvage, contribution or subrogation type collections) and manage services.

The adjusting firm will also provide the client, Mr. Olive continued, with a 24-hour claim reporting service and trained appraisers in every Equifax location around the country "to make certain that the true value is established and overpayment is avoided."

Meanwhile, Atwell, Vogel & Sterling Inc. will help the self-

Continued on following page

from museums to motor truck cargo

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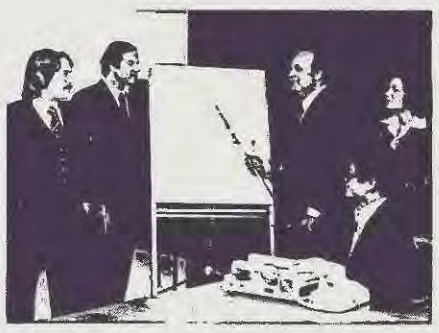

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Continued from preceding page
insurer pinpoint existing hazards on the worksite, make recommendations to eliminate those hazards and provide resources to interpret loss data.

Physical Measurements Inc. will conduct employe health evaluations, devise programs customized to meet the medical objectives of the client, develop ongoing clinical records and conduct surveys to determine how the work environment affects an employe's health.

With facilities nationwide, Equifax Claims will provide investigation services tailored to the client's specifications, a claims specialist to act as a regular contact in each of the facilities and prompt and on-the-scene handling of each claim. This feature of the new program alone means direct cost savings to the self-insurers, Mr. Olive claimed.

Equifax's extensive network of offices across the nation will cut down on charges for long-distance travel or markups for out-of-town investigations, Mr. Olive noted, and will also offer quicker service.

Dataflo Systems was designed specifically for the self-insurer of a fleet of automobiles or trucks, the new program director commented. The motor vehicle records service will provide a self-insurer with information about the overall driving record of a person applying for position as a driver.

This data processing system, Mr. Olive explained, is designed to tie in with any in-house system and will help a company curb unnecessary risks by hiring safe drivers.

Equifax is planning to introduce the risk management package to brokers and agents this month at seminars highlighting the program's concepts. Based on the response from the brokers and agents in the Southeast region, Equifax will then consider expanding the self-insurance support package into other areas of the country, Mr. Olive said. ■

J&H buys in Mass.

Johnson & Higgins has purchased David A. Wilcox and Sons, an insurance broker in Arlington, Mass., in order to gain a greater presence in the greater Boston area. Although J&H has operated an office in downtown Boston since 1963, this move enables it to serve a number of important clients that David A. Wilcox has in the area. James and Walter Wilcox, the two principals of the firm, will become senior members of the J&H staff.

Report blasts doctors' stronghold over Blues

WASHINGTON—Congress should consider legislation that would give the federal government greater power in regulating Blue Shield plans to break up doctors' dominance in setting medical payment schedules, a House subcommittee recommended.

The House Interstate and Foreign Commerce subcommittee on oversight and investigation found that nearly all 69 Blue Shield boards are controlled by doctors and other health care providers who have a vested interest in rising health care costs.

While not denying that doctors dominate Blue Shield boards, BC/BS president Walter McNerney said there is no demonstrated correlation between the number of physicians on Blue Shield boards and the price of medical service.

The subcommittee report, however, said physicians serving on Blue Shield boards have an inherent conflict of interest because their financial interest "is hostile to that of subscribers.

"We find it hard to believe that a physician whose group practice receives up to $500,000 from Blue Shield in 1977 is unconscious of that fact when making reimbursement decisions," the report said.

The report singled out the District of Columbia Blue Shield plan as an example of how doctor domination of Blue Shield leads to higher physician fees with no incentives for cost containment.

Under the District of Columbia Blue Shield guidelines, reimbursement schedules are revised annually by the doctors to reflect national increases in either physicians' fees or the cost of living, whichever is greater.

Such rules "demonstrate an attempt to maximize the usual charges of a physician" and "almost preclude" attempts to hold doctors' fees below the rate of inflation, the report found.

Significantly, the report found that in Delaware, one of the few Blue Shield plans not dominated or controlled by physicians, insurance premiums dropped 7% in 1978.

The report singled out the District of Columbia Blue Shield plan how buyers are excluded from the plan. Of the 15 board members, 10 are doctors. The five remaining "public" members include the president of Blue Shield, two hospital officials, the president of the state AFL-CIO, which represents hospital workers, and an officer of the bank that is the investment manager for Blue Cross.

The report lashed out at state officials, who under the McCarran-Ferguson act regulate the insurance industry, for not acting to curb conflicts of interests in the 69 local Blue Shield plans.

Of those 69 plans, the report found 44 plans are controlled by doctors and hospital officials. In eight other plans, the directors are selected by the physicians.

Plans in Ohio and Wisconsin are operated by state medical associations, which also approve board members in 56 other plans.

Fee-setting committees of 68 plans are dominated by doctors, with Delaware being the only exception. ■

Safety groups earn dividends

PHILADELPHIA—Howard Johnson Motor Lodge Operators Council earned a 19.5% dividend as a safety group policyholder of Pacific Employers Insurance Co.

Dividends, which depend on loss experience and member participation, are expressed as a percentage of the premiums paid by participants, so a 22% dividend would return $220 in cash for $1,000 paid in premiums.

Safety groups are composed of small and medium sized businesses that are members of trade associations or meet group eligibility requirements. An individual package of fire, theft and liability insurance is written to meet the needs of organization members.

In 1977, more than $6 million in dividends was returned to trade association members participating in safety group programs. ■

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Reporting requirements

FASB rule may apply to public pension plans

STAMFORD—Despite objections from representatives of public employe retirement systems, the Financial Accounting Standards Board has tentatively decided that reporting requirements currently being drafted for defined benefit pension plans should apply to state and local government funds as well as private sector plans.

The board decided that there was not enough distinction between public and private sector plans to call for exclusion of the public plans from the rules, said Jules Kassel, FASB employe benefits project manager.

He noted that specific rules could be applied differently to public plans, but a decision on that would be reached later.

While some administrators of public pension funds opposed coming under FASB's standards, others said they would have no problems with the change. "We don't see it having any effect," said B.K. Walters, executive director of the Municipal Employes Annuity and Benefit Fund of Chicago. "Our accounting staff doesn't feel it will be too much of a burden, even though it will involve a little more detail work."

John LaCarrubba, executive director of the New York City Board of Education Retirement System, said the FASB rules would create "no problem for us as long as they don't tell us how to run the system."

However, Warren Black, executive secretary of the Missouri Public School Retirement System, said the FASB rules would create a lot of unnecessary duplication of work. He cited as an example the requirement for corporations to measure the day-to-day valuation of bonds as well as their long term value.

"The FASB doesn't realize that public funds are different in that much of the reporting standards in the private sector are for tax purposes and have no bearing on public funds," said C.M. Sullivan, director of the Arizona State Retirement System.

Because public funds investment income is tax exempt, public funds should have greater flexibility in how they report capital gains and losses, he argued. Arizona currently operates its pension system under private sector rules. Mr. Sullivan has tried to implement more flexible rules, but was opposed by state auditors.

In a statement issued early in 1978, the Task Force on Public Employe Retirement Systems of the National Council on Government Accounting objected to several provisions of an FASB exposure draft on reporting requirements.

Those concerns centered around the distinctions between public and private sector pension plans, said Tony Mandolini, chairman of that task force and a partner in the Chicago office of Peat, Marwick, Mitchell & Co.

Specifically, the task force cited inconsistencies between the proposed reporting format and formats currently used by most public plans, differing bases for investment valuations and methods for determining the accrued value of benefits.

Mr. Mandolini said his task force hopes to meet with FASB staff members in January to try to resolve disputed issues. ■

Life insurance grows

Life insurance purchases in October totaled $34 billion, a 12% increase from the $30.18 billion in purchases made in the same month a year ago, the American Council of Life Insurance says. Industrial life insurance purchases in October were $658 million, compared with $578 million a year ago. In addition, group life insurance set up under new or revised group contracts cost $8.68 billion in October, slightly higher than the $8.59 billion in purchases in October 1977.

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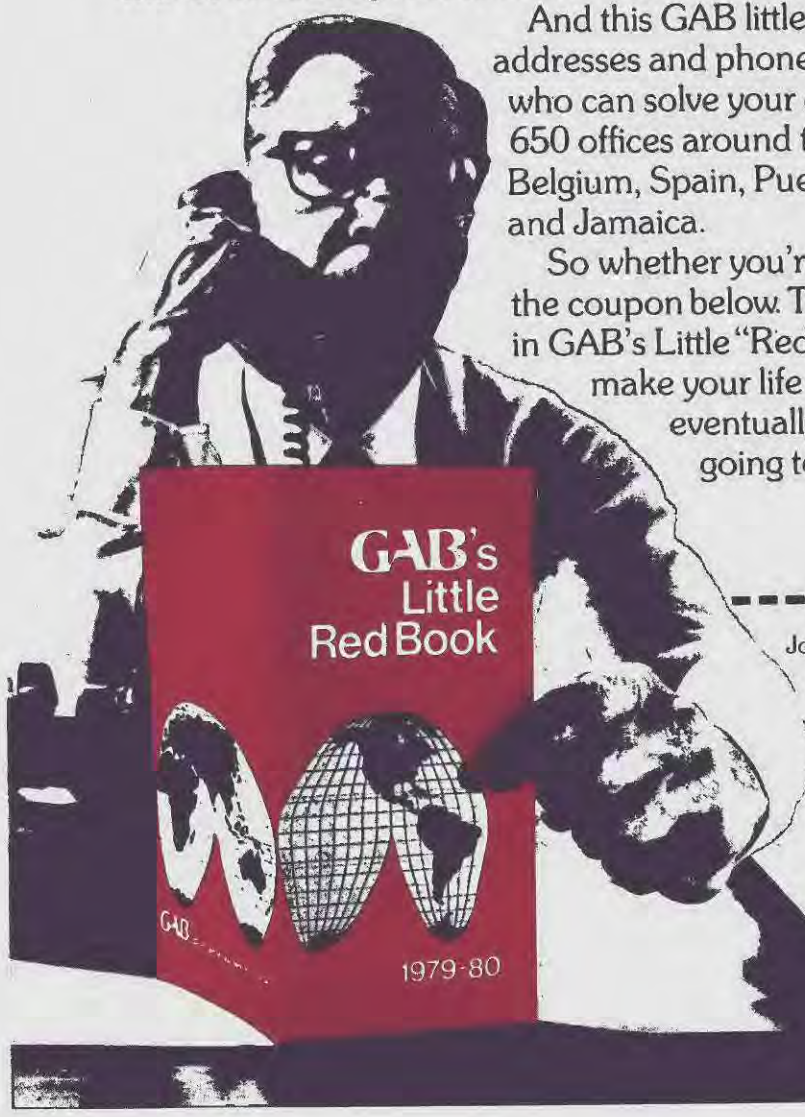

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FAA proposes new rules for improved air safety

WASHINGTON—The Federal Aviation Administration has proposed sweeping changes in air traffic control systems to reduce the risk of aircraft collisions.

The FAA safety proposals, announced late last month, were stimulated by a September mid-air collision of a Pacific Southwest Airlines jet and a single-engine Cessna over San Diego. One hundred forty-four persons died, making it the worst air accident ever to have occurred in the U.S. Three suits have been filed in U.S. district court in San Diego in connection with that accident. Many more suits are expected to follow.

FAA chairman Langhorne Bond said the agency had become "complacent" about the danger of a collision before the San Diego accident, because there hadn't been a single mid-air crash involving a major commercial airliner since 1972.

However, in that six-year period, there had been about 1,000 near-collisions. Mr. Bond said the safety changes will reduce by 80% the number of near-collisions at altitudes above 10,000 feet.

Under the FAA proposals, an additional 44 airports will be placed within blocks of airspace called "terminal control areas." Twenty-one such areas exist today. A pilot must receive permission from an air traffic controller to enter a terminal control area and the plane must be equipped with certain navigational and radio devices. Student pilots cannot enter.

In addition, the altitude above which planes cannot fly without specific permission will be lowered to 10,000 feet from 18,000 feet east of the Mississippi River and in most of California, and to 12,500 in other areas west of the Mississippi.

Furthermore, radar display units in airport towers will be improved to provide air traffic controllers with altitude readings and other information about the planes in their areas. The San Diego tower controllers lacked the improved radar displays.

Finally, 24 new instrument landing systems will be installed at non-commercial airline airports in metropolitan areas. The Cessna in the San Diego collision was practicing on an instrument landing system at the San Diego main airport because that was the only such system available within 40 miles.

FAA chairman Mr. Bond said the new equipment will cost about $43 million. Three hundred new air controllers will be hired to operate the equipment at an annual cost of about $11 million.

The Professional Air Traffic Controllers Assn. said at least 2,000 new controllers are needed to upgrade safety at the nation's airports. ■

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PBGC loses Salisbury to benefit group

WASHINGTON—Dallas Salisbury last month left the Pension Benefit Guaranty Corp. (PBGC) to become executive director of a new benefits research organization.

Mr. Salisbury, who directed the PBGC's multiemployer pension plan task force, will direct the Employe Benefit Research Institute, founded by 13 actuarial and employe benefit consulting firms.

EBRI will collect information on a wide range of benefit issues including the impact of inflation on retirement income, the appropriate way of integrating public and private pension systems and the effect of an aging population on the retirement system.

Members of the institute include: Alexander & Alexander Inc.; Buck Consultants Inc.; A.S. Hansen Inc.; Hewitt Associates; Johnson & Higgins; Kwasha Lipton; Martin E. Segal Co.; Meidinger & Associates Inc.; Milliman & Robertson Inc.; Tillinghast, Nelson & Warren Inc.; Towers, Perrin, Forster & Crosby Inc.; The Wyatt Co., and William M. Mercer Ltd. ■

london line

U.K. doctors fear surge of suits after recent award

By JOHN MILLER

LONDON—Doctors in Britain fear they may face a sudden surge of malpractice claims after a high court judge awarded $200,000 of compensation to the mother of a 9-year-old boy injured during delivery.

His brain was damaged at birth after surgeons had used forceps for the delivery.

Claims for medical negligence are now running at more than $4 million a year in the U.K., still much below U.S. levels, while indemnity premiums are rising by 75%.

After the judge told consultant surgeon Joseph Jordan that his method of delivering the baby had fallen below the standards professional competence required by law, the surgeon protested "I am concerned about the verdict, which might make some doctors wary of delivery methods. If we start practicing medicine with lawyers sitting on our shoulders, it may not be good for the patients."

Raymond Booth, his colleague and secretary of the Royal College of Obstetricians and Gyneologists, agreed, "Doctors will now be wary of trying to resuscitate babies for fear of producing damaged children whose parents will sue for negligence," he said. "There is fear that there will be reaction toward 'defensive' medicine by many medical men after this verdict, unless it is overturned on appeal."

Change predicted

Lloyd's announced intensive probe into its powers over members and its soaring membership, now approaching 17,000, suggest there may be a change in its present self-regulatory structure.

Details of the inquiry will be announced soon. During the year there will be a flow of information to Lloyd's regulatory powers sent to the working party, now being organized to meet the criticism that has been leveled against the market in recent months over some of its decisions.

But no one expects drastic developments until all the problems of running such a huge organization, with a premium income likely to top $5 billion, have been explored.

Effective control over the conduct of underwriters and brokers at present is exercised by a committee of 16 who are elected by annual rotation for four-year terms.

They are working members, chosen by their own colleagues, under traditions more than 200 years old. Their role is explained as "doing all things conducive to the functions of Lloyd's."

But running a highly complex organization in the 1980s will clearly be so time consuming that the strain must begin to tell on their constitution, since their services are entirely voluntary and have to be fit into their daily work.

Now might be the time for change, but only after all the market's needs have been considered, as they will be in the next few months.

Changes in Lloyd's internal controls, however, will not mean any shift in its traditional attitudes toward the public, where the syndicates still provide unlimited liability, the unique attribute of the Lloyd's market in world insurance.

Export insurance

Britain's state-controlled Export Credits Guarantee Department, which offers protection to firms operating abroad against sudden political expropriation and war risks, will raise its premium rates by about 10% by April.

The increase reflects the effects of inflation and adverse claims experience in some areas. Rates for this type of cover were raised less than two years ago, but did not adequately increase the reserve funds.

For comprehensive cover on U.K. exports sold on short-term credit (up to six months), which is running nearly $25 billion a year in capacity, the premiums will rise by between three cents and nine cents per $100 of insured values.

The object is to hike average premium income to 32 cents per $100 for this class of business. This was the target figure of the 1977 rate increase, but it was not achieved because of the difficulties on calculating the precise effects of such increases.

For business on terms of two years or more, ECGD is streamlining its premium system to simplify procedures for exporters. But it will still aim to earn another 5% in income. There will be room for discounts when payment arrangements are spread over time and the maximum amount of risk at any one time is less than the overall insured value of the contract.

ECGD wants to maintain reserves equal to 2.25% of the amount at risk in its commercial account by the early 1980s. The ratio has currently fallen to 1.9%.

Victims of crime

More than $100 million has been paid out to victims of violent crime in the U.K. in the last 14 years by the Criminal Injuries Compensation Board, a state-funded plan.

Set up to help people who could not recover normal insurance damages after being injured by muggers or bank robbers, it paid out a record $20 million in 1978. This is double the figure of four years ago and reflects the rising cost of crime in Britain.

Damages are awarded on the basis that normally applies in civil actions. The highest award in the past year was $120,000 to a 22 year-old man who was almost paralyzed by brain injuries suffered in an assault by a sidewalk robber seven years ago.

The fund has paid about $100,000 to people hurt in periodic street riots, including police personnel, and there is a provision to help people hurt in bombings.

The psychological effect of criminal assaults is stressed by the board. "It seems obvious the offenders in many cases never contemplated the disastrous results of

Continued on following page

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Continued from preceding page
their crime, which have turned tough men into a shadow of their former selves or made young women too frightened to go out at night. Such cases are costing large sums of money in awards from the board or in other social security aids."

Auto injury costs

Plans to compensate victims of auto accidents by a levy of two cents a gallon on gasoline have been turned down by the U.K. government, which wants more time to study no-fault proposals submitted by a public commission 10 months ago.

The ultimate charge on public funds will run to more than $100 million a year, but so far there is no intention to make it retrospective to aid people already disabled by such mishaps.

Terrorist insurance

Insurance cover up to $150,000 is being purchased for members of Japanese embassy or consulate staffs who may be prone to terrorist attacks in foreign countries. They will receive about $90,000 if their hand or leg is maimed, while $150,000 will be paid to their families if they are killed.

The scheme has been prepared by the Japanese Foreign Ministry under an arrangement with Kyoel Mutual Fire & Marine Insurance Co. Premiums must be paid by the ministry's employe welfare fund since official money cannot be used for this purpose. It is expected that 1,500 staffers in more than 150 Japanese embassies or consulates will be covered when the scheme is fully operational.

U.K. accepts Moscow

The U.K. government rejected a request to try to move next year's Olympic games from Moscow, on which the National Broadcasting Co. holds a $50 million cancellation cover.

The London market wrote $40 million of the policy for NBC and $10 million is written elsewhere (*BI*, Sept. 18).

U.K. sports minister Denis Howell told Parliament, when it was asked to try to get the venue changed, that the Olympic games are the only place where the youth of the world "mixed freely together" irrespective of creed or color.

Labor MP Eric Moonman, from Basildon, Essex County, urged the venue be moved because of Soviet suppression of human rights. But he was told by Mr. Howell, "British sportsmen decide for themselves where they should go."

Milking insurers

Insurance companies in Britain are being pressed to contribute to a $2 billion fund which trade union backers of the present Labor government would like to see established for investment purposes.

The fund is not yet in existence, though efforts to bring it into being with money from pension funds and North Sea oil revenues are now being examined in political circles.

Ron Peet, chairman of the British Insurance Assn., complains that the proposals for the fund are "quite unrealistic," as industrial development will not be achieved in this way.

The contemplated fund would be under state control, so that its cash could be channeled in directions not touched by private investment.

"Trade unionists have been quick to see that nationalization of U.K. insurance companies is not a sensible idea," Mr. Peet explains. "But they have not outlined the criteria which should be applied to this proposed investment fund. An improvement in the profitability of U.K. industry is wanted by everyone, but this will not be achieved by milking insurance funds to support projects which cannot be justified on commercial grounds.

"If the British government believes that certain investments are desirable on social grounds alone, they should finance these through taxation of the public, and not by picking the pockets of the prudent," he suggested.

Nuclear waste

New arrangements to cover the risk of dumping nuclear waste at sea have been made by the British government. In the future the U.K. Atomic Energy Authority can issue full indemnity for any claims made against shipowners as a result of damage or injury caused by their role in such processes.

Until now the indemnity had to be approved by the government in cases where ships were being used to dispose of nuclear waste. The U.K. has been disposing of solid, low-activity nuclear waste at sea since 1949, and its safety measures are so well prepared that no compensation claim has ever been made. ■

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School offers study grants for safety

TUCSON—Stipends are available to students enrolling in the graduate program in safety management at the University of Arizona here.

The program consists of 45 units of study, including 21 units of MBA courses in business administration, 21 units of safety management and related courses and three units of research. A full time student should be able to complete these requirements in 13 months of study, earning a Master of Science in Finance with a specialization in safety management.

The program is one of the core areas of the Arizona Center for Occupational Safety and Health, funded by a grant from the National Institute for Occupational Safety and Health.

Stipends of up to $3,900 a year are available on a competitive basis and research assistantships are available to interested students willing to extend their academic training over 24 months.

The university is interested in attracting persons who are currently employed and want to pursue a graduate degree in safety management as well as students completing an undergraduate program.

Nestor R. Roos is director of the safety management program at the University of Arizona. ■

New services firm

Marketing Management Inc. of Birmingham, Ala., has formed a new loss control and safety service subsidiary, Management Safety Inc. MSI will provide technical training in personnel management, equipment maintenance, safety, hazard control and communications for insurance clients of the parent company and the business community.

Firms bolster profit sharing in wake of ERISA: Study

By MARY ELLEN McKEE

EVANSTON—An extensive survey of 38 large companies nationwide shows that management made "a virtue out of necessity" when it was forced to revamp company profit sharing plans to meet the legal requirements of the pension reform law.

"Management in these companies not only brought their plans into compliance with ERISA, but also strengthened their profit sharing programs. . .sometimes in dramatic ways to serve more effectively as organizational incentives and retirement income plans," observed Bert L. Metzger, president and treasurer of the Profit Sharing Research Foundation here, which prepared the study.

The study examines current eligibility requirements, employe and company contributions, vesting procedures, forfeitures, investment practices and pension plans of 24 industrial companies, 10 retailers, three commercial banks and one insurer and analyzes what trends in these plan features were a direct result of ERISA.

By the end of 1976, the 38 companies in the profit sharing study had a cumulative total of 1,173 years of profit sharing experience. All except two have had a profit sharing relationship with their employes for at least 20 years.

Of the 38 companies, 24 or 63% are unionized to some extent and 19 out of the 24 or 79% include their unionized employes in the profit sharing plans.

ERISA, passed by Congress in 1974, accelerated the trend toward shorter waiting periods, to join profit sharing plans, the study shows. But the law interfered with the trend toward reducing or eliminating minimum age requirements the study says. Over 70% of the plans examined require a waiting period of less than two years of service before entering a profit sharing arrangement, while the remaining 21% have multiple requirements involving age and service factors.

Profit sharing plans are becoming increasingly contributory, mostly on a voluntary, not a mandatory basis. Over two-thirds or 68% of the profit sharing plans use contributory features but the majority of the them do not require employe contributions as a condition for participation in profit sharing. Voluntary contributory plans rose from the least popular to the most popular type of plan.

The study also found that 83% of the 38 companies have either raised the dollar ceilings on employe contributions or have eliminated the ceiling entirely.

No major shifts in company contribution practices among the 38 companies, however, have occurred since the last study, based on information gathered prior to enactment of ERISA, but published in 1976.

Fixed formulas rather than discretionary arrangements determine company contributions to profit sharing for almost all of the companies in the current survey, published recently. This feature remains relatively unchanged from the results of the pre-ERISA study.

Seven out of 10 companies or 70% of the companies utilize a specified-percentage-of-profits, close to figures of the last study, with two companies switching from sliding scales to specified-percentage-of-profits. The remainder of the 38 companies calculate company contributions on a sliding scale.

Three out of four companies share from the first dollar of profits and up with their employes without setting any minimum profit guidelines for company contributions to the plan. However, those companies do specify that employes must meet certain conditions before sharing in the profits.

Nine companies guarantee a minimum contribution to profit sharing each year—even in low profit or no profit years. Most of these guaranteed contributions are stated in dollars, as a minimum match of the employe contributed dollar, or as a percentage of pay of the participants, the study reveals.

Compensation is the sole or partial allocation factor in 74% of the plans. With the shift to voluntary contributory plans, there is also an increasing tendency among the 38 companies to base allocation less on employe savings and more on employe compensation, with employe contributions and length of service playing a minor role when compared to the last study.

Swifter and more uniform vesting patterns have also emerged af-

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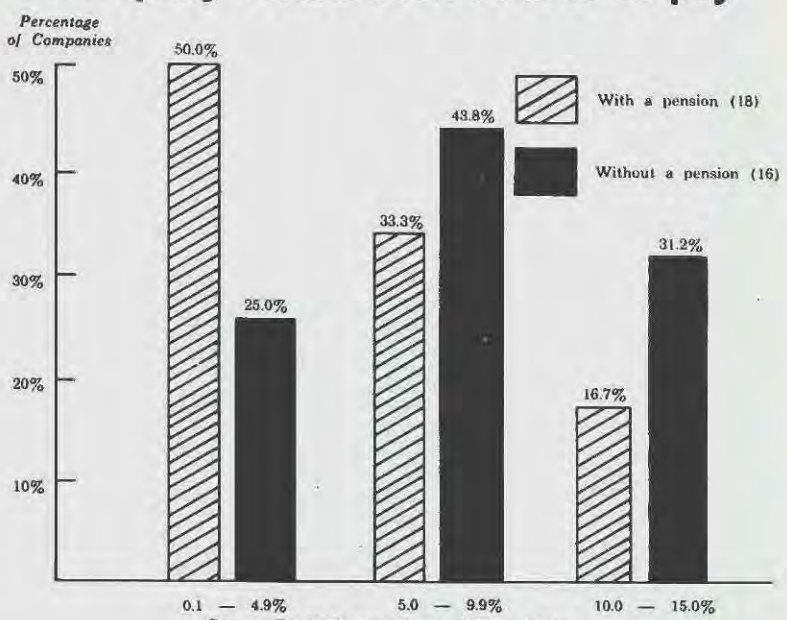
Company contribution as a % of pay



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Profit sharing study . . .

Continued from preceding page

ter ERISA, the study indicates. Five to 15-year graduated vesting is, by far, the most popular type of vesting schedule, with 24 of the participating companies employing this procedure. Full and immediate vesting occurred in seven of the companies and five plans use full deferred or "cliff" vesting.

The "golden handcuff" concept of retaining people through long vesting schedules is a thing of the past, study figures reveal. Over 60% of the plans fully vest participants after 10 years of service and, as required by ERISA, all plan participants are fully vested after 15 years of service. Certain plans, the study indicates, now provide full vesting after a designated age, with no consideration of the years of service, at early retirement or upon termination "through no fault of the employe."

ERISA has greatly changed the handling and reallocation of forfeitures too, the study shows. Companies are deferring the reallocation after a one-year break in service instead of reallocating forfeitures in the year of the employe's termination.

Specific purposes for loans and withdrawals made from profit sharing funds have broadened as a result of ERISA. But companies without pension plans and with noncontributory profit sharing plans either prohibit loans or withdrawals, or structure their withdrawal features so that the long term adequacy of the accounts will be preserved.

Management personnel among the 38 companies in the study have found that the loan and withdrawal feature adds new and attractive dimensions—flexibility and employe self-determination—to the profit sharing plan.

Giving employes new money and transfer of balance options have doubled among the 38 companies since the last study. Investment practices among the 38 profit sharing trusts differ considerably, with 10 companies or 26% using a diversified portfolio, another 26% of the companies investing exclusively or predominantly in their own company stock and 18 or 48% establishing distinct funds for employe investment choice.

In the contributory plans, the employe can choose how both his money and company contributions will be invested in 10 out of 13 or 77% of the plans. The employe can choose the investment vehicle only for his own contributions in plans in three of the surveyed companies.

Usually three types of investment funds are available to the employe: an equity fund, a fixed-income plan and a fund of the employer's company stock. Members of the 38 profit sharing plans in the study can normally channel contributions into one or more of the funds in 10% multiples.

Three out of four plans permit participants to transfer their account balance from one fund to another, up from one-half in the pre-ERISA study. Fifteen companies limit this transfer privilege to groups of participants who meet age and service requirements, while 13 companies extend this transfer option to all participants.

Ninety-five percent of the companies invest to some extent in their own company stock with invested percentages ranging from 1.8% to 100%. Seventeen companies hold employer securities amounting to over 50% of their profit sharing trust assets.

Providing voting rights to plan members is also becoming a popular practice among employers, the study indicates. Fifty-three percent of the companies use this feature in their plan compared with 43% which offered their employes the pass-through-voting arrangement in the similar pre-ERISA study.

Investment guidelines, which are designed to reduce the market risk of the profit sharing participant, on the other hand, have been adopted by one in three of the companies in the current study.

Slightly over half or 58% of the companies have pension plans in addition to profit sharing. This percentage, the study asserts, has not changed during the post-ERISA period, though several "modifications" have been made in each group. Most pensions in this study were final average pay, defined benefit plans,with an offset of up to one-half of the primary Social Security benefits.

According to the study, companies with pension plans as their basic retirement income security program in addition to a profit sharing plan are likely to include cash-deferred options, more liberal partial withdrawals, employe investment choices and more investment in the company's own stock as features in their profit sharing plans. ■

Insurers pay $15 million

SANTA CLARA, Calif.—National Semiconductor Corp. expects to recover about $20 million from its insurers for losses resulting from a 1977 fire that destroyed most of its production facility near Glasgow, Scotland.

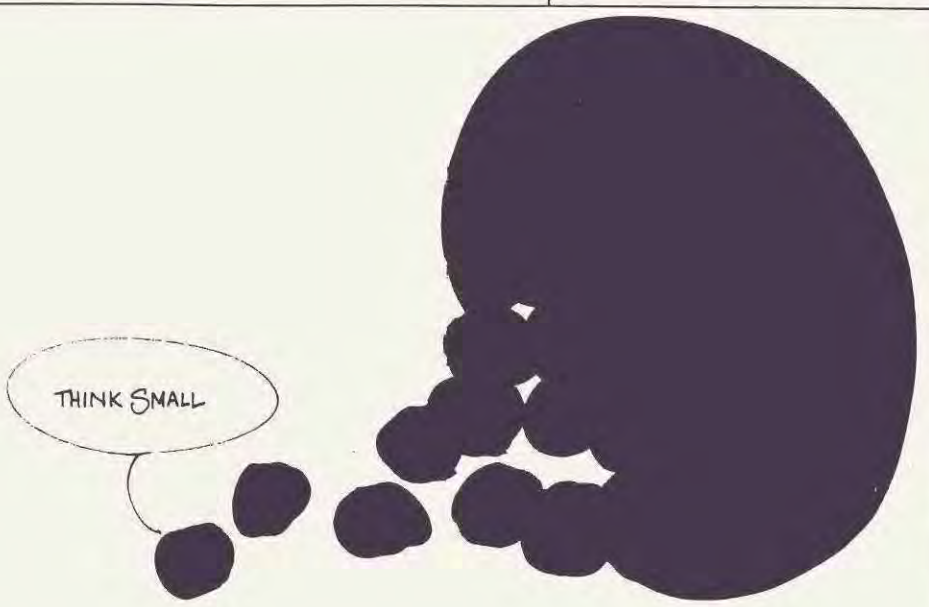
The company announced in early December that it had received a $7.8 million payment from Lloyd's of London, one of its major insurers, bringing to $15 million the total insurance recovery on the loss.

Paul York, director of corporate insurance for the firm, said the total settlement includes six American insurers, whom he declined to name pending receipt of the balance of payments.

The fire loss included $9.5 million in damages to the physical facilities and $10.5 million in business interruption losses.

The blaze broke out the morning of April 22, 1977, in a manufacturing area of the plant where the company makes integrated circuit "wafers" for its line of electronic products.

There were no injuries, but manufacturing was knocked out at the facility for about eight months. Full production has not yet been restored because of difficulty and delays in replacing some sophisticated technical equipment. ■



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Deadline for swine flu claims causes filings to hit 3,300

WASHINGTON—Two years after the Ford Administration called a halt to the ill-fated swine flue mass immunization program, more than 3,300 claims seeking about $3 billion in damages have been filed against the government.

The number of claims filed surged in December, probably due to the popular misconception that the deadline for filing claims was Dec. 16.

In fact, the filing deadline was two years from the time of injury. Forty million swine flu shots were administered between Oct. 1, 1976 and Dec. 16, 1976, so the statute of limitations may have expired months before Dec. 16, 1978 for some people who say they were injured as a result of the vaccination.

As of Dec. 15, a total of 3,329 claims asking for $3.159 billion in damages had been filed. At the same time, 11 claims totaling $36,649 had been settled. The settlements ranged from $8,000 down to $49.50 awarded to a person who claimed that the shot was improperly administered, leaving her with one very sore arm.

The biggest claim was filed by a 84-year-old man who claimed everything in the world was wrong with him as a result of being innoculated. "He even claimed that the shot made him lose his appetite," recalled Jeffrey Axelrad, Justice Department tort branch director.

"The 84-year-old man sent a letter along with his claim telling us exactly where to send the check for $900 million. He was very precise," Mr. Axelrad said. The man later withdrew his claim.

The swine flu program is filled with bizarre claims. One woman, for example, sued the government for $1 billion. A Justice Department attorney contacted the woman and asked: "Do you really mean $1 billion?" The woman said she must have made a typographical error and inadvertently added three zeros to her claim, she only sought $1 million. Her $1 million claim is still pending.

Perhaps the most unusual claim was filed last month by someone who claimed that after receiving the swine flu shot, he became a compulsive water drinker.

But many claims appear to be serious. According to the Center for Disease Control in Atlanta, 532 persons were stricken with Guillain-Barre, a rare syndrome that results in paralysis, after they received a swine flu shot. Of those 532 Guillain-Barre victims, 32 died.

Although the government has only paid out about $36,000 to swine flu victims, Mr. Axelrad expects a significant increase in payments as more claims are settled in the months ahead.

"Settling claims will be drawn out over an extended period of time," Mr. Axelrad said. "If you call me at this time next year, we still will be talking about litigation."

Under the Federal Tort Claims Act, the Justice Department reviews all claims and rules on their validity. If the department decides a claim is valid, it negotiates the amount of the settlement.

If the Justice Department decides a claim is not valid, a plaintiff can sue the government in U.S. district court. A plaintiff can only seek compensatory and actual damages; punitive damages are not allowed.

Several attempts have been made by plaintiffs to sue the manufacturers of the vaccine. But the Supreme Court ruled recently that plaintiffs can only sue the government as established by a law Congress passed in 1976 in which the federal government agreed to accept primary liability.

However, the government does retain the option of suing the drug manufacturers if it can prove that the manufacturers were negligent in producing the vaccine. No such evidence has turned up and Mr. Axelrad said there are no current plans to sue the manufacturers. ■

Insurers wary of oil, gas drilling

NEW YORK—New oil and gas drilling operations in the Canadian Arctic are increasing costs and pressures for Canadian marine underwriters, the president of the Canadian Board of Marine Underwriters said here recently.

"We are developing a lot of very high-classed technology at a very high cost," said Samuel T. Byron Jr., at a recent meeting of the American Institute of Marine Underwriters. "This is being developed by extremely competent people, but it is not productive and will not be productive until we have the ability to get the product ashore."

Canadian underwriters are taking closer looks at each marine risk, he said. ■

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Umbrella liability 25% less

Fuqua finds markets responsive

ATLANTA—Robert S. Spencer, vp-risk management at Fuqua Industries Inc., is stepping into the new year with 25% and 15% casualty premium reductions.

Fuqua recently renewed its primary casualty insurance and umbrella liability coverage in a more competitive market, which allowed Fuqua greater flexibility in selecting insurance carriers and granted the Atlanta-based firm large premium reductions.

"The experience was very pleasant," Mr. Spencer said. "It looks like it's going to be a good year."

"It didn't surprise me," Mr. Spencer said. "In the summer we began to see the market easing. It's the old cycle in insurance companies that when companies generate an underwriting profit, they get more competitive."

Fuqua, which bid its umbrella liability coverage because the premiums were too high, secured a 25% premium reduction this year, Mr. Spencer said, by switching back to The Home Insurance Co. from Northbrook Insurance Co. "The Home was very competitive in writing it," Mr. Spencer noted.

Fuqua moved its umbrella policy from The Home to Northbrook last year to obtain a policy that did not exclude punitive damages. Last year The Home was among several other insurers excluding punitive damages under a now abandoned industry decision. In the fall of 1977, the Insurance Services Office had said it was revising liability policies to exclude coverage for punitive damages. The Home Insurance Co., however, is again writing policies that do not specifically exclude punitive damages.

"There's no question about it, punitive damage coverage is much more available now," Mr. Spencer said.

In renewing its primary casualty insurance with Old Republic Insurance Co. for the second year, Fuqua's premiums were decreased 15%. Old Republic acts as a fronting company for Fuqua, ceding reinsurance to its Bermuda captive insurance company, Fuqua Insurance Co. Previously, Commercial Union Insurance Co. was the firm's primary carrier. ■

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riskWatch

By SUSAN ALT

Study reveals ways employers could encourage health, fitness

Work safety, productivity and total health insurance costs have long been recognized as influenced by overall employe health and fitness. Similarly, preventive medicine has long been recognized as the way to bring about better health and fitness.

None of this is surprising, although a new study performed by Louis Harris & Associates for Pacific Mutual Life Insurance Co., made public just last month, shows there are some contradictions between what we believe is good for us and what we've been willing to do get fit and stay that way.

Alt

It's almost universally agreed that preventive health is one good way to curb future increases in health care costs. Business leaders at the largest companies in the nation, in fact, favor this method of controlling health care costs over all other possible solutions.

More people than ever understand the benefits to be gained from eating healthier foods, not smoking, exercising regularly, maintaining proper weight and drinking less. Yet, the fact remains that obesity and coronary disease are national plagues. A large population persists in smoking and overconsuming drugs and alcohol.

Nonetheless, more people have begun exercising regularly, millions have stopped smoking and public knowledge of diseases such as cancer and hypertension has increased greatly. Even more heartening is the enthusiasm expressed by survey respondents for regular exercise programs at their places of work, changes in benefit programs encouraging preventive care and examinations rather than in-hospital treatments for acute illness, information programs on fitness and nutrition and counseling for such problems as obesity, alcoholism and drug abuse.

Employers and employes alike appeared most enthusiastic about benefit programs that would provide first-dollar coverage for visits to doctors and other out-of-hospital treatments, while penalizing users with a $100 or $150 deductible for in-hospital care, even if the programs were to cost up to $5 a month more.

Harris found 81% of all businesses consider health insurance for employes a major cost of doing business. Employers generally believe doctors, hospitals, insurance companies and the American Medical Assn. bear heavy responsibility for controlling health care costs. While almost all businesses acknowledged their own responsibility in controlling health care costs, only 54% said employers have "a great deal" of responsibility for these controls.

Over two-thirds of all companies are already taking steps to limit employe health care costs, though labor leaders don't agree this employer-involvement is quite so prevalent. Employers most often use second surgical opinion programs (37% of all companies), monitor hospital and doctor fees (18%) and establish health maintenance programs providing employe education, diagnostic testing and physical exams (12%). Very few (only 1%) are negotiating with unions to change or decrease benefits.

Although 37% of all companies say they pay for a second opinion before surgery to verify the need for the operation, only 6% actually insist on a second opinion.

An interesting, and alarming, contrast is evident in employers' views of what kind of benefits they think employes prefer. Nearly three-fourths of companies think employes would prefer fee-for-service health care, and only 9% said employes would want prepaid group care. But by contrast, union leaders indicated employe preference for prepaid group practice care would be much higher relative to fee-for-service care (40% versus 49%).

Pacific Mutual and Harris concluded the opportunity for employer involvement in preventive medicine and cost control—particularly by launching counseling programs and educational campaigns encouraging workers to stay fit—is tremendous.

The survey makes patently clear that a substantial majority of Americans believes serious diseases can be prevented and controlled if identified early enough by doctors as a result of regular check-ups. As many as 65% of all employers claim they already provide regular examinations for at least some employes, but it looks as if employers could provide—and promote—a benefit perceived as one of the most valuable in a benefit package: annual employer-paid physical exams for employes.

Doctors can't countersue in N.Y., face more liability

By ELLIS SIMON

NEW YORK—Two rulings by New York State's highest court, handed down within a week of each other, are likely to aggravate the malpractice threat faced by doctors here.

The state court of appeals ruled late last month that lawyers who act maliciously and unethically in bringing baseless malpractice actions against doctors can't be held liable for damage to the doctor's reputation.

In an unrelated action, the court decided that doctors can be sued for malpractice if they fail to properly advise a patient that she risks bearing an abnormal child.

Dr. Eugene E. Drago of Schenectady attempted to collect damages from Albany attorney Jerome Brownstein. The attorney had filed a malpractice action against Dr. Drago on behalf of the survivors of a patient who was not under Dr. Drago's care.

In its ruling, the court of appeals reversed an appellate division opinion stating that Dr. Drago had adequate cause for a tort action. The court of appeals chose to act with "judicial restraint" since there are proposals before the state legislature to "create new liabilities in such a circumstance."

Harold Blodgett, attorney for Dr. Drago, said he was "shocked" by the court of appeals ruling against the doctor. "The facts in the Drago case are more pronounced than in any other case in the United States we know of," to justify the doctors suit against the attorney, he said.

Although doctors have won such suits against lawyers in the lower courts of other states, in no state has the highest court ruled in favor of the physician, noted Joel Edelman, legal consultant to the Illinois State Medical Society.

Doctors, angered at injury to their reputations and the cost and trouble of baseless malpractice actions against them, fought back against the plaintiff attorneys. They reasoned they were not only clearing their own names but also setting examples that would cause plaintiff attorneys to think twice before representing a client in a malpractice action.

The supreme court in Iowa has also thrown out a similar suit by a doctor against an attorney, which along with a like decision in Oregon brings the number of states to three where the highest court has refused to grant doctors an avenue of recovery against attorneys. Another case is being appealed to the highest court in Illinois.

Courts have weighed the "chilling effect" that a countersuit would have against victims of malpractice seeking damages against the doctor's right to seek redress, Mr. Edelman said. They seem reluctant to change the law themselves, apparently waiting for state legislatures to establish the liability of lawyers for maliciously bringing malpractice actions against doctors.

The court of appeals decision leaves doctors whose reputations have been damaged by a baseless malpractice suit without a means of redress, complained Dr. Edward Siegel, deputy executive director of the New York State Medical Society. The only recourse available to a physician who has been victim of a malicious suit is to ask the state bar association to discipline the plaintiff's attorney, Dr. Siegel added.

While the Drago decision fails to close the door to attorneys bringing baseless suits against doctors, another court of appeals ruling could leave physicians open to additional liability actions.

In a five-to-two decision, the court said in another case that a doctor who fails to advise a pregnant patient that her child may be born abnormal can be required to pay for the cost of lifelong special care for such a child.

The decision involves two companion cases brought by the mothers of a 3 ½-year-old retarded girl suffering from Down's syndrome and a girl born with kidney disease who died at 2 ½.

Dolores Becker, the mother of the retarded child, claimed that she was not advised by her doctor that the risk of Down's syndrome increases with the age of the mother. She was not administered an amniocentesis test that would have determined whether the condition existed, she charged. Mrs. Becker was 37 when she became pregnant.

The other woman, Hetty Park, gave birth in 1969 to a child who died five hours after birth from polycystic kidney disease. Doctors advised her that the chances of a recurrence in a second child were "practically nil," but her next child was also afflicted with the kidney disease.

Both mothers claimed that had they been advised of the risks of bearing abnormal children, they would have sought abortions.

The rulings did not find the doctors liable. Both cases must still be litigated according to standard rules in negligence and medical malpractice cases in which liability is judged on accepted medical practice in an area.

However, Dr. Siegal of the state medical society said the decision will have an inflationary effect upon the practice of medicine because doctors will order tests to reduce their exposure to suits. In the New York area, an amniocentesis procedure costs between $300 and $350, he added.

But ordering the procedure could also expose a doctor to a malpractice suit since women who undergo the procedure have a slightly greater chance of miscarriage. Those who suffer complications from the test could sue their doctors for malpractice. ■

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New black brokers emerge: Career, consumer opportunity

By MARY ELLEN McKEE

CHICAGO—Ample opportunities exist for black people in the insurance industry, but convincing blacks of this is a problem, says James L. Chastain, head of a newly created insurance department at the predominantly black Howard University.

That only six black brokers hold Chartered Property & Casualty Underwriter designations and only seven local chapters nationwide of the Risk & Insurance Management Society have any black members support Mr. Chastain's claim that the insurance business, on the whole, is virgin territory for blacks.

But Mr. Chastain expects significant inroads to be made in 1979, considering the insurance curriculum at Howard, coupled with the formation of a new black-owned brokerage firm, a battle being waged by the largest black-owned insurance brokerage firm to double its premium volume in five years and the New York College of Insurance's continuation of its successful work-study program.

Mr. Chastain, formerly a professor in the insurance department at Drake University, made the switch to Howard University recently to fulfill the "urgent goal" of drawing more blacks into the insurance mainstream.

"Education is one the strongest ways to attract people into an industry," Mr. Chastain noted. Convincing students that the insurance industry is a viable profession will shape the educational directions at Howard."

Drawing black students into the insurance industry will shape educational directions of Howard University's insurance curriculum.

—James L. Chastain

Meanwhile, Robert Isaacson, manager of the new black-owned broking firm, Ebony International Brokerage Corp. in New York City, admits that the firm's staff will aggressively go after the commercial business of companies seeking to fulfill affirmative action goals, as well as "traditionally substandard business" in urban areas.

"It's not a crime to use color as a way to get one foot in the door of a company, merely a device to gain an opportunity," Mr. Isaacson said. "And Ebony brokers plan to use this device not only to get business off the ground, but also to establish the credibility of blacks in the brokerage business."

Brokers at Ebony, Mr. Isaacson emphasized, will not rely on their color to maintain the business. "We don't expect to be handed a book of business based on color alone, we just want the opportunity to provide sound and equitable insurance programs and service which is responsive to the needs of the urban communities," he added.

The idea to form Ebony International sprouted from a heated controversy during the annual meeting of the Society of Chartered Property & Casualty Underwriters in Detroit last fall, Mr. Isaacson said. At the meeting, several local groups from around the nation accused agents and brokers attending the meeting, and the insurance industry as a whole, of being totally unresponsive to the needs of minority groups. Members of these groups suggested the situation was due largely to the lack of minority group representation in the insurance community.

"Ebony is the direct end-result of those entreaties," Mr. Isaacson added.

E.G. Bowman Co. Inc. in New York City, the largest black-owned brokerage agency in the country, has built a business going after Fortune 500 accounts and at the same time responding to the needs of the people and businesses in the once-troubled Bedford-Stuyvesant area of Brooklyn.

Three things accounted for E.G. Bowman's successful entry into the insurance industry, says Ernesta Procope, founder and president of the black-owned agency. "First, we had the motivation and we knew where we wanted to go," Mrs. Procope said. "And then, we had to be assured of the cooperation and support of our insurance companies.

"It would not do us any good to go after and sell new accounts if

Continued on page 84

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Black brokers . . .

Continued from page 82

our companies would not write the coverage," Mrs. Procope said. "So we outlined our intentions and plans to the companies, and consequently the companies bent over backwards to help us make a transition from a strictly personal lines agency to a strong commercial lines agency once they realized we were serious brokers."

Acquiring the expertise needed to compete effectively for good accounts was the second prerequisite for the successful entry into the commercial market for E.G. Bowman, according to Mrs. Procope. "We satisfied this requirement by adding highly qualified and motivated people to the agency staff and contracting for the services of experts in various specialties," E.G. Bowman's president noted.

The broker's first business contacts for commercial accounts grew "out of our location in the inner city and our efforts to rehabilitate and preserve the Bedford-Stuyvesant area as a viable community," Mrs. Procope noted. One of the most important lessons a black broker or any broker must learn is to use every opportunity to present its program to a buyer, according to Mrs. Procope.

"My civic activities in the Bedford-Stuyvesant area brought me into contact with influential business people, and their exposure to me gave them an opportunity to evaluate my abilities and judge my performance," Mrs. Procope said. "I used these contacts outside my work to bring in commercial accounts for the agency," she added.

It was a slow process, Mrs. Procope admitted, but it opened very important doors for the company. "I found that once these corporate insurance buyers got used to the idea of a black woman broker, they were interested only in competence, dependability, integrity, economy and service," she said.

E.G. Bowman, which handles insurance programs for over 30 Fortune 500 companies to date, is also a pioneer in handling accounts in the Bedford-Stuyvesant area ranging from local brownstones, churches and a daycare center to a methadone treatment center.

At the core of her success—and she feels, the key to success for any other black brokers—is the belief that so-called "bad risks" can be profitable as long as their insurance programs are carefully designed and administered.

Finally, Mrs. Procope believes education is at the bottom of any successful career, but is vital for black brokers. She offers in-house classes for new personnel to familiarize them with all aspects of the insurance business and also to give her an opportunity to test their talents and abilities. After completion of these classes, all employes are encouraged to augment the knowledge they receive on the job with classes from local colleges or the College of Insurance.

Once corporate insurance buyers got use to the idea of a black woman broker, they were interested only in the level of competence, dependability, integrity and service in my work.

—Ernesta Procope

Shirley L. Clark, manager of new commercial accounts for E.G. Bowman, followed Mrs. Procope's suggestion and is the first black woman in the country to earn the CPCU designation. And James L. Drake, vp of the agency, is one of five black men in the nation to hold the designation.

"We're still climbing the ladder," Mrs. Procope added. "You should never be satisfied with being good—you have to aim to be the best."

Mrs. Procope intends to reach that goal with a new sales campaign that was launched last fall targeting Fortune 500 companies as prospects. The program, says vp James L. Drake, is designed to double the annual premium volume of the company. ■

Other state regulators monitor N.Y. exchange

JEFFERSON CITY, Mo.—The New York Insurance Exchange could come under the scrutiny of a National Association of Insurance Commissioners regulatory subcommittee that is looking into adequacy of present regulation of nonadmitted markets.

Missouri insurance director Gerald B. Buxton, chairman of the NAIC regulatory information subcommittee, said he is monitoring development of the exchange to see if any action should be taken by the regulator's group.

A task force of Mr. Buxton's subcommittee is studying the adequacy of current laws governing non-admitted markets. Any guidelines produced by that task force should consider the role of the exchange, Mr. Buxton believes. California insurance commissioner Wesley J. Kinder, who chairs the task force, could not be reached for comment.

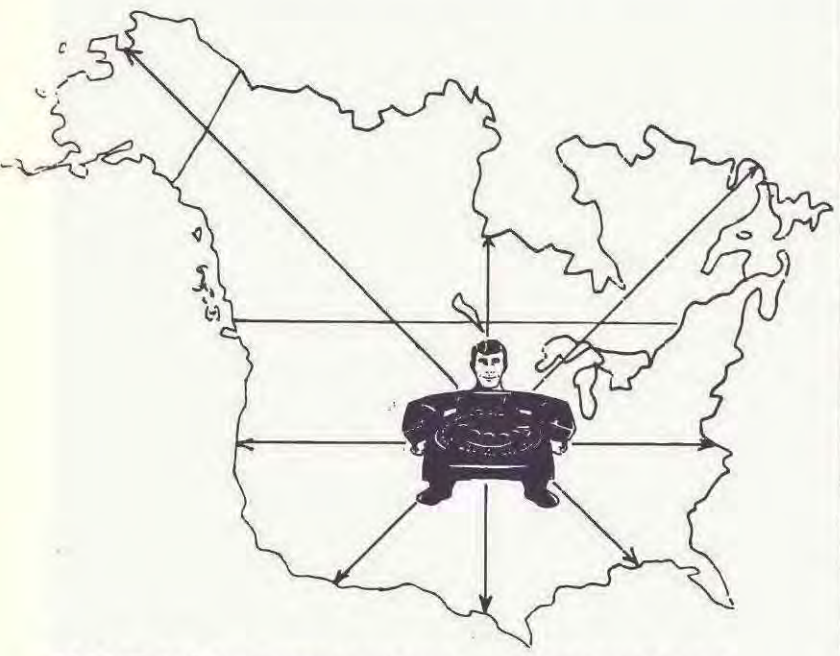
The New York Insurance Exchange, which is expected to become a legal entity by mid-1979 and begin writing business by the end of the year, will be an unregulated market writing reinsurance and insurance on foreign risks and risks rejected by the state's free trade zone for insurance companies.

The free trade zone was established by the same legislation as the insurance exchange and allows specially licensed companies to write high premium, hard-to-place, unusual risks without prior approval of the insurance department on rate and form.

At the recent NAIC meeting in Las Vegas, Mr. Buxton questioned how the exchange will report to other states. "The rest of us will have to look to the New York department for information," he complained.

However, Mr. Buxton told *Business Insurance*, "it doesn't mean I'm opposed to this type of thing."

New York insurance superintendent Albert B. Lewis, who was not at the Las Vegas meeting, said he would not be surprised if the task force proposes special regulations regarding the exchange. He noted, however, that department representatives answered most criticisms of the exchange raised at the Las Vegas meeting. ■



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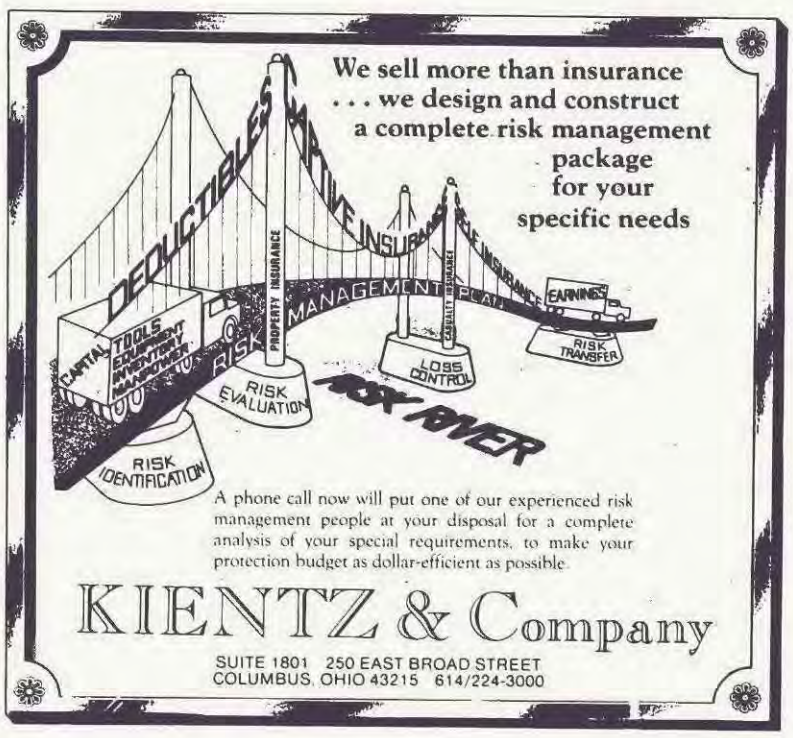

Football helmet manufacturer wins in product suit

By JERRY GEISEL

BOSTON—Rawlings, the big sporting goods manufacturer, successfully defended a personal injury case involving its football helmet, which had emerged as yet another horror story in the annals of product liability litigation.

The case assumed notoriety not only due to the large amount of damages sought—$6 million—but also because the suit was filed against the manufacturer even though the plaintiff lacked hard evidence that the injured high school football player was wearing a Rawlings helmet at the time of the accident.

A spokesman for ATO Inc., Rawlings' parent firm, regards the firm's victory in Boston as critical to the future of the football helmet industry.

Football helmet manufacturers have been the targets of an unusually high number of product liability suits since the early 1970s. Riddell, the nation's leading helmet manufacturer, lost a spectacular personal injury suit in 1975 when a Miami jury awarded $5.3 million to a high school football player who was left paralyzed by a football game accident. That case was later settled for an undisclosed, but lower, amount.

Riddell later successfully defended a $2.5 million suit filed in Phoenix, Ariz., but it is now facing an $11.5 million suit filed in U.S. district court in Baltimore as well as other suits filed in other states.

The Boston case involves a 1968 accident in which 17-year-old John Horgan, a junior at St. Peters School in Gloucester, Mass., was injured while attempting to tackle the opposing team's halfback.

While making the diving tackle, Mr. Horgan crashed into the halfback, his helmet striking his opponent's thigh. Mr. Horgan's spinal system was damaged in the collision, leaving him permanently paralyzed below his neck.

A suit was not filed, however, until 1974, six years after the accident and only one month before the statute of limitations on filing suit was to expire.

Plaintiff attorney Harry Philo of Detroit said the Horgan family waited so long to file suit because it didn't occur to them that it might have been the inadequacy of the football helmet that caused the injury.

"You would have had to be a top mechanical engineer skilled in the field of bio-mechanics to understand that it was inadequacy of the helmet as an energy managing system that caused the boy's injury," Mr. Philo said. "You can't expect a working class family to recognize liability that even the football establishment will not admit to today."

The catalyst for the suit was a conversation John Horgan's mother had with another woman while having her hair styled in a beauty shop.

The woman told Mrs. Horgan that one of her children had been injured playing lacrosse and that a suit had been filed. The woman suggested that Mrs. Horgan contact her attorneys concerning the possibility of filing suit regarding her son's football accident.

Mrs. Horgan took her advice and retained Boston attorneys Philip Crowe and Ralph Sbrougna. Mr. Philo joined the plaintiffs attorneys just before the case went to trial.

Before the Horgan suit was filed, the plaintiffs attorneys attempted to find the helmet John Horgan was wearing on the day of the accident. The search was complicated by the fact that the school was closed several years after the accident. The helmet could not be located.

Mrs. Horgan contacted former teammates and friends of her son to see if they could supply the kind of helmet John Horgan was wearing at the time of the accident.

Eventually, someone brought a battered old Rawlings HC-5 football helmet to the Horgan house. Young Mr. Horgan thought the HC-5 was the same kind of helmet that he wore prior to the accident. As a result, the Horgans filed suit in 1974 against Rawlings in U.S. district court in Boston.

The Horgans contended that the Rawlings helmet was improperly designed because it lacked sufficient padding to protect the head and neck from shock of a collision.

During the 16-day trial, plaintiff attorneys were unable to produce concrete evidence that young Mr. Horgan was wearing the Rawlings HC-5 helmet. They said all invoices relating to St. Peters' athletic equipment purchases were destroyed or lost after the school had been closed.

However, defense attorneys were able to locate school records that revealed that St. Peters purchased some Rawlings HC-5 helmets in 1965 and a different Rawlings model in 1966. In 1967, the school also made a major purchase of football equipment, buying 36 Nakoda helmets.

During the trial, the St. Peters' coach testified that when the new equipment arrived in 1967, the old football helmets were discarded.

It took the jury about four hours to absolve Rawlings from liability. The jury voted to acquit Rawlings because they decided the Horgan's attorneys failed to prove that Rawlings manufactured the helmet worn in the accident, according to Joseph Regan, one of Rawlings' defense attorneys.

The jury voted in favor of Rawlings because it agreed with the Rawlings expert witnesses who testified at the trial that the helmet was properly designed, Mr. Regan added.

One legal source close to the case criticized the Horgan's attorneys for not conducting a more rigorous search to locate the school's athletic purchase equipment records before "embarking on a very serious case."

Mr. Regan could not estimate what it cost Rawlings to defend the suit since the legal bills have not been tabulated yet. But he noted that the costs of an unfavorable verdict far overshadow the legal expenses associated with winning a case.

In the Horgan case, Rawlings liability protection exceeded $6 million with coverages supplied by three separate policies underwritten by The Travelers and CNA insurance companies. ■

Insurers fear losses in 1980

NEW YORK—Insurers current profitable underwriting results are being eroded by the failure to keep premiums in line with rising costs, Insurance Services Office president Daniel J. McNamara warns.

While the insurance industry should earn an underwriting profit this year, he predicts black ink may disappear in 1980. ■

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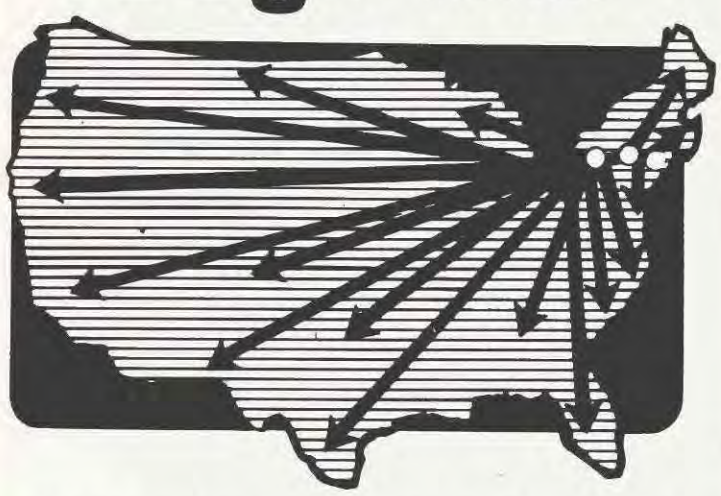

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Carnation ruling . . .

Continued from page 1

Carnation to provide capitalization of Three Flowers up to $3 million if needed to cover losses over the $120,000 initial capitalization.

In November 1972, the tax year at issue, Carnation paid American Home $1.95 million in annual property premiums. The next month, American Home paid $1.76 million to Three Flowers under the reinsurance agreement, transferring 90% of the risk to Three Flowers. On its 1972 tax return, Carnation claimed as a business expense deduction the full premium paid to American Home and reported $1.6 million earned by Three Flowers as "Subpart F income," earned on the foreign insurance of U.S. risks. (A company's foreign source income allows it to take advantage of a foreign tax credit provision of the Internal Revenue Code.)

Upon audit, the IRS challenged $1.76 million of the $1.95 million deduction by Carnation, and decreased Carnation's Subpart F income attributed to Three Flowers to $50,616. Carnation petitioned the tax court in 1976.

Tax court judge William Goffe affirmed the IRS's action, basing his decision on a 1941 Supreme Court ruling in a case involving an intricate scheme using insurance purchases to avoid estate taxes (Halvering *v.* LeGierse). The Supreme Court had noted that transfer of risk was essential to an insurance transaction and that two transactions could be considered together to determine if risk shifting had occurred.

No risk shifting

Applying these principles to the Carnation case, the judge found there was no risk shifting, therefore no insurance transaction, for the portion of risk ceded by American Home to Three Flowers. The IRS correctly interpreted the tax consequences to Carnation of dealing with its captive insurer, the judge said.

"The loss suffered by Carnation would ultimately be borne 90% by Three Flowers and 10% by American Home. The agreement to purchase additional shares of Three Flowers by Carnation bound Carnation to an investment risk that was directly tied to the loss payment fortunes of Three Flowers, which in turn was wholly contingent upon the amount of loss suffered by Carnation," the judge said.

"The agreement by Three Flowers to reinsure Carnation's risk and the agreement by Carnation to capitalize Three Flowers up to $3 million on demand counteracted each other," the judge found. "Taken together, these two arrangements are void of insurance risk."

The judge, like the IRS, allowed as insurance only the 10% portion of Carnation's property risk retained by American Home.

Ford Motor Co. fared much better in its out-of-court settlement with the IRS, because in effect it is simply being charged with earning an insurance broker's 5% commission on the $5.7 million in premiums. This means Ford will ultimately pay "a whole lot less" in back taxes than it would have based on the IRS's original challenge, *BI's* source said.

Analyzing the settlement as described to her by *BI*, Marianne Burge, a partner with Price Waterhouse in New York, observed, "It's understandable the IRS might approach a settlement in this way, considering that the foreign affiliates wouldn't have insured with Transcon without guidance from the parent to do so."

However, Ms. Burge recalled a former case involving First Security Bank of Utah and credit life insurance placed with an affiliate of the bank in which the court held the IRS "could not impute an insurance commission to the bank because the bank was not an authorized commission agent."

Ford's argument

Other companies insuring corporate risks with a captive insurer should not expect to strike a bargain similar to Ford's with the IRS should they be challenged, cautioned a source close to the case. The facts of the case are unique to Ford, he believes.

"It doesn't set any precedent," agreed Ms. Burge. "But it does have a psychological effect because it suggests the IRS, having selected this case to litigate, consequently decided not to go through with it."

Ford was considered by observers to have a particularly strong case. The transactions with its captive involved only foreign money: Premiums were paid by Ford's foreign affiliates to a Ford subsidiary in Bermuda, known then as Trans-Global Insurance Ltd., now Transcon Ltd.

In addition, Transcon was operated as a bona fide insurance company, not a file-folder firm to skim profits from affiliates, Ford argued.

More cases

Final papers filed last month in U.S. Tax Court, officially settling Ford's case against the IRS, didn't reveal details of the settlement as disclosed to *BI*. The two-page document, dated Dec. 11, merely states that Ford Motor Co. and the IRS agree that Ford's taxable income for 1970 is $737.7 million. That's $8.2 million more than Ford had originally admitted for the year, but $6.8 million less than the IRS had calculated in auditing the 1970 return.

Still at issue in the 1970 return, however, is the effect of foreign tax credits from 1972 on the 1970 return. Therefore, Ford's total tax liability for 1970 is still undetermined.

The settlement had been agreed to in principal over a year ago, but it was not made official until the papers were filed with the tax court last month. Nor were the details of the settlement known to others.

Ford tax returns for years after 1970 are also being challenged by the IRS, including further IRS objection to Ford's accounting for transactions involving Transcon, *BI* learned. These disputes over later years have not reached the court yet, but there is now little hope in light of the Carnation decision that the pending disputes will also be settled out of court, according to *BI's* source.

No one expects resolution of these two cases to be the final word on the tax ramifications of firms using captive insurers.

Already pending in tax court are two cases, brought by Ingram Corp. and Toyomenka (U.S.A.), challenging IRS's treatment of their transactions with offshore captive insurers. In addition, Ocean Drilling & Exploration Co. and Mobil Oil Corp. have filed petitions in the court of claims for refunds of taxes paid that include captive-related issues. ■

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Letters . . .

Continued from page 10

overall health coverage.

Dennis L. Peterson
Marketing coordinator, Delta Dental Plan of Wisconsin Inc., Stevens Point, Wisc.

Our sample may have been skewed in favor of Delta's competition, because Delta Dental received only two mentions by Benefit Board panelists using the firm as dental carriers.

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Allstate blitz . . .

Continued from page 1

Property & Casualty.

Northbrook Property & Casualty and its six branch offices will operate separately from Northbrook Excess & Surplus Lines Insurance Co., an existing Allstate subsidiary formerly named Northbrook Insurance Co. Northbrook Excess & Surplus Lines is the largest U.S. surplus lines underwriter with about $300 million earned premiums in 1978.

Both firms, located in Northbrook, Ill. where Allstate is headquartered, are, "distinct entities," according to Mr. Leibold. "There will be no change at all in the operation of the commercial insurance divison and it will in no way impact the Northbrook Excess & Surplus Lines Company."

Company officials declined to discuss premium projections for the new market effort and said they have not set specific goals on how much of the market they hope to acquire or how quickly. "But our intent is to become a major carrier," said Mr. Leibold.

The effort will actually be a major industry blitz utilizing a fleet of branch offices with the company aiming to propel itself into the top 10 of commercial carriers by the mid-1980s, sources close to the company say.

Although Northbrook Property & Casualty will aggressively seek to establish itself as a significant factor in the commercial insurance market, it is not seeking any particular ranking among commercial carriers, Mr. Leibold maintains. "Our ultimate objective is to become a major carrier but no time frame has been set, because as we continue to grow, other companies will continue to grow as well."

Lags commercially

Allstate, although a perennial giant in personal lines insurance, has lagged behind many companies in the commercial marketplace, which Mr. Leibold said could be worth $44 billion in premiums industry-wide in 1979. Allstate was 21st on Best's list of commercial groups in 1977, but is reliably reported to be aiming for a spot among the top 10 commercial carriers.

It is projected that Allstate will net $250 million in commercial premiums for 1978, he said. This differs from the Best's 1977 figure because it is solely commercial business for Allstate, while Best's figure is for entire groups and includes some personal lines volume.

"We were not satisfied with our growth in commercial property/casualty so Allstate made a commitment to achieve increasing penetration in the commercial lines market and this commitment is backed up by all of our resources," Mr. Leibold said.

The new Northbrook firm will offer a, "broad range and good cross section of products while aiming at medium to large size manufacturers, retailers and service companies, generating an average of about $3,000 to $150,000 yearly in premiums.

Northbrook Property & Casualty will place heavy emphasis on the sale of multi-peril packages, but will offer most lines of commercial coverage such as auto, workers compensation, general liability and fire and allied lines. It will probably steer clear of such risks as ocean marine and oil drilling, said Mr. Leibold.

Allstate has been planning for about three years to compete for commercial risks. Mr. Leibold spent a good part of 1978 helping set up Northbrook Property & Casualty, which was previously Allstate's fire insurance company, along with planning the six nationwide field offices through which the independent agents will operate. "Considerable effort during 1978 was devoted toward strategic and operating plans," he said.

Allstate first created a commercial insurance division last September, naming Mr. Leibold as its head. Mr. Leibold joined Allstate in January 1978 from CNA Insurance Cos. where he was senior vp and director of marketing.

The first of the Northbrook Property & Casualty branches will open this month in Rolling Meadows, Ill., a Chicago suburb. It will be followed by five other field offices that will begin operating at unspecified times during the year.

No agents have been selected yet for appointments to the Rolling Meadows office, but the process will probably begin later this month.

The other branch offices will be "geographically dispersed" near urban areas, but Mr. Leibold declined to say where. The branches will be responsible for underwriting and marketing business.

Branches planned

"It's fair to say" that branches will be located in the same areas as four of Allstate's commercial regional offices, which are in Atlanta, Los Angeles, Long Island, N.Y. and Rolling Meadows, Mr. Leibold admitted.

Northbrook Property & Casualty is licensed to operate in all states as well as the District of Columbia, with the exception of Texas where approval is expected shortly.

Allstate's regional centers will back up the branch offices, handling claims processing and service, accounting, collections, pol-

Continued on following page

Top 10 commercial lines groups*

Rank & Company	1977 premium volume (in billions of dollars)
1) Aetna	$1.90
2) Travelers	$1.71
3) Fireman's Fund	$1.54
4) Hartford Fire	$1.48
5) Liberty Mutual	$1.42
6) INA	$1.28
7) Continental	$1.24
8) USF&G	$1.12
9) Crum & Forster	$1.10
10) American International	$1.09

Allstate ranks 21st with $460 million in premiums

*Includes p/c premiums and some personal lines.

Source: Best's Executive Data Service

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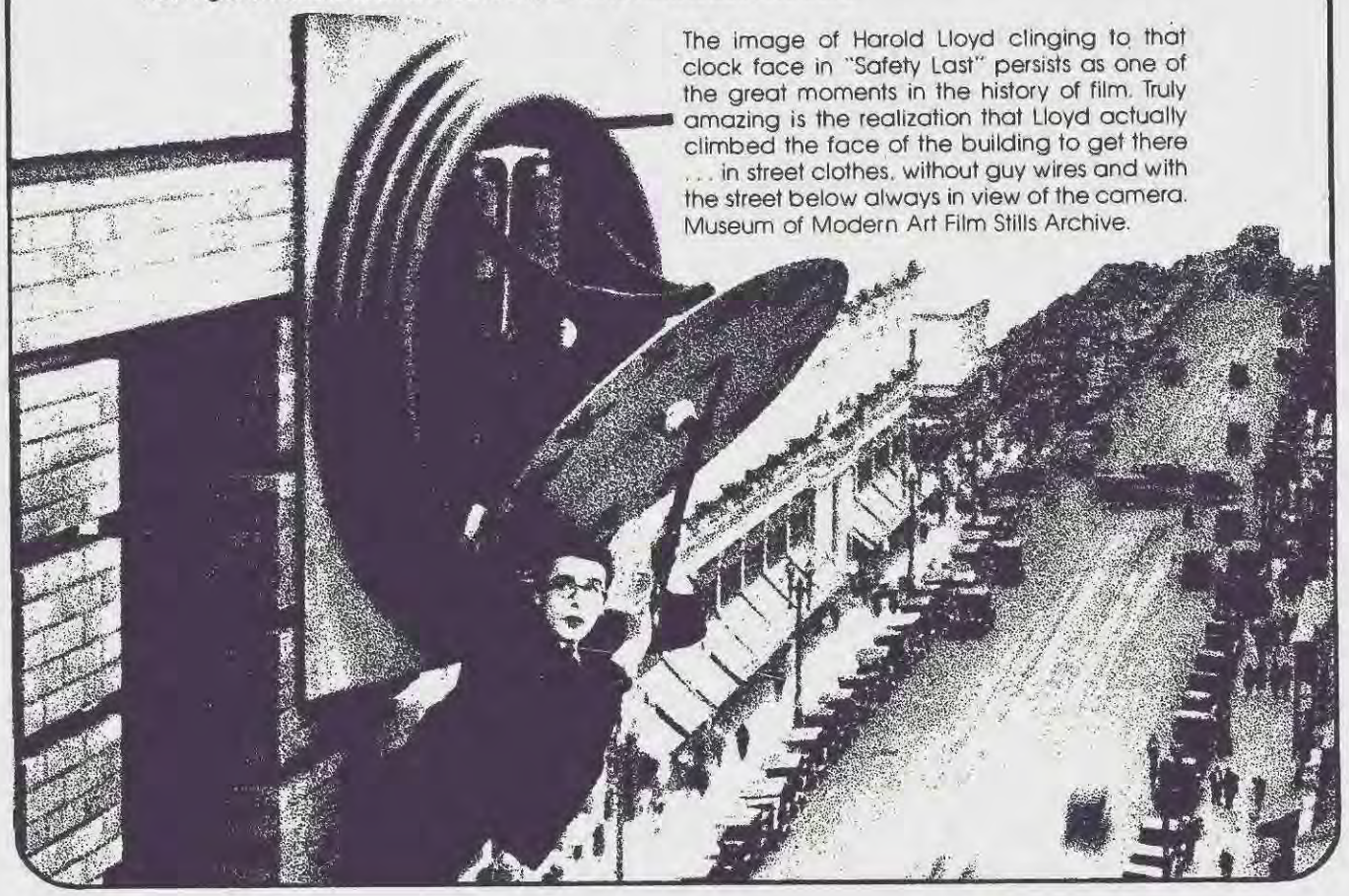

The image of Harold Lloyd clinging to that clock face in "Safety Last" persists as one of the great moments in the history of film. Truly amazing is the realization that Lloyd actually climbed the face of the building to get there . . . in street clothes, without guy wires and with the street below always in view of the camera. Museum of Modern Art Film Stills Archive.

Allstate blitz . . .

Continued from preceding page
icy issuance and loss control for policies directly written by Allstate as well as for Northbrook Property & Casualty clients.

"We have also planned to make available a new commercial lines processing system utilizing computer equipment so processing will be on a centralized basis," said Mr. Leibold. "The network will run through the regional offices and down to the branches so we will be able to tie them together."

"The branches will be strategically located to serve major concentrations of commercial business in urban areas. Each office will be staffed with good, solid underwriting talent as well as agency representatives who will bring a high degree of underwriting content to their jobs," Mr. Leibold said.

Agents interested

Northbrook will seek agents experienced in commercial insurance and will develop an orientation program for agents commissioned later, he said. Agents will be allowed to write business for other insurers while selling Northbrook Property & Casualty policies, he said.

Requests for information about agent appointments have come from all over the country. "There's been a high level of interest in what we're doing, especially from independent agents. And we've had a lot of special requests about when we can take agent appointments," Mr. Leibold said.

Explaining why corporate officials decided to commission independent agents rather than hire them as part of Allstate's regular sales staff, Mr. Leibold said all possible avenues were explored. Because independents already control 80% of the commercial marketplace, that was the "best way to go," he said.

"Allstate has been successful in working with independent agents on personal lines and it was recognized that the independent agency force controls the commercial marketplace and it seemed to be the best way to go where the market is," he explained. "We determined the most desirable way to get that market penetration would be to work with the independent agency situation."

Analysts and industry observers say Allstate probably won't be able to displace any of the top commercial insurers in the near future. But indicate they consider the company aggressive enough that its entry into the commercial market will be successful.

"They are a large, aggressive company and I assume they will try to become a major factor eventually," said Bob Brian of Hartford-based Conning Co., an investment research firm. "I'd be surprised if the effort were small."

Allstate's plans will benefit the insurance and investment communities, he added. "Their entrance into commercial lines areas will be a favorable development for the investment field and will provide new avenues of growth and additional capital to the insurance market in those lines."

Competitive market

Allstate will face stiff competition because the commercial lines market is already "rapidly becoming more competitive," observed Harvey Bundy, a securities analyst for William Blair & Co. in Chicago. "It will make the market much more competitive than it's been. Allstate is one additional factor and State Farm is doing the same thing," he said.

(State Farm has been trying to increase its commercial lines business over the last three to five years, especially in multi-peril packages, but no major restructuring is planned for this year to attract new commercial risks, a company spokesman said.)

The competition could lead to a situation similar to one that existed in the insurance industry in 1974, when decreasing rates caused companies to sustain higher loss ratios and insufficient premiums to cover them, Mr. Bundy suggested.

Some independent agents that do not deal with Northbrook Property & Casualty will probably fear losing business, Mr. Bundy predicted. But most will probably be able to sustain themselves in the marketplace even though "they'll have to work a little harder over the next couple of years," he said. ■

AIG creates new division

NEW YORK—American Home Assurance Co. has organized a "Foreign American" division that will specialize in insuring the United States exposure of foreign-based corporations. The division will write property, workers compensation, comprehensive, general and automobile liability and umbrella and excess coverages.

American Home's New York headquarters and the foreign offices of American International Underwriters will handle the business. Both firms are subsidiaries of American International Group. ■

Flood losses

Insured losses caused by flooding and wind storms that swept through portions of Kentucky, Florida and West Virginia last month are estimated at $2 million, according to the American Insurance Assn.

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Fewer improvements . . .

Continued from page 1

Hancock Mutual Life Insurance Co. reported slightly higher business for the fourth quarter of 1978 as compared with the previous year.

Many plan revisions implemented by his firm's clients, however, were the result of negotiated contracts or were decided upon prior to the implementation of the Carter guidelines, he added.

Although a slowdown in benefit improvements has yet to be felt at Equitable Life, a fall off is expected in the months ahead, said senior vp John Goddard. "Improving benefits is deferrable. We saw that the last time during the Nixon administration anti-inflation drive. The (Carter) guidelines will dampen the ability of employers to buy and insurers to sell benefit improvements."

Under the wage and price guidelines instituted by the administration, the combined increased cost resulting from improvements in wages and benefits is limited to 7%. The amended rules exclude increases over 7% in the cost of maintaining current health benefits and the cost of providing federally mandated benefits, such as disability benefits to pregnant employes and complying with the Age Discrimination in Employment Act (ADEA).

Prior to those amendments, there was an upswing in the number of accounts going to the market as a result of rate increases, noted Unionmutual's Mr. Hepburn. "Normally, the smart buyer goes along with rate increases, but the type of people who normally would not market their business started doing so," he said.

Had the guidelines not been amended, there probably would have been increased pressure on employers to find "alternative solutions," such as another insurer, added Metropolitan's Mr. Briggs.

Federal burdens

Insurers see the addition of new federally mandated benefits affecting their businesses to differing degrees. John Hancock's Mr. Thomas expects the mandated benefits to be a major source of new business with equal benefits for pregnancy disability offsetting the negative impact of the wage and price guidelines.

Regardless of whether the administration had introduced its anti-inflation measures, employers would have been hard-pressed to implement new benefit improvements because of the financial strain of paying the cost of maternity disability as illness, according to John Turner, senior vp at Northwestern National Life Insurance Co.

However, Prudential group marketing vp Dennis Walsh expects the pregnancy benefit law to have greater impact upon small accounts. Large accounts, which comprise the greater part of the Prudential's business, already provide pregnancy benefits equal to or close to the federal standard.

The Department of Labor regulations on age discrimination in benefits are also expected to affect the cost of providing benefits, particularly for long term disability, noted Mr. Hepburn.

Preliminary DOL rules calling for disabled workers over age 60 to receive LTD benefits for five years or until age 70 would raise rates 12% to 15%. But, should all disabled workers be eligible for benefits until age 70, rates for LTD would increase by 18% to 22%, he said.

Using old tricks

Metropolitan's Mr. Briggs discounted the impact of the cost of providing benefits to older workers. Increased insurance costs would probably be offset by savings in pension costs, he said.

Insurers' marketing strategies will likely reject the impact reductions in new business coming from benefit improvements. Companies that have been aggressively seeking new accounts are not as likely to be hurt as firms that have been sitting back and depending on plan revisions, said one West Coast insurance executive.

"All you can do is try to steal business away by offering better service, cash flow advantages and other funding devices," said Jae Wittlich, vp with CNA's Continental Assurance Co. "As far as coming up with something unique, there is very little that is unique."

However, Unionmutual's Mr. Hepburn predicts insurers will introduce new products, such as sophisticated life insurance and long term disability programs, to offset some of the loss of new business. Such programs could offer more liberal contracts to groups with better experience and provide benefits relating to specific needs, such as using a survivor concept instead of a death benefit, he said.

Payroll deductions

The anti-inflation guidelines will also make payroll deduction plans more attractive to employers, said Northwestern National's Mr. Turner. A number of employers have already rearranged their benefit programs to make employes pick up the cost of long term disability coverage, he remarked.

Payroll deduction benefit plans could be attractive for small accounts, but they are not likely to account for a large part of new business, said Equitable's Mr. Goddard. They do offer the advantage of enabling the employer to pick up the cost for them at a later date, providing a visible benefit improvement, he added.

While there has been a trend toward payroll deduction benefits as a way for employes to buy insurance at a lower cost, employes have also been affected by inflation, and "to the extent that they're squeezed by inflation, they'll be reluctant to increase their purchase of insurance," suggested Metropolitan's Mr. Briggs.

Despite the negative impact the Carter wage and price guidelines are expected to have upon the benefit business, insurers are not critical of the President's moves. Mr. Briggs said the insurance industry should support the President's efforts, particularly in helping to control health care costs.

"The most important thing is to get this inflation thing under control," he said. "Until we do that, we won't have a normal marketplace.

But, CNA's Mr. Wittlich pointed out that the wage and price guidelines could delay implementation of cost containment features which, for the first year or two, produce costs greater than anticipated savings. ■

OPIC resumes in Bangladesh

WASHINGTON—The Overseas Private Investment Corp. (OPIC) has resumed its insurance and finance programs for U.S. companies that want to begin development projects in the Peoples Republic of Bangladesh.

Insurance and finance programs had been stopped in 1975 because of technical disagreements between OPIC and Bangladesh.

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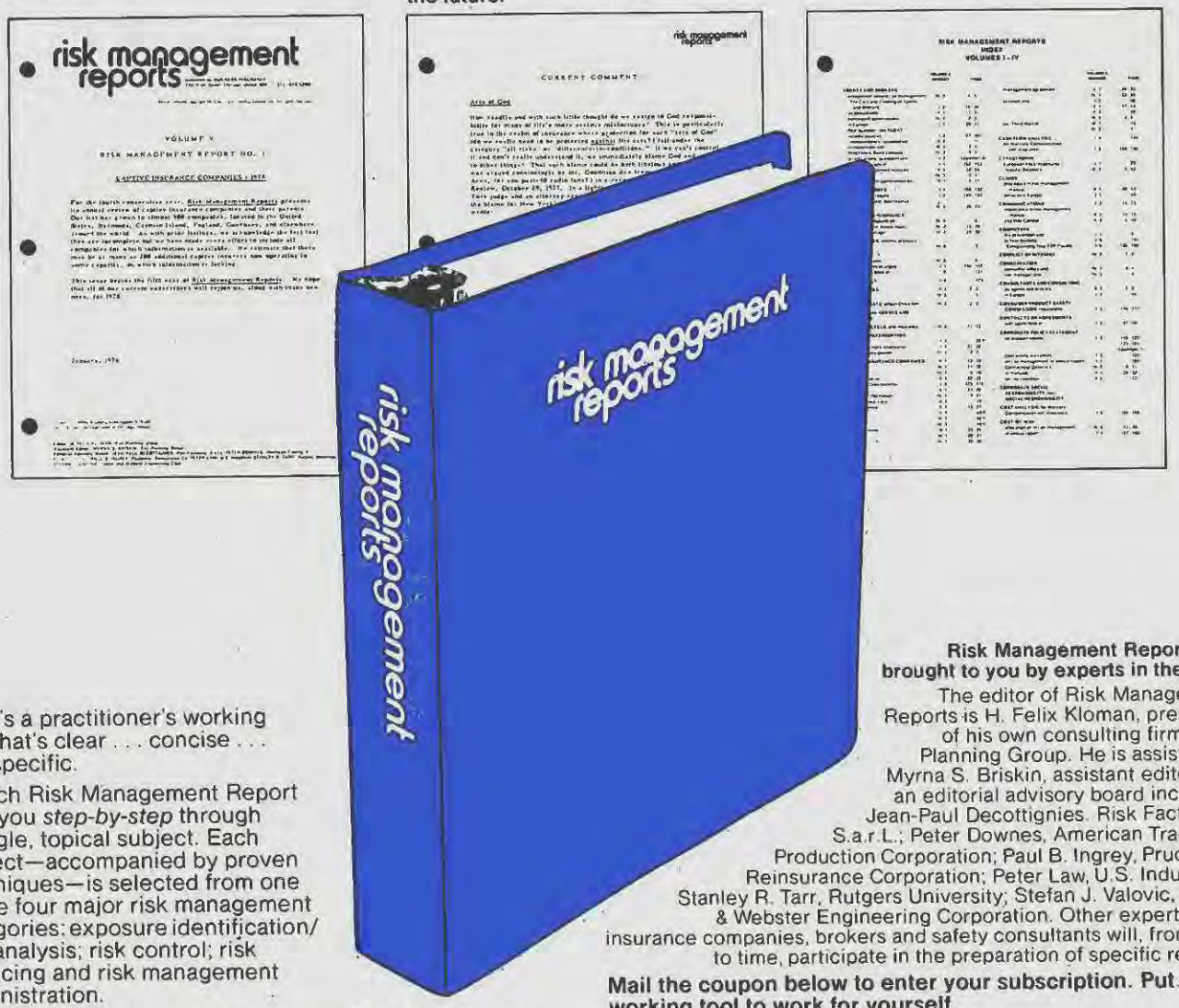

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Schoenewolf in Dodd's place at United Brands

Two corporate changes of headquarters set off a chain reaction of personnel moves that reached Chicago from Boston and New York, as Singer Co. relocated to Stamford, Conn., from New York City and United Brands Co. moved back to New York after five years in Boston.

Donald L. Schoenewolf, 35, moved from Singer as director of risk management to United Brands as risk manager so he could stay in the New York area. The opening at United Brands was created when **Jed Dodd** decided not to relocate to New York from Boston and look for a financial position in Boston.

Meanwhile, Singer's insurance manager of six years, **David O. Bullock,** 38, was promoted to director of risk management and insurance at Singer to fill Mr. Schoenewolf's former position. **Nicholas N. DeRosa,** 31, was hired from Chicago Pneumatic Tool Co. where he'd been for five years, to fill Mr. Bullock's former position at Singer.

Ironically, Mr. DeRosa originally joined Chicago Pneumatic to replace Mr. Bullock when Mr. Bullock moved to the insurance manager position at Singer. Chicago Pneumatic's new insurance manager is **William Benedict,** recently of the Factory Mutual System.

In the shuffle, Singer also lost **Frank Koerner,** 28, as property insurance administrator, who went to United Brands as domestic insurance manager. Singer plans to phase out the property insurance position by consolidating it with casualty insurance management and promoting a Singer financial analyst to the vacant spot.

* * *

James F. Coffey, 40, who single handedly directs risk management and insurance at Lincoln First Banks Inc. in Rochester, N.Y., has been promoted to vp, risk and insurance manager from assistant vp, his title since 1976. Mr. Coffey is backed by insurance personnel in Lincoln's 140 banking offices. He reports to Terry D. Giles, vp and treasurer. Prior to joining Lincoln in 1973 as risk and insurance manager, Mr. Coffey was insurance manager at Marine Midland Banks Inc. His 20 years insurance experience also includes work at Continental Insurance Cos. and Merchants Mutual Insurance Co.

* * *

Thomas Sheehan, 40, has been hired as corporate risk manager for National Medical Care in Boston, reporting to treasurer David G. Lubrano. Mr. Sheehan replaces **Diana Petersen,** 27, who is on maternity leave but working part-time for National Medical Care. Mr. Sheehan previously was insurance administrator for the Quincy Shipbuilding division of General Dynamics in Quincy, Mass. His replacement there is **Robert A. Graham,** 40, who sold his agency, Sequoia Insurance, in Cape Cod, Mass.

* * *

New to the headquarters of General Dynamics Corp. in St. Louis is **Wesley A. Armstrong,** 51, as corporate director of insurance, reporting to treasurer Wayne Wells. Mr. Armstrong replaces **Robert Bussey,** who retired. Previously, Mr. Armstrong was director of insurance and employe benefits at General Host Corp. in Stamford, Conn., for two years. **Anne Bates Linden** has been hired as director of property and casualty insurance at General Host, reporting to Morris Kline, vp of corporate staff services in Phoenix.

Tiboni

* * *

Brian J. Tiboni, 33, is the new director of insurance services with the Hospital Assn. of Pennsylvania. Formerly he was associate director of health policy and operations with the Pennsylvania insurance department for seven years. In his new position, he is responsible for developing and administering insurance programs for member institutions, monitoring and evaluating insurance-related legislation and regulations and advising on health maintenance organizations and employe benefit programs. The association presently offers eight group insurance programs to member institutions. The programs include: comprehensive general and professional liability; directors and officers liability; long term disability; a tax sheltered annuity plan; life, accident, death and dismemberment; dental; volunteer workers accident insurance and business guard, a property insurance.

* * *

Raymond C. Olsen, 36, has joined Penn-Dixie Industries Inc. in New York City as director of risk management, a new position created by consolication. Mr. Olsen reports to treasurer John Manning. Previously, Mr. Olsen was manager of loss prevention at Union Camp Corp. in Wayne, N.J. No replacement has been hired.

* * *

David Fleming is the new risk manager for the city of Portland, Ore. with an approximate salary of $28,080. He reports to financial officer Ronald Lappi and replaces **Michael Lewis,** who joined Tromp & McKinley, an insurance agency in Eugene. Mr. Fleming, who previously was risk manager for the city of Salem, is being temporarily replaced by **Ronald R. Hutchinson,** 34. Mr. Hutchinson has been with the city for 1 ½ years as a field safety representative and hopes to be promoted to the management spot. He has also worked for the city of Phoenix.

* * *

Charles E. Wilson, 42, has joined Ball Corp. in Muncie, Ind., as manager of corporate risk, reporting to treasurer Leon Grandcolas. Mr. Wilson replaces **John Stephenson,** who retired. Previously, Mr. Wilson was an account representative for Allendale Insurance Co. in Cincinnati.

* * *

At Westinghouse Electric Corp. in Pittsburgh, **Michael Bryant** has been promoted to director of insurance from manager of insurance, replacing Richard P. Ackerman, who joined R.J. Reynolds Industries Inc. in Winston-Salem, as reported. **William G. Kalb,** 24, has joined Westinghouse as an insurance assistant. He previously was insurance administrator for Brockway Glass Co. in Brockway, Pa., and has been replaced by **Anthony Joseph Ten-Barge,** 28. Mr. Ten-Barge was an insurance auditor for Travelers Insurance Co. in Washington, D.C.

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In Burlingame, Calif., The Gap, a casual-apparel retailer has formed a risk management department and named **Ginny Talucci,** 32, CPCU, risk and insurance manager to head it. Ms.Talucci had been a broker with the San Francisco firm of Kahn & Nippert. At The Gap she reports to the senior vp, finance. The retailing firm has 359 stores in 39 states.

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In Boston, Mass., **Diane Kenny** was named risk manager, a newly created position, for the H.P. Hood Dairy Co. She was assistant risk manager at Harvard University in Cambridge, Mass. Named to replace her there was **Annemarie Esposito,** formerly assistant manager at Marsh & McLennan.

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Richard J. Barquist, 31, has joined U.S. Industries Inc. as insurance manager for the industrial equipment and production groups, reporting to S. Peter Law, vp of corporate services. Mr. Barquist is responsible for casualty/property and group insurance, workers compensation and loss prevention for the industrial division based in Oak Brook, Ill. He replaces **Donald Lange,** who joined Hyram Walker Corp. in Canada. Previously, Mr. Barquist was an insurance analyst with Pullman Inc. in Chicago. Pullman has not named a replacement.

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We'd like to report on staff changes in your risk management or employe benefits department. Just drop a note to Rebecca A. Fannin, Business Insurance, 708 Third Ave., N.Y., N.Y. 10017 or call 212-986-5050. We'd also like to receive pictures of those involved.

OSHA asks for court review

WASHINGTON—The federal government has asked the Supreme Court to review a lower court ruling that struck down the Occupational Safety and Health Administration's worker exposure standard on benzene, a chemical linked to cancer.

The action represents OSHA's attempt to reverse an October U.S. Court of Appeals ruling in New Orleans which found that OSHA failed to take into account cost-benefit factors in deciding its limits for worker exposure to benzene. Further, the appeals court said the section of the standard barring skin contact with liquid benzene was based on outdated and inclusive data.

OSHA's standard requires employers to limit employe exposure to one part benzene per million parts of air over an eight-hour period. The current exposure level is 10 parts per million parts of air.

The Labor Department says the new standard would affect about 600,000 workers at 150,000 worksites. ■

armr

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BALANCE SHEET — JUNE 30, 1978 [in U.S. dollars]

ASSETS	
Certificates of deposit	$10,165,964
Cash and time deposit	32,544
Accrued interest receivable	359,475
	$10,557,983
LIABILITIES AND EQUITY	
Liabilities:	
Loss Reserves	$110,761
Unearned premiums	89,613
Accrued interest payable	46,319
Total liabilities	246,693
Commitments and contingencies	
Stockholders' equity:	
Common stock, par $1 — shares authorized, 20,000,000; shares issued, 5,000,000	5,000,000
Additional paid-in capital	5,000,000
Retained earnings	311,290
Total stockholders' equity	10,311,290
	$10,557,983

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A complete copy of the certified audit is available at

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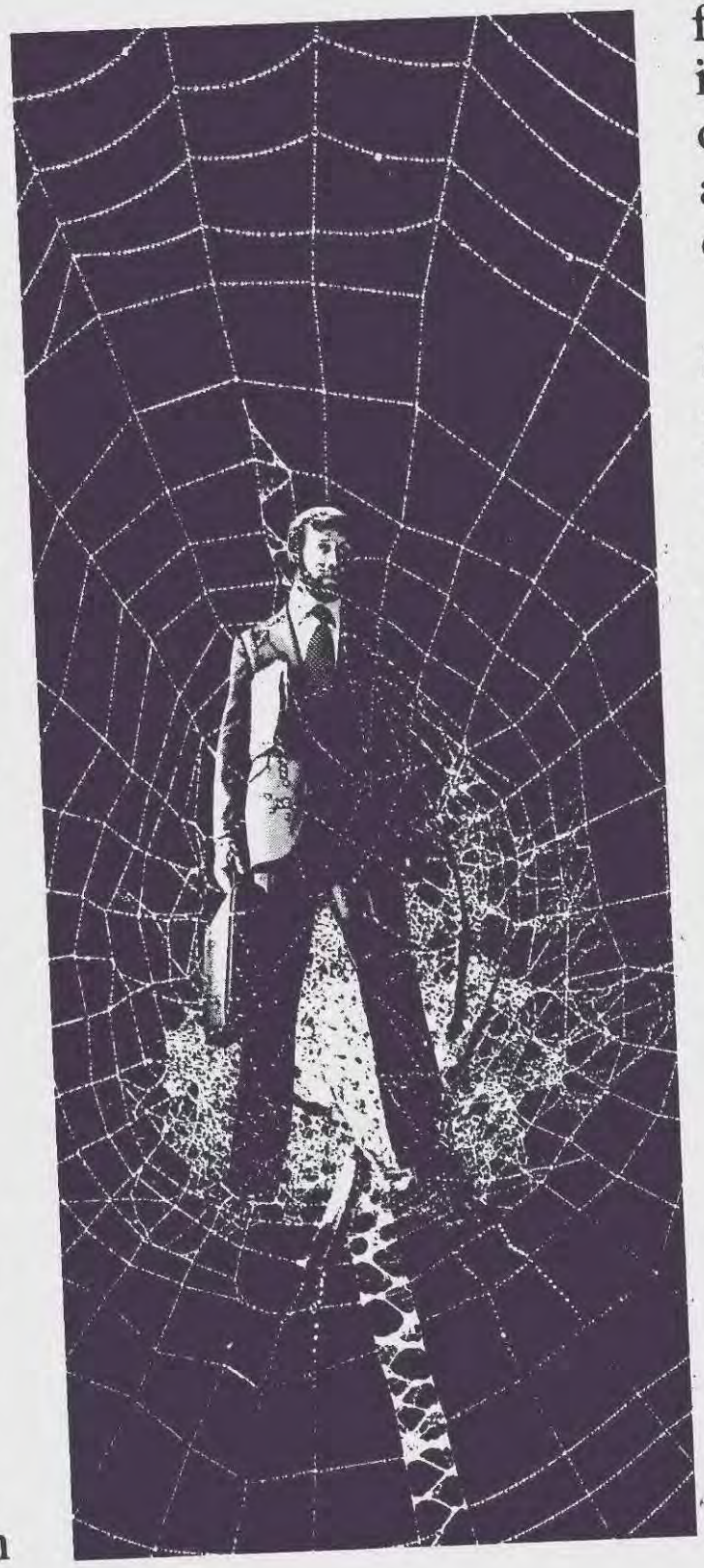
How not to be captive to your captive.

A captive program is not for everyone. But for those seriously thinking about one, an important consideration is how to operate it in a way that doesn't place you in a bind but allows you to achieve your objectives.

Captives can often tie up management time, money, and talent without providing the benefits expected. However, there is a way to avoid being captive to your captive.

AFIA has been involved with captives since they first began to attract the attention of the marketplace. And probably are working with more overseas captives than anyone else. Our role is to eliminate the stumbling blocks that tie-up time, money and management. And because we have been foreign insurance specialists for over 60 years, we can bring the knowledge and experience to your captive no one else can.



Operating in more than 80 countries, AFIA can provide admitted local policies with competitive rates and conditions, and AFIA reinsurance can simplify such matters as cut-through clauses, reinsurance recoveries, and corporate guarantees.

AFIA provides the full insurance services needed allowing the parent company to obtain the benefits of a captive without being tied up by it. It's why we say, there's a place for every type of insurance situation in AFIA's world, and one reason why 90 of the top 100 U.S. companies operating abroad insure with AFIA.

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Jack Bogardus, president, tells how A&A works from a client's point of view:

"With Anistics, financial managers handle risks based on certainty rather than uncertainty."

"There's a whole new group of financial and risk managers in the country today, young tigers who have come out of business school and are looking for advanced techniques. Insurance doesn't mean anything to them. It's just a word. What they are interested in is bottom line. And this is what our Anistics operation does, it takes their point of view—helps forecast and remove the uncertainty from the future, so these managers can handle risks based on certainty."

Working from a client's point of view is our way. From our top management to the men and women in over 110 cities here and overseas. That means working as allies, solving business problems together. If developing new techniques is what it takes to do a better job, we'll develop them. As we did with Anistics, a highly sophisticated, computerized subsidiary which helps major corporations determine the best ways to predict and finance losses.

We think our dedication to acting as an ally of the clients we represent is a big reason why A&A has become a worldwide leader in the insurance brokerage and financial services business. We have the facilities, expertise and strength to act as effective allies. We work from the client's point of view, whether the corporation is large or small.

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