

# Business Insurance

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Updates

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## Caremark admits to kickbacks in health care fraud settlement

NORTHBROOK, Ill.—Caremark International Inc. will pay \$161 million in criminal fines and civil payments to close a health care fraud investigation by the U.S. Justice Department and numerous federal and state agencies.

Under terms of the settlement, reached June 15, Caremark admitted that its employees paid kickbacks to get doctors to refer Medicare and Medicaid patients to Caremark's home infusion, oncology, hemophilia and human growth hormone businesses. The

See Updates on next page

## U.S. buyers seek added security from U.K. insurers

By GAVIN SOUTER

In a move that could both give policyholders an added measure of security and pressure insurers to settle claims, some major U.S. corporations with coverage from London insurers are forcing them to put up pre-answer security bonds.

Nearly all states have long had laws on the books requiring non-admitted insurers to post such bonds—which can cost millions of dollars—when a claim is made but before there has been a determination of coverage. However, policyholders with long-tail exposures began paying particularly close attention to these statutes only with the recent turmoil at Lloyd's of London.

So far, policyholders are seeking the bonds primarily in California courts and only in cases involving environmental coverage from Lloyd's of London syndicates. Policyholder lawyers, though, expect the action to spread to other states and to other London insurers.

Lawyers for the syndicates, some of which have already purchased bonds, argue that policyholders are not primarily concerned with added security because the claims are already fully reserved. Instead, they say, policyholders are trying to strong-arm insurers into settling claims that the policies do not cover.

In recent weeks, several U.S. aerospace companies that are making environmental-related claims on their Lloyd's liability policies have sought pre-answer security bonds. The companies include Raytheon Co. of Lexington, Mass.; Hughes Aircraft Co. in Los Angeles; and Lockheed Martin Corp. in Bethesda, Md. In a related reinsurance action, an insurer of Hughes Aircraft—Argo-

See Bonds on page 37

## Clinton takes new stab at health care reform

By JERRY GEISEL

WASHINGTON—The drive to pass health care reform legislation—in shambles only a few months ago—has new life with the Clinton administration's endorsement last week of a scaled-back package.

Also last week, a bill was unveiled in the House that would provide medical savings accounts tax breaks to employees.

Included in the president's new package are non-controversial proposals like curbs on pre-existing medical condition exclusions, limited federal subsidies of COBRA premiums for low-income workers who lose their jobs and new health care purchasing options for small employers.

### That was then ... this is now

President Clinton's latest health care reform proposals are dramatically scaled back from his sweeping 1993 plan.

1993

Mandatory, government-established health care purchasing alliances

Employer health care mandate with employers to pay 80% of premiums

Ban on flexible benefit plans

Barring self-insurance for companies with fewer than 5,000 employees

1995

Limited government subsidies of COBRA premiums

Curbs on pre-existing medical condition exclusions

Expanded tax deductions for health care premiums paid by self-employed

Increased health care purchasing options for small employers

GRAPHIC BY JOHN HALL

Conspicuously absent are government-established, monopolistic health care purchasing alli-

ances, an employer health care mandate and caps on health in-

See Benefits on page 4

## Sweeping bill to reform OSHA debated in House

By MARK A. HOFMANN

WASHINGTON—A House panel on Wednesday will begin debating a proposed massive overhaul of federal oversight of workplace health and safety.

The Safety and Health Improvement and Regulatory Reform Act of 1995, introduced by Rep. Cass Ballenger, R-N.C., would radically redirect the Occupational Safety and Health Administration.

Under the bill, at least half of the agency's budget would be earmarked for consultation and training programs, and the agency would be subject to the risk assessment and cost/benefit measures approved by the House earlier this year (BI, March 6). The bill also would abolish the National Institute of Occupational Safety and Health as a separate entity and merge the federal Mine Safety and Health Administration with OSHA.

The House Economic and Educational Opportunities Subcommittee on Workforce Protections, which Rep. Ballenger chairs, has

See OSHA on page 38

## Recovering from blast

### Oklahoma risk managers credit pre-planning

By RODD ZOLKOS

SEATTLE—As difficult as it is to recover from a catastrophe like the bombing of Oklahoma City's Alfred P. Murrah Federal Building, the task becomes doubly difficult when your state's risk management office is included in the destruction.

Oklahoma's risk management department was one of several state agencies with offices in the heavily damaged Journal Record

building, across a parking lot from the bomb's target (BI, April 24). In addition to blowing out every window in the building and collapsing walls, the blast scattered the files of some 3,000 pending tort claims in the risk management office.

But proper disaster planning and appropriate use of electronic data processing systems speeded the risk management department's recovery, allowing it to move quickly into helping the other state agencies recover from the disaster, said John Zakariassen, the state's risk manager.

sen, the state's risk manager.

"Because of the systems that were in place, state agencies were able to get back on their feet very quickly," he said. "I had the risk management office open at 8 a.m. the next day and it was because of the computer systems we had."

Mr. Zakariassen discussed his department's experience earlier this month on a panel at the annual Public Risk Management Assn. conference.

See Oklahoma on page 24

Oklahoma's state risk management office sustained damage in the blast



## Updates

### Caremark settles fraud suits

Continued from preceding page

firm also admitted sending inflated bills to Minnesota and Ohio Medicaid programs and failing to keep accurate records at its pharmacies.

The Northbrook, Ill.-based health care services company pleaded guilty to two counts of mail fraud and agreed to pay \$85.3 million to the federal government and \$44.6 million to the states of Minnesota and Ohio. Caremark also must pay \$29 million in federal fines and must contribute \$2 million to a program for people with HIV or AIDS.

A federal judge will decide whether to accept the plea agreement in each of the criminal matters.

The settlement allows Caremark to continue providing services to Medicare and Medicaid patients. Investigations continue of former Caremark employees and others involved in the kickback scheme.

Caremark will take a special \$110 million aftertax charge to second-quarter earnings to account for the settlement. The firm may have to increase that charge by \$20 million to \$35 million aftertax because of ongoing legal fees and other related costs.

### HMO satisfaction survey

NEW YORK—Kraft Corp. and Southern California Edison Co. are among the 65 companies participating in a satisfaction survey of more than 50,000 employees in health maintenance organizations.

Managed care research firm CareData Reports Inc. will evaluate HMO satisfaction in five regions: Southern California, Cleveland/Great Lakes Area, Northern New Jersey, Connecticut and Houston.

Employees will be asked to rate the plans on access to network hospitals, primary care physicians and specialists, and on pharmacy benefits, plan administration and customer service. The survey also asks about the treatment of specific illnesses, like asthma and diabetes.

CareData did a similar survey last year in the New York metropolitan area (*BI*, Nov. 7, 1994). Like that survey, this data will be used to rank specific health plans on overall consumer satisfaction.

CareData retains ownership of the data but will provide standard reports on the results—due out in October—to participating employers at no charge. Participating health plans, employers requesting special analyses and others must pay for the information.

HMOs sponsored by Kaiser Foundation Health Plans, CIGNA Corp., Aetna Health Plans, Blue Cross & Blue Shield and Prudential Insurance Co. of America are among the plans to be studied.

### N.Y. HMO disclosure backed

ALBANY, N.Y.—A bill proposed by New York Gov. George E. Pataki last week would require health maintenance organizations to disclose to potential members coverage provisions, including limits and exclusions, utilization review practices, physician reimbursement methods and the drug formularies the HMOs use.

The bill, which has not yet been introduced, is designed to take the mystery out of buying health insurance, Gov. Pataki said.

HMOs also would have to offer doctors and other health professionals a hearing before they could be terminated. Violations would be punishable by fines.

### Second injury fund to close

HARTFORD, Conn.—Connecticut Gov. John Rowland is expected to sign into law a bill that would close the state's debt-ridden Second Injury Workers Compensation Fund to new claims as of July 1.

The fund is carrying an unfunded liability of \$6 billion and lacks proper management, say sponsors of a measure the Connecticut Legislature passed earlier this month.

Second injury funds are designed to encourage employers to hire individuals with a previous injury, by paying part of their benefits if they become totally disabled. The funds have been widely criticized for being poorly run and duplicative of the Americans with Disabilities Act (*BI*, June 5).

New cases that would have been slotted for the fund will now fully remain with workers comp insurers. Current claims in the fund will be run off over about 10 years through continued assessments on businesses. However, the rate will be 16% of workers comp costs instead of 20% and that percentage will decrease over time.

### J&H loses age bias ruling

NEW YORK—Johnson & Higgins' compulsory retirement policy for directors is unlawful, a federal district court judge has ruled.

The policy of making directors retire at age 60—or 62 if they have been directors for 15 years—violates the Age Discrimination in Employment Act, U.S. District Judge Leonard B. Sand of Manhattan said last week in granting summary judgment to the Equal Employment Opportunity Commission.

The court might have found differently if directors were able to remain employees of J&H after they had resigned their position on the board and sold their stock in the company, he wrote.

J&H argued it would be awkward and unrealistic for directors to move from positions of power and prestige to being "mere employees."

Alternatively, J&H could restructure its retirement policy so that it kicks in at age 65, Judge Sand said.

The judge rejected J&H's argument that the EEOC should not have filed the suit because none of the directors named in the suit had sanctioned it (*BI*, March 6). J&H officials did not return calls.

See Updates on page 38

### Errors and omissions

• Value Health Inc. is acquiring prescription drug benefit firm Diagnostek Inc. for \$414.5 million. A June 12 Update misstated the price.

# House bill would create pool for catastrophe reinsurance

By MARK A. HOFMANN

WASHINGTON—Commercial insurers would be able to tap into a new catastrophe reinsurance fund in the wake of a massive natural disaster if disaster relief legislation introduced in the House of Representatives last week becomes law.

The Natural Disaster Protection Partnership Act of 1995 resembles previous measures that dealt with the implications of major disasters for the commercial insurance

market. Like earlier bills, it also would create a catastrophe reinsurance pool, but the new measure differs in the fact that the pool would be overseen by a non-profit private corporation rather than the federal government. The proposed Natural Disaster Insurance Corp. also would provide primary catastrophe insurance to homeowners.

The excess reinsurance program would cover losses caused by earthquakes, volcanoes, tsunamis and hurricanes. The coverage

would not be available until the property/casualty insurance industry suffered aggregate losses in excess of 15% of consolidated industry surplus from those four perils during a 12-month period. According to the Insurance Information Institute, consolidated surplus reached \$190.6 billion at the end of 1994, which would set the loss trigger at approximately \$28.6 billion.

The bill further refines the trigger by holding that "only such

See Cat fund on page 37

# AT&T pact expands benefits

Contract with unions boosts pensions, managed care

By CHRISTINE WOOLSEY

WASHINGTON—A tentative agreement forged by AT&T Corp. and 101,000 members of the Communications Workers of America and the International Brotherhood of Electrical Workers would expand managed care coverage, augment child and elder care programs and boost pension benefits.

The new three-year contract would be retroactive to May 28,

the day after the unions' former labor agreements expired. Both the CWA and the IBEW are expected to ratify the new contract in the next few weeks.

Highlights of the contract, which was negotiated in Washington on June 9, include improvements to AT&T's self-insured point-of-service plan for active employees.

Beginning Jan. 1, 1996, employees who seek care from network

providers would receive 100% coverage for eligible medical expenses. Those employees would no longer have to pay a \$150 annual deductible or coinsurance, which had ranged up to 20%.

But, employees who obtain care from network providers would have to pay a \$10 copayment for most visits to physician offices and pay a \$40 copayment for hospital emergency room treatment.

See AT&T on page 36

## Insurance rating agencies respond with approval

# ITT spinoff to benefit insurer

By MICHAEL SCHACHNER

HARTFORD, Conn.—Rating agencies and analysts are reacting favorably to ITT Corp.'s announcement last week that it will spin off its various businesses, including insurance operations, to shareholders in order to create three separate, publicly owned corporations.

The largest of the new independent companies to be operating by Jan. 1 will be ITT Hartford Group Inc., which comprises the nation's eighth-largest property/casualty insurance operations and the 12th-

largest life insurance operations. ITT Hartford generated \$11.1 billion in revenues last year for ITT Corp. The other two groups will be ITT Corp. and ITT Industries Inc.

Insurance industry rating agencies said the move, which has been anticipated for months, is a positive one for ITT Hartford because it will free the company from any potential drain on capital from its parent company.

Standard & Poor's Insurance Rating Service, which in March lowered its rating on various ITT Hartford entities but kept those ratings on

CreditWatch pending resolution of ITT Corp.'s ratings, said Hartford's A+ rating will be affirmed and removed from CreditWatch before year's end.

Moody's Investors Service confirmed its Aa2 financial strength rating of the ITT Hartford Insurance Group intercompany pool as well as Hartford's A1 senior debt rating.

And, A.M. Best Co. placed Hartford's life insurance unit ratings of A++ under review but said the company's A+ property/casualty ratings are unaffected.

See Hartford on page 36

# Small businesses seek federal reforms

WASHINGTON—Wide-ranging regulatory and legal reforms are high on a list of 60 changes that small businesses would like to see from the federal government.

The White House Conference on Small Business, which issued its recommendations last week, also endorsed the creation of a private, non-profit corporation to reinsure catastrophes (see related story).

Regulatory reforms endorsed by those attending the conference included allowing businesses to re-

quest safety inspections from the Occupational Safety and Health Administration and then to correct the shortcomings without facing immediate sanctions. The delegates also asked Congress to eliminate retroactive liability under Superfund for wastes that were legally disposed of before 1987. The delegates also endorsed applying cost/benefit analyses to environmental regulations.

Tort reform measures, such as instituting loser-pays rules in civil

cases, also were endorsed.

Other issues dealt with by the attendees—who had been chosen in 59 state meetings—included taxation, individual retirement accounts, capital formation, procurement, affirmative action programs and reducing the paperwork burden on small business.

The 60 final recommendations were culled from more than 400 approved at regional small-business conferences held earlier this spring.

—By Mark A. Hofmann

## Inside

• A national initiative aims to encourage Medicare-eligible retirees to join HMOs. **PAGE 6**

• The NAIC's move to open its doors is a welcome step, this week's editorial says. **PAGE 8**

• Insurance growth in China to remain slow. **PAGE 31**

• The P/C insurance industry is undergoing major structural changes, analyst Myron Picoult says. **PAGE 39**

## Departments

Advertiser Index.....28  
A.R.M. Exercises.....23  
Benefit Beat.....6  
Books & Ideas.....23

Classifieds.....34  
Datebook.....34  
For the Record.....17  
Insurance Services Guide.....35  
International.....31  
Letters.....8  
Opinions.....8  
Perspectives.....23

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# Long-term view pays for owners of captives

By GAVIN SOUTER

TUCKER'S TOWN, Bermuda—Once a company decides to set up a captive insurer, it should kiss

**BERMUDA** conventional insurance  
**INSURANCE** symposium

programs goodbye forever, a risk manager says.

Captive owners should resist the lure of cheap insurance and stick with their captives in soft and hard markets, since insurers which undercut captive premiums usually offer less extensive coverage and try to avoid paying claims, he said.

And in the future, captives will play an increasingly important role as insurance buyers become more sophisticated, other experts said.

Captive owners will use their captives to overcome regulatory problems and to fund larger and broader self-insured retentions, captive experts said earlier this month at the Bermuda Insurance Symposium II.

The establishment of a captive should create a permanent gulf between the captive owner and the commercial insurance market, said Bart C.M.I. Beusmans, general manager of Akzo Nobel Risk & Insurance Management B.V. in Arnhem, Netherlands, which is the risk management subsidiary of chemicals, pharmaceuticals and fibers manufacturer Akzo Nobel N.V.

"When you reach the decision to self-insure, you have reached the point of no return," he said.

And the captive owners should not reverse their decision when insurance prices fall, Mr. Beusmans said.

"A captive can only survive if it follows the normal rules of insurance. If you take away business

See Captives on page 12

# NAIC moves draw attention

## Revisions prompt calls for accreditation reform

By RODD ZOLKOS

The National Assn. of Insurance Commissioners' decision to revise accreditation standards for risk retention group regulation is welcome news to those who've seen the issue block Vermont's accreditation.

While NAIC accreditation teams have questioned some aspects of Vermont's regulation of traditional insurers, the state's treatment of risk retention groups as captives rather than as traditional insurers as stipulated by the NAIC repeatedly was seen as the major obstacle to the state's accreditation.

But that changed earlier this month, when the NAIC decided not to require insurance departments seeking accreditation to regulate risk retention groups organized as captives in the same way as traditional insurers (BI, June 12). Until the NAIC develops an appropriate way to regulate those RRGs, they won't be part of the criteria for the accreditation standards.

While the NAIC decision is widely welcomed by those with ties to Vermont's insurance community, some still argue that removing RRG regulation as a factor in Vermont's accreditation bid shouldn't detract from a continued need for reforming the NAIC accreditation process itself.

John L. Primmer of the Primmer & Piper law firm in St. Johnsbury, Vt., said that like others involved in Vermont's captive industry, he was pleased by the decision of an NAIC working group that risk retention groups chartered as captives are unique, requiring a different regulatory approach than

traditional insurers.

"We thought it was the solution two years ago. It's what the federal law says and so we think the people who focused on that and took it into their hands have resolved it absolutely right," Mr. Primmer said. "Hopefully it will break the logjam on Vermont's accreditation."

"I think it's a positive thing the NAIC has done," said John Salisbury, president and chief executive officer of the Vermont-domiciled Housing Authority Risk Retention Group.

Vermont "has already, in our judgment, fairly extensive standards for risk retention groups. In fact, some of their standards probably could be used in the traditional (insurance) community," Mr. Salisbury said.

But Jon Harkavy, vp and general counsel of captive management firm USA Risk Group in Arlington, Va., calls the NAIC decision "hard to read" and "a shrewd political move."

He said he believes that NAIC officials felt the battle with Vermont ultimately wasn't worth any possible gains, and they realized the organization was better off taking RRGs off the accreditation table and eliminating

the possibility of a legal battle with Vermont or, at the very least, a continuation of the already lengthy dispute.

From an alternative market perspective, though, Mr. Harkavy said he views the NAIC's move with two concerns in mind.

The first is whether the NAIC's appoint-

**There has been too much emphasis on seeing Vermont accredited or not accredited, 'rather than in the accreditation process itself.'**

—Jon Harkavy

ment of a working group to study the RRG issue was "a fig leaf for the NAIC," he said, just to get the RRG issue off the table. The second is, "Are they going to try to set up separate standards which could be far worse than they are now?"

Mr. Harkavy said he believes there has been too much emphasis in the alternative market on seeing Vermont accredited or not accredited "rather than in the accreditation process itself." His concern is with reforming

See Vermont on page 29

# Commissioners lash back at NCOIL critique

By MEG FLETCHER

ST. LOUIS—It's state insurance regulators' turn to criticize state legislators for their swipe at the National Assn. of Insurance Commissioners' accreditation program and operations.

However, some issues raised earlier this year by legislators—like too many closed meetings—are now moot (BI, June 12). The NAIC recently voted to open its doors and to suspend the criteria of regulating risk retention groups organized as captives as an accreditation requirement (see related story).

The National Conference of Insurance Legislators began the exchange in March, when

an NCOIL committee issued a 62-page, broadly critical report claiming that the NAIC and its accreditation program usurped state power to regulate insurance (BI, March 3).

That committee and its parent—the Task Force on Insurer Solvency—formally adopted the report in late March. But, NCOIL took the unusual step of postponing action by its Executive Committee on the report until a July 28-29 meeting in Chicago, during which NAIC representatives will make a presentation (BI, April 3).

The NAIC released its 14-page reply during its recent summer national meeting in St. Louis. The NAIC points out numerous exam-

ples of what it considers unsound reasoning, as well as "errors and inaccuracies" in the NCOIL committee's report, including one claiming that some NAIC actions have usurped a person's right to due process.

The NAIC criticized the NCOIL committee for repeatedly citing the fronting discussion and resulting model act as an example of NAIC misconduct, though that model act is not an accreditation standard.

In its sharpest criticism, the NAIC labeled as "outrageously erroneous" an NCOIL committee claim that New York regulators had made the fronting regulation a de facto accreditation standard by including a reporting

See NAIC on page 29

# Pension simplification bill resurrected

By JERRY GEISEL

WASHINGTON—The Clinton administration is throwing its weight behind pension simplification.

With much fanfare, President Clinton last week used an annual small business conference to unveil a pension simplification package.

Many of the provisions—including an easier way to run non-discrimination tests for 401(k) plans and new safe harbors that could let employers skip the tests—essentially are recycled from provisions in 1992 legislation that passed Congress. But, President Bush vetoed the bill for reasons unrelated to the pension provisions.

But some of the ideas are new and geared to upper middle-class voters, whose support the president wants in 1996.

For instance, under the package, many employees earning between \$66,000 and \$80,000 would be able to contribute more to their 401(k) and other savings plans.

With many Republicans making hay about excessive rules and regulations, benefit experts see the proposal as a way for the Clinton administration to show that it also wants to cut red tape.

"The public has been saying that it wants less burdensome regulations and the administration is responding to that," said Frank McArdle, a consultant with Hewitt Associates L.L.C. in Washington.

Benefit consultants characterize the pension sim-

plication proposal as a modest step.

"Nothing in this package will revolutionize the administration of pension plans. But in the aggregate, the simplification and other provisions are a definite plus for employers," said Fred Rumack, director of taxes and legal services for Buck Consultants Inc. in New York.

"This is a useful first step," concurred Henry Saveth, a principal with A. Foster Higgins & Co. Inc. in New York.


At least one consultant, Sylvester Schieber, director of Watson Wyatt Worldwide's Research and Information Center in Washington, said the administration should do more to expand employee opportunities to contribute to savings plans.

Two proposed changes, though, would increase the chances that upper middle-income employees will contribute more to 401(k) and other savings plans. They would:

- Change the general definition of "highly compensated employee" for non-discrimination testing purposes to those earning more than \$80,000. Currently, the definition includes all those earning more than \$66,000.

That will enable employees in the \$66,000 to \$80,000 bracket to make the maximum deferral to their 401(k) plans because they would be considered—for non-discrimination testing purposes—non-highly compensated.

See Pensions on page 29



### How Clinton would change non-discrimination tests for 401(k) plans

- **Highly compensated employees:** Change definition so more employees could defer the maximum amounts the law allows.
- **Corrective distribution rules:** When plans fail the tests, deferrals generally would be returned to the very highest-paid people until the imbalance was corrected.
- **Prior-year testing:** Previous year's figures for low-paid workers could be compared with current year's figures for high-paid.
- **Safe harbors:** If employers contributed enough, they could avoid non-discrimination tests altogether.

DEPARTMENT OF THE UNITED STATES

# Benefits

Continued from page 1

insurance premiums—the heart of the administration's last reform package, which died last year amid massive congressional and public opposition.

Several months after his sweeping reform package failed, President Clinton acknowledged that he had tried to do too much and said he would develop a more modest plan. Last week's unveiling of the new proposal fulfills the president's pledge.

By backing a more politically realistic package, the administration has increased significantly the chances that Congress will pass a reform bill.

Such progress seemed unthinkable last year, when Republicans and Democrats viciously blamed each other for the demise of the

president's plan.

"The likelihood of that legislation being enacted is much improved. You have the key actors—congressional leaders and the administration—approaching the reform issue from the same perspective. They agree on the best tenets of reform," said Stuart J. Brahs, vp-federal government relations at The Principal Financial Group in Washington.

"This is a program from which Democrats and Republicans can begin negotiations," said Frank McArdle, a consultant with Hewitt Associates L.L.C. in Washington.

By contrast, the administration last year essentially closed the door on hammering out a bipartisan package when it steadfastly stood by provisions like an employer mandate that were anathema to most congressional Republicans.

## The administration has increased significantly the chances that Congress will pass a health care reform bill.

Employer groups welcome the administration's decision to opt for a scaled-back package, though they say they can't endorse it until the details are spelled out.

"Certainly a well-targeted initiative is a welcome change from what we saw last year," said Richard Smith, director of health care policy at the Assn. of Private Pension & Welfare Plans in Washington.

As to the details of the package, the administration filled in some of the blanks.

At a White House press briefing last week, officials described in broad form a provision that would provide federal subsidies of COBRA health care continuation premiums.

Under current law, employers can charge COBRA beneficiaries a premium equal to 102% of the group rate. Many potential lower-income beneficiaries, though, cannot afford to pay COBRA premiums, which, for family coverage, can be several hundred dollars a month.

Under the administration program, the federal government would subsidize the COBRA premium for up to six months for lower-income workers who lose their jobs and qualify for unemployment benefits.

The amount of the subsidy would be tied to the income of the COBRA beneficiary through a sliding scale. Clinton administra-

tion officials did not elaborate on how that sliding scale would work.

But they did say that as many as 4 million people might qualify for the subsidies, which would cost the government about \$14 billion over seven years.

There would be no change in the maximum period of time individuals can receive COBRA benefits. Under the Consolidated Omnibus Budget Reconciliation Act of 1985, employees who quit or lose their jobs can receive COBRA benefits for 18 months, while dependents who are entitled to coverage because of a death, divorce or marital separation are entitled to 36 months of benefits.

Subsidies also would be available to low-income workers who lose their jobs but are not entitled to COBRA coverage. That group includes employees who work for companies with fewer than 20 employees. COBRA does not apply to small employers.

Details on other provisions, including a curb on pre-existing medical condition exclusions, which has overwhelming congressional support, were not available last week.

Insurance industry lobbyists say those details may be worked out with congressional leaders. By contrast, last year the administration presented Congress with a highly detailed proposal, one that several committees essentially rewrote anyway.

While the Clinton administration was presenting its health care reform outline, House Republican leaders and others unveiled a long-awaited proposal to give new tax breaks to employees who participate in medical savings accounts.

Under the MSA legislation, introduced by Ways and Means Committee Chairman Bill Archer, R-Texas, and Rep. Andrew Jacobs, D-Ind., and co-sponsored by about 60 mostly Republican House members, MSAs would be tied to a catastrophic medical plan. Such plans are defined in the bill as those with deductibles of at least \$1,800 for individual coverage and \$3,600 for family coverage.

Employers and employees could make annual tax-deductible contributions that would be the lesser of the catastrophic plan deductible, or \$2,500 for individual coverage and \$5,000 for family coverage.

Employer contributions would not be added to employees' taxable income, though investment income earned on employees' account balances would be included.

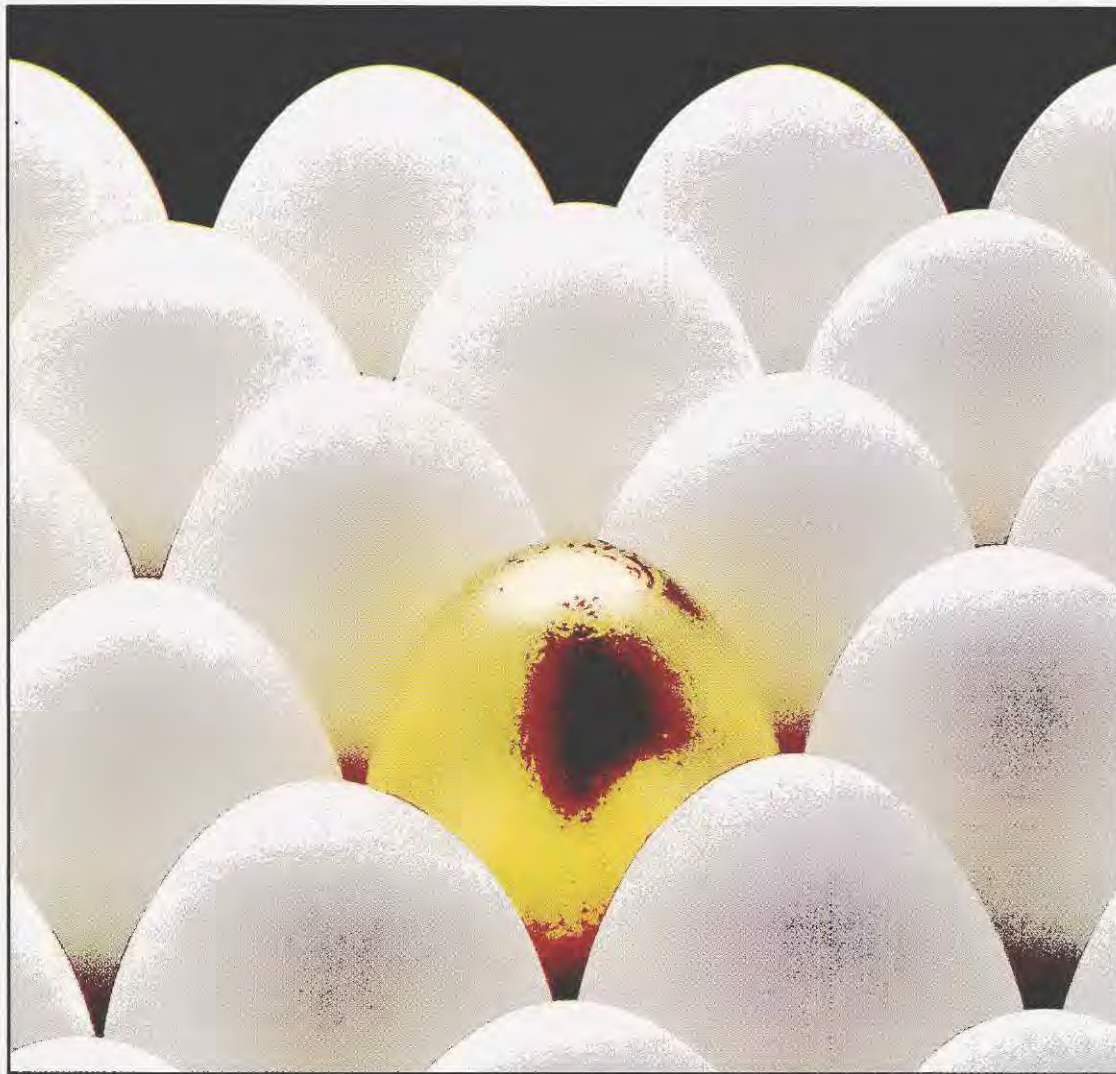
During the year, employees could withdraw funds from their accounts to pay for uncovered medical expenses.

At the end of the year, account balances could be withdrawn for any purpose, though the amount would be subject to income taxes and a 10% excise tax. Account balances, though, could remain in the MSA and be rolled over at the end of the year to pay for future medical expenses.

The administration has not yet staked out a position on MSAs, though Hillary Rodham Clinton last year criticized them, arguing that employees might delay needed care to build up account balances.

It is unlikely that the administration would oppose an MSA proposal once it realizes that the concept enjoys broad support, said Victoria Craig, director of research at the Council for Affordable Health Insurance, an Alexandria, Va., small-insurer group that strongly backs MSAs. **B**

## Guess what we just laid?



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# Employer group steering retirees toward HMOs

NEW YORK—A group of more than 50 employers, together with consulting firm Towers Perrin, is launching a national initiative to encourage approximately 1.5 million Medicare-eligible retirees to join health maintenance organizations.

The National Medicare HMO Initiative will target retirees in 30 states, giving them the option of enrolling in Medicare HMOs that have contracted with the federal Health Care Financing Administration.

Retirees that choose to join the networks will replace their Medicare indemnity benefits and any employer-provided supplemental benefits with HMO coverage.

All or most of the HMO premiums are paid by Medicare and are based on the average cost of

## Benefit Beat

health care in the county where the retiree lives. Many employers probably will pick up any portion of premiums not covered by Medicare.

While enrollment in HMOs will not be mandatory, many retirees are expected to choose the HMO option because of its improved benefits and lower costs.

"Retirees enrolling in HMOs generally receive more generous benefits," said Joe Martingale, a Towers Perrin principal in New York.

HMOs offer more preventive care coverage than Medicare does, such as regularly scheduled mammograms. Most HMOs also offer

discounted prescription drug benefits and some coverage for hearing aids or vision care. And, retirees typically do not have to deal with any paperwork related to health care claims.

A recent study by the Group Health Assn. of America, a Washington-based HMO trade association, indicates that Medicare recipients are joining HMOs in record numbers and that the majority are happy with the coverage and providers. In fact, 84% of retirees enrolled in HMOs would not switch back to traditional fee-for-service coverage.

Steering retirees into HMOs would give employers immediate cash savings from the managed care arrangement, plus lower liability and expense under Financial Accounting Standard 106,

Mr. Martingale said.

Towers Perrin will select Medicare-risk HMOs interested in participating in the initiative. The consulting firm will evaluate the HMOs based on information on access and quality, history of patient satisfaction, the types of benefits offered and cost-efficiency.

Then, each employer will be able to select the HMOs it wants to contract with in a given service area.

"Our hope is, through competition, to encourage HMOs to provide the best service in the eyes of the patient, the highest quality as measured by our indicators and the best premium," Mr. Martingale explained.

Among the employers participating in the initiative are: Citi-

corp in New York; E.I. du Pont de Nemours & Co. of Wilmington, Del.; Mercantile Bankcorp Inc. of St. Louis; the Federal Reserve System; New England Electric System Cos. of Westborough, Mass.; and Reynolds Metals Co. of Richmond, Va.

—By Christine Woolsey

## Retirement plan growth

More midsize and larger employers are offering pension and savings plans and are holding the cost of those plans steady, according to a recent survey.

But it may not be doing much good. In savings plans that give employees the choice of participating, employees may be contributing too little and investing too conservatively to retire comfortably, the survey found.

Ninety-one percent of employers surveyed—those with 200 or more employees—offer at least one pension plan, up from 89% in 1994 and 78% in 1993, according to the national survey sponsored by KPMG Peat Marwick L.L.P.'s compensation and benefits practice in Montvale, N.J.

Employers' costs for retirement plans, on average, is equal to 6.5% of payroll, down from 6.75% in 1993 and 1994.

The survey gauged the prevalence of certain retirement plan options among employers:

- More than half—58%—of the 1,183 employers surveyed offer 401(k) plans.

- Forty-one percent offer defined benefit plans, which is higher than the 34% of employers offering defined benefit plans in 1994 and 38% in 1993.

The survey is one of many recently that highlight an area of growing concern to benefit managers—low employee retirement savings rates.

Although the average 401(k) plan allows certain employees to contribute as much as 14% of their annual compensation, employees on average put in only about 5%, down from 6% in 1994.

In addition, more than 35% of those employees who are eligible to participate in a 401(k) plan fail to do so, the survey found.

Employers worry that low participation and savings rates—combined with many employees' choice of low-return, conservative investments—may not provide adequate savings for a secure retirement.

Eighty-two percent of employers that offer pension and savings plans believe employees will need three basic sources of income for a comfortable retirement—employer-provided benefits, personal savings and Social Security.

Only 4% of employers surveyed said a retiree could live on the income provided solely by the employer's retirement plan. Seven percent of the employers said a retiree could live on income from just the employer's retirement plan and Social Security, while the remaining 7% felt retirees could live on their personal savings with the employer plan as a supplement.

"Employers need to educate employees about retirement savings and the need for employees' own savings, even when the employer is providing a retirement plan," said Roy Oliver, national partner in charge of Peat Marwick's compensation and benefits practice in Los Angeles.

Copies of "Retirement Benefits in the 1990s: 1995 Survey Data" are available for \$135 each by faxing requests to Jim Berryman at 201-307-8071.

—By Christine Many

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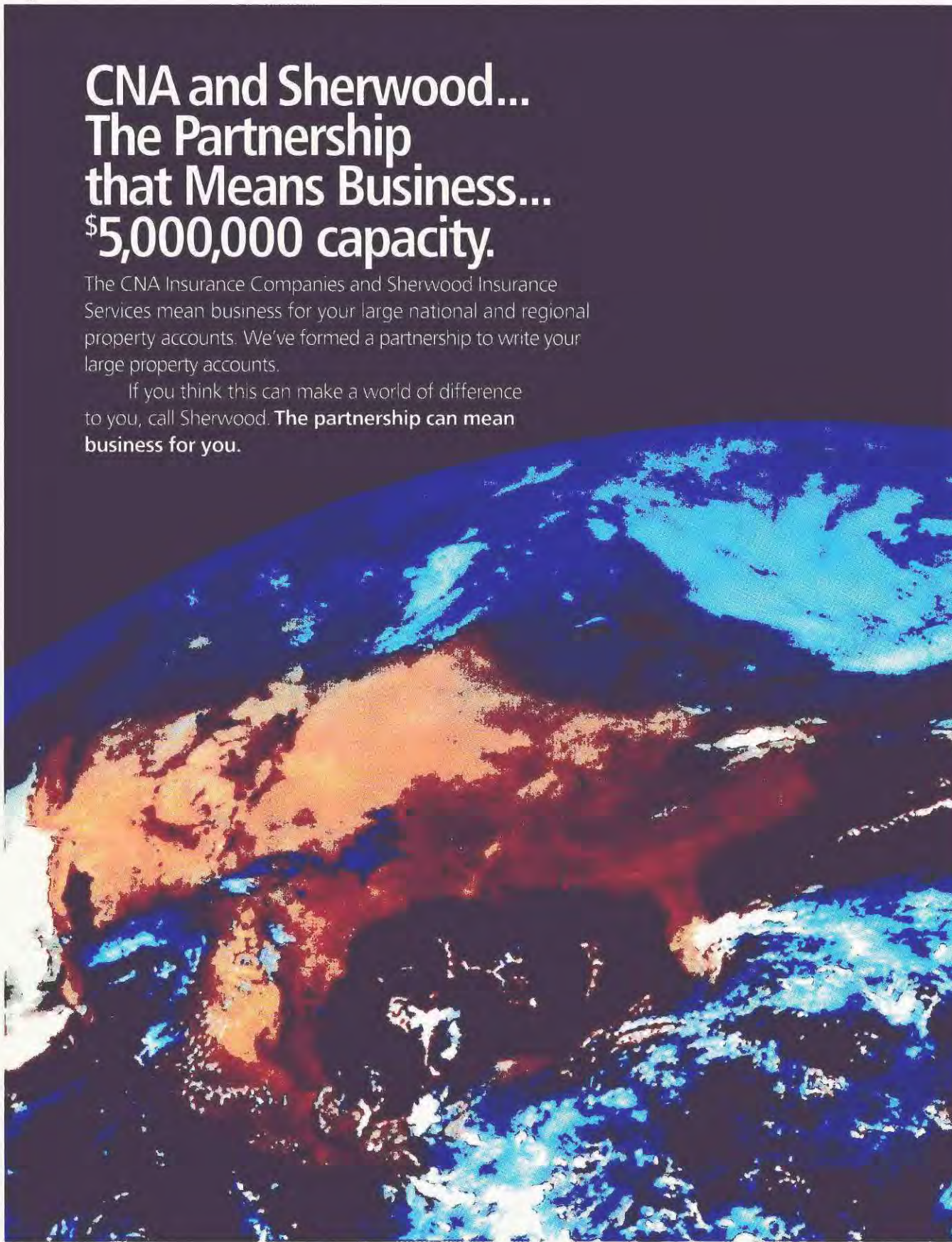
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# Opinions

## Keep the momentum going

WE WELCOME the sweeping changes the National Assn. of Insurance Commissioners is making as it strives to open up its processes and refocus its mission.

We hope this effort continues in the months ahead, because there is still much that can be done by the NAIC to help states improve solvency oversight and coordinate their activities.

Earlier this month, the NAIC approved proposals to open up key meetings and sessions, as well as certain conference calls, to the public. The NAIC also is moving to provide greater information on its budget, including the salaries of the NAIC's highest-paid employees.

The biggest attention-getter, and deservedly so, was the decision to eliminate the requirement that risk retention groups be regulated as traditional insurers for state insurance departments to attain NAIC accreditation. That removes a major roadblock to Vermont's drive to be accredited (see related story, page 3).

While complaints about the NAIC's obstinate refusal to accept Vermont's method of regulating risk retention groups have been the most visible criticism of the regulatory group in recent months, by no means was it the only one.

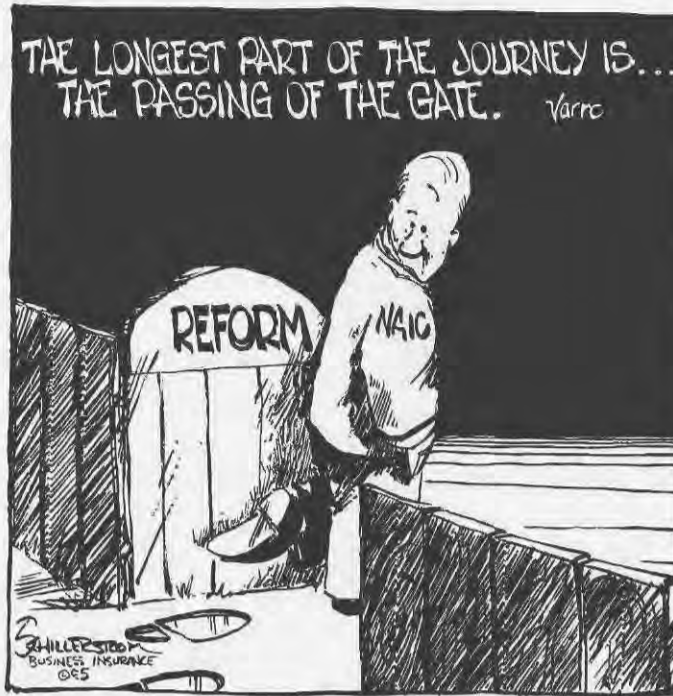
The NAIC has been under fire on several other fronts in the past few years. These included its development of a model fronting law that threatened to jeopardize many valid fronting arrangements for captives. That law was finally revised to include some key exemptions after much complaint. The group's accreditation program has been accused of usurping state legislators' authority and has prompted several states to introduce legislation that would give them oversight of NAIC activities. And even within its own ranks there are grumblings from new and veteran commissioners alike that the group has lost its focus and may have overstepped its bounds.

We hope that the recent changes made by the NAIC signal a willingness to reform the process of accreditation and decision-making that has led to these disputes.

One step in this direction is the NAIC's effort to define its identity. The group decided at its recent meeting that the NAIC "is a group of public officials imbued with the public trust and/or an instrumentality of the states."

Like other groups imbued with the public trust, it should be accountable to its public. We hope the new open-door policy will mean a better exchange of ideas between policymakers and policyholders.

Another step forward would be to continue to reform the accreditation process. While clearing the way for Vermont is a major victory, there are other problems



with the accreditation program that should be addressed. For example, the accreditation program largely has mutated into a one-size-fits-all plan. In an effort to forestall federal regulation, the program has become a de facto national regulatory scheme.

The goal to elevate the standard of regulation across the country is desirable, but the program still must be flexible enough to recognize some states' individual strengths or unique situations. New York, for example, should not necessarily be expected to regulate insurers the same as Wyoming, and vice versa.

Finally, the NAIC must strive for greater cooperation with groups that have a vested interest in the regulation of insurance, including risk managers, large and small insurers, reinsurers and state and federal lawmakers.

The NAIC recently issued a critical reply to a report by the National Conference of Insurance Legislators that took issue with the NAIC's accreditation and operations (BI, March 3). Unfortunately, the NAIC's unnecessary reply sounded more like a sore loser wanting to get in the last word than a response to valid issues and problems raised by the legislators.

The NAIC instead should move forward and aim to improve the regulatory process and address flaws in the accreditation program.

We think the group may be off to a good start and hope the momentum continues.

## Letters

### Correspondent stakes its fortunes with Lloyd's

To the editor: Recently, a great deal of attention has been paid to the financial losses suffered at Lloyd's of London. Some members of the media have asked if Lloyd's will survive.

As a Lloyd's correspondent, Petersen International Insurance Brokers has been designing and placing business with Lloyd's in the international medical, special risk disability, life and special risks arena for many years.

Over those years, many competitors of the Lloyd's market have sought Petersen International's business relationship.

We have even tried working with some of those Lloyd's competitors in various capacities. In addition, we have represented domestic insurers for life, disability and medical insurance. However, we have never found a stronger, better relationship than at Lloyd's.

In late 1994, Petersen International consciously ceased writing business with all other insurers. The Lloyd's market is our principal insurer. This is not to say that we will never represent another; it is only to illustrate that we trust the Lloyd's market as it is a market

and not a single entity.

Lloyd's has survived wars, famine, floods, fires, earthquakes, pestilence, economic depression, recession and inflation. Without Lloyd's, the world would not have progressed as it has. Lloyd's should be able to pull through the troubles it has faced in the past few years and needs the change that it is undergoing at this time.

**Thomas R. Petersen**  
Petersen International  
Insurance Brokers  
Valencia, Calif.

### Praise for "Beyond the Beltway"

To the editor: Thank you very much for the informative June 5 article, "Beyond the Beltway: Action in the Statehouses." The graphics were great and the layout was wonderful.

I hope you make this a regular feature in your magazine. The content and the way it is presented make it easy for the reader to locate the desired sections and

keep up to date on these unfolding legislative issues.

Please commend Meg Fletcher, Jerry Geisel and Mark Hofmann for this great set of articles.

**Julee Thomas**  
Manager-Risk & Insurance Services  
Adventist Health System West  
Roseville, Calif.

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## Captives

Continued from page 3  
from the captive, you are interfering with the spread of risk," he said.

And insurers cannot offer lower premiums than a captive in the long term without reducing their service or attempting to avoid paying claims to subsidize unrealistically low premiums, Mr. Beusmans said.

Risk managers should avoid placing business with those insurers whether they have a captive or not, he said.

"I don't want to do business with insurers that say that they can beat our captive," Mr. Beusmans said.

Akzo Nobel has three active captives: Crea S.A. in Luxembourg; Electro-Risk in the Netherlands; and another in Bermuda,

which it acquired through a merger and plans to close.

Risk managers should stick with their captives for the other benefits they bring, too, Mr. Beusmans said.

For example, companies can use captives to finance significant self-insured retentions, which helps to create a greater awareness of risks in operating units, he said.

Captives' attractions will become increasingly apparent to large multinational companies, which will seek excess insurers and reinsurers that understand the reasons the policyholder uses a captive, Mr. Beusmans said.

"The captive owner is seeking a real partner—someone who is able to think like a captive and offer tailor-made solutions," he said.

Insurers will have to work in different ways with captive owners as the structure of insurance programs and the insurance market changes, said William G. Watson, senior vp of risk management at Reliance National Insurance Co. in New York.

Insurance buying practices will change significantly within 10 years, he predicted. The layers of insurance will be much larger; liability and property retentions will be combined into one retention; benefits will be included in captive insurance programs; retentions will cover global programs; and the insurance contracts will last for several years.

Captives also will be used as the vehicles to allow companies to purchase multiyear contracts, he said.

And, captives will provide the mechanism for single retention levels and wide coverages, Mr. Watson said.

"The individual insurance contracts going into the captive will be workers comp, general liability, products liability, property and other coverages but the captive will pull them all together and buy reinsurance above the corporate retention," he said.

Risk managers are changing the way they buy insurance, agreed Robert Mulderig, chairman and chief executive officer of Mutual Risk Management Ltd. in Hamilton, Bermuda.

"Risk managers are realizing that they retain too little in terms of risks and they buy way too little in limits," he said.

Consequently, in the future they will fund significantly larger retentions through their captives and, at the same time, buy much higher excess insurance limits, Mr. Mulderig said.

The coverage provided by the captives will be very broad and the captives largely will look to other participants in the alternative risk transfer market for excess coverage, he said.

As risk managers use their captives more, they will make greater demands on their insurance providers and service companies, said Mark Angers, executive vp at brokerage Lockton Cos. Inc. in Kansas City, Mo.

"Brokers, captive managers and others are being asked to provide more value for the their fees and this will intensify," he said.

Risk managers are becoming more sophisticated and want to become more involved in the management of their captives, Mr. Angers said.

As a result, risk managers will seek advice from more diverse sources, including banks and other financial advisers, he said.

The session was moderated by Brian S. Webb, vp-marketing for BF&M Management Ltd. in Hamilton, Bermuda. **BI**

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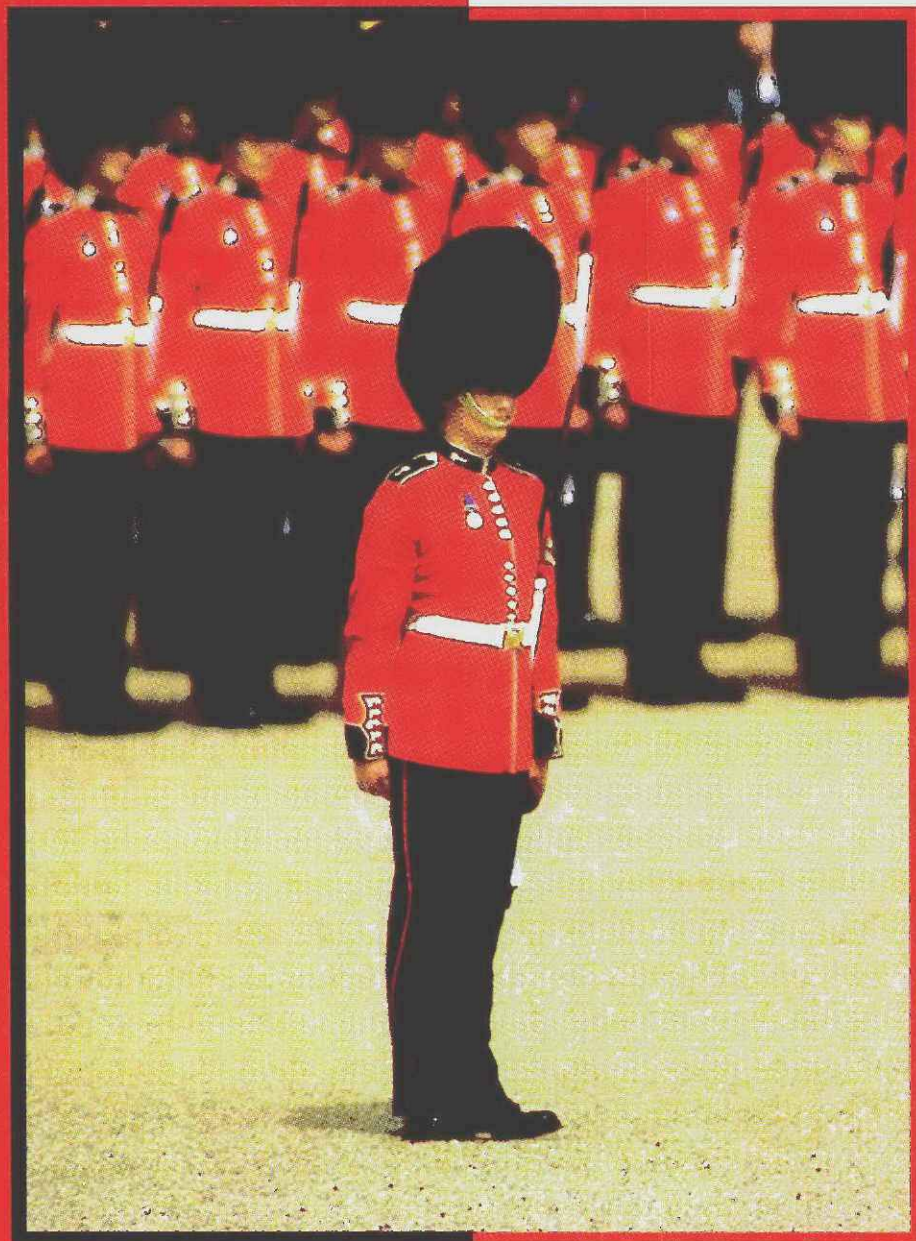
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# E.U. may see financial reinsurance growth

By PAUL D. WINSTON

TUCKER'S TOWN, Bermuda—Demand in continental Europe for financial reinsurance products is expected to grow

**BERMUDA INSURANCE SYMPOSIUM** as the market becomes more competitive with the removal of trade barriers, a reinsurance executive contends.

The European market for finite risk reinsurance currently is more limited than the North American market because European consumers and regulators are not constantly scrutinizing insurers' performance, according to Dirk Lohman, a deputy member of the board of management at Hannover Reinsurance Co. in Hannover, Germany.

While financial products have been used in Europe to run off business and finance growth, they generally have not been used to finance liabilities and smooth balance sheets, he said earlier this month during a panel discussion at the Bermuda Insurance Symposium II.

Insurance consumers in continental Europe are less security- and rating-conscious than consumers in the United States, Mr. Lohman explained.

This reaction—which is the same for all financial services—is because there have been relatively few insolvencies of European insurers and banks outside of Italy, Spain and the United Kingdom, he said.

Another factor limiting demand for financial reinsurance is that direct writers dominate the insurance distribution system in Europe, so there are no agents watching out for financially insecure underwriters, said Mr. Lohman.

Also a factor is how regulators approach their jobs, said Mr. Lohman, noting that regulators in the European Union are focused more on solvency than consumer interests. "Regulators understood consumer protection to mean promoting transparency and preventing insolvencies," he said. This was accomplished through highly regulated markets, rigid tariff systems and uniform policy conditions. It also meant the closing of markets to outside competition and, at times, the stifling of innovation.

In addition, insurance companies in Germany, for example, are not required to file their annual statements and solvency ratios until many months after the close of their fiscal years, he noted. Insurers are required to report within six months of the end of the year, while reinsurers have 10 months.

Financial reporting is done only on an annual basis, not on a quarterly basis, he added.

As a result of the reporting requirements, even publicly held insurers are not subject to the same degree of scrutiny by analysts as their U.K. and U.S. counterparts. "There's not much to follow because reporting is only done on an annual basis and that information is in arrears," he said.

Because of limited demand for financial disclosure, continental European insurers generally have not been interested in financial reinsurance products.

"Managements are unwilling to admit problems to outsiders, particularly financial reinsurers," he said.

In Europe, Mr. Lohman summarized, there is a limited necessity to disclose information, a limited willingness to disclose information and a limited need for non-traditional reinsurance.

However, a number of changes about to occur as a result of the European Union's third directive on insurance could increase demand, according to Mr. Lohman. These changes include:

- The opening of the European Union property/casualty markets will cause a shift to greater competition from protected markets. As a result, insurers will need to develop new ways to differentiate themselves from competitors, such as through their financial strength or new products, he said. In addition, competition will reduce profit margins.

- The changes in the European Union mean a change in insurance regulation, resulting in regulators placing a greater focus on individual companies' performance, Mr.

Lohman said.

For example, regulators are expected to require some insurers to report information on a quarterly basis, such as premiums written and losses paid. "It's inevitable that over time, the European authorities will start to demand similar reporting to what the NAIC is asking," he said.

- Analysts will demand more information as more is made available.

- Changes in tax and accounting regulations in the European Union, particularly those related to "equalization" reserves.

Other factors that could increase demand for financial reinsurance are that as litigation increases, European insurers could face greater uncertainty and volatility over their

long-tail liabilities, Mr. Lohman said. In addition, the privatization of state-owned insurance companies may create demand for financial reinsurance, he said.

While Europe won't be a "bonanza" for financial reinsurers in the 1990s, new products will find greater demand, Mr. Lohman predicted.

Other speakers on the panel agreed that there is life for financial reinsurance, even after recent financial regulations like Financial Accounting Standard 113 narrowed the market for certain funded products (*BI*, Oct. 31, 1994).

"Centre Re, Scandinavian Re and Inter-Ocean all expect significant rises in business this year," observed W. Jay Branum, president of Inter-Ocean Reinsurance Co. Ltd.

in Hamilton, Bermuda, who moderated the panel. "Also, the entry of Stockholm Re, ACE and Liberty Mutual show the market has opportunity for growth."

Dave Brining, senior vp and chief financial officer of Scandinavian Reinsurance Co. Ltd. in Hamilton, Bermuda, observed that finite risk reinsurance still is used to address several needs, particularly as insurers seek to enhance their risk-based capital ratios or to obtain higher ratings.

Gregory E. Leonard, president of Pegasus Advisors Inc. in Simsbury, Conn., said financial reinsurance demand will continue because buyers are more sophisticated, regulators and auditors are applying "more logical" rules for their use and products will become simpler. **BI**

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By GAVIN SOUTER

# Using derivatives to cut risk requires careful management

TUCKER'S TOWN, Bermuda—Financial derivatives do not cause large losses—but the people who use them can.

**BERMUDA INSURANCE SYMPOSIUM** Used properly by insurers and reinsurers, derivatives can reduce risk and provide access to capital not normally available to cover catastrophic risks, a panel of experts agrees.

To do that, though, reinsurers and insurers must learn to deal with capital providers who are not insurance experts and who may not be used to the industry's business practices, they say.

The catastrophe reinsurance futures currently being traded at the Chicago Board of Trade show that the contracts can be used successfully. And a new product soon to be

introduced could make derivatives more attractive to the insurance industry.

In cases like the recent Barings P.L.C. debacle—in which the company collapsed and was sold because of huge trading losses (*BI*, March 13; March 6)—derivatives may appear to magnify risks, said Joseph B. Cole, managing director of Centre Financial Products Ltd. in Chicago.

But it is not derivatives that cause the losses, he said at a session he moderated at the Bermuda Insurance Symposium II, held in Tucker's Town, Bermuda, earlier this month. "It is speculation and lack of management control... When they are

used properly, derivatives will decrease risk 100% of the time."

Insurers are well suited to derivatives due to the natural spread of risk they have through insuring different risks, which often are in different regions, Mr. Cole said. "Insurance companies are nothing more than hedge funds in disguise."

And insurance can be the base for an attractive derivative because it is well defined, it can be segregated by region, and it has quarterly aggregate figures.

With their as-yet-unknown losses, long-tail risks can present some difficulties, but overall insurance- and reinsurance-related derivatives should prove popular, he said.

Derivatives based on insurance allow capital providers to share catastrophic risks without having to participate directly in the insurance market, said Thomas A. Bolt, managing director of the insurance derivatives group at Bankers Trust International P.L.C. in London.

And they allow insurers and reinsurers to lay off some of the risks of collecting on policies, he said.

Risk managers, too, may realize important advantages in using derivatives.

They can use derivatives to cover the diverse property, liability and financial exposures—even those that normally are not covered by insurance, Mr. Bolt said.

But the derivative products need to be well defined, he said. "Risk managers want something that is clear and transparent." This would allow them to use derivatives along with conventional insurance to cover risks.

"Derivatives can bring certainty when there is uncertainty as to what is covered by an insurance contract," said Andrew M. Martin, managing director of Sedgwick Payne Insurance Strategy Group Ltd. in London.

Derivatives can spread risks even further than conventional insurance. And unlike insurance coverage, financial derivatives have intrinsic value and can be traded, Mr. Martin said.

Buyers of insurance also could use derivatives to hedge against premium increases, he said.

"But continuity in relationships is absolutely zero," Mr. Martin cautioned.

In London, the absence of a suitable index stands in the way of insurance- and reinsurance-based derivatives. In the late 1980s, Lloyd's of London rejected attempts to use syndicate results as an index, he said, though attempts still are being made to base an index on Lloyd's.

"We may get in to a position where a finance director can walk over London Bridge in the morning and see a spring tide rising while there is an easterly wind and hedge the risk of flooding (by using insurance derivatives)," he said. The finance director then could sell the derivatives after the tide has subsided.

By contrast, options now being traded at the Chicago Board of Trade—which uses as an index quarterly industrywide loss ratios developed by the Insurance Services Office Inc.—can be used today to complement a reinsurance program.

Dena Kotsores-Karras, manager of market and product development at the CBOT, said that derivatives can be used to create a new layer of coverage; fill gaps in existing layers; balance exposures in terms of risks and levels of exposure; and hedge the risk of retained losses.

"You can think of them as off-the-rack reinsurance," she said. "They may not fit you exactly the way you want, but they will cover most of the exposed parts."

The futures and options traded are gaining in popularity, Ms. K-Karras said.

During the hurricane season last year, between \$17 million and \$18 million in capacity was available through the CBOT contracts, and the sellers of the contracts received \$3.5 million in premiums, she said.

"That might seem small, but it is significant for a market in its infancy," Ms. K-Karras said.

The sellers of the contracts are usually hedge funds and small investment companies. "It's people that can make decisions on the day and don't go through committees to get approval," she said.

The CBOT currently is working on a new product that will be an improvement on the existing contracts, Ms. K-Karras said.

The new contracts will be related to nine loss regions and three specific states—Florida, California and Texas.

Also, the new contracts will have six- and 12-month development periods after the loss quarter as opposed to the three-month development periods for the existing contracts, she said. Experience with the Northridge, Calif., earthquake showed that three months is not long enough to assess some catastrophe losses, Ms. K-Karras said.

The new contracts, which will trade alongside existing contracts, also might not use ISO statistics, she said.

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## Preventing insolvencies demands vigilance: Panel

By GAVIN SOUTER

TUCKER'S TOWN, Bermuda—Though more Bermuda insurers will go insolvent as the market

### BERMUDA INSURANCE SYMPOSIUM

ma-  
tures, a new insurance law should keep disruptions in the market to a minimum, said Bermuda's outgoing senior regulator.

Despite the new insurance law, U.S. regulators still view offshore domiciles with skepticism, a senior U.S. regulator said.

At the same time, policyholders should view the regulation of some U.S. insurers with some skepticism, a rating agency executive said.

By the time an insurance company's capital base gets down to near the solvency level, it's probably too late to do anything but pick up the pieces," Mr. Levin said.

Solvency standards are too simplistic to evaluate insurance companies that can cover multifaceted and worldwide risks, he said.

Risk-based capital standards set by the NAIC will be a marked improvement as they will allow regulators to review the operations of an insurance company early on in a crisis or prior to a crisis, Mr. Levin said.

Beginning with 1994 financial  
*Continued on next page*

## Bermuda rocks the world

TUCKER'S TOWN, Bermuda—About 475 insurance and reinsurance industry executives, risk managers and other guests gathered in Bermuda May 30-June 2 for the Bermuda Insurance Symposium II.

The symposium, titled "Bermuda: One Market for the World" and held at the Marriott Castle Harbour resort, explored all phases of Bermuda's insurance market, from captives to property catastrophe reinsurers to financial reinsurance.

Symposium attendees also were treated to a repeat performance of Rock 'n Roll Re, a band made up of executives in the Bermuda industry (see photo).

The band featured: Graham Pewter of Commercial Risk Reinsurance Co. Ltd. on drums and vocals; Tony Hay of Marsh & McLennan Global Broking (Bermuda) Ltd. on lead guitar; Michael Cobb of Johnson & Higgins (Bermuda) Ltd. on rhythm guitar and vocals; Reid Kempe of X.L. Insurance Co. Ltd. on rhythm guitar; Mark S. Berry of Mid Ocean Reinsurance Co. Ltd. on keyboards; and Robin Spencer-Arscott of Aon Risk Services (Bermuda) Ltd., on rhythm guitar and vocals.



JILL RUBINCHAK

Michael Cobb (left) and Robin Spencer-Arscott jamming.

The next Bermuda Insurance Symposium is scheduled for 1997. For more information, contact Suzie McKeegan, Bermuda Insurance Symposium, 73 Front St., P.O. Box HM 1366, Hamilton HM FX, Bermuda; 809-292-6386; fax: 809-292-6990.

## Despite the changes in Bermuda's law, U.S. regulators remain wary of offshore domiciles, says Lee Douglass.

An inevitable consequence of the maturing of Bermuda as an insurance market is an increase in the number of crises at insurers on the island, said Malcolm Butterfield, the former registrar of companies on Bermuda.

"We are going to see more crisis situations because the market is maturing, so we have to exercise the proper amount of diligence," he said.

Among the changes made by the Insurance Amendment Act 1995 are new \$100 million minimum capital requirements for catastrophe reinsurance and excess liability insurers (*BI*, Sept. 5, 1994). The law also gives regulators greater powers of intervention.

"They give us as much power as possible to stop money walking out of companies that are in a crisis," said Mr. Butterfield, who was recently appointed head of the insolvency and liquidation department at KPMG Peat Marwick. He was succeeded as registrar by Kymn Astwood, previously inspector of companies (*BI*, May 22).

Despite the changes in Bermuda's law, U.S. regulators remain wary of offshore domiciles, said Lee Douglass, who is insurance commissioner of Arkansas and president of the National Assn. of Insurance Commissioners in Kansas City, Mo.

U.S. regulators cannot get sufficient information about offshore companies to make informed decisions on their financial strength, Mr. Douglass said.

"When claims don't get paid, people don't want to hear that there is nothing I can do about it because the insurer is offshore," he said.

However, the new regulations in Bermuda are a "step in the right direction," Mr. Douglass said.

But it is not just offshore domiciles that sometimes have inadequate regulatory procedures, said Alan Levin, managing director in Standard & Poor's Insurance Rating Services Group in New York.

U.S. regulators relying on solvency margins to assess companies are being too simplistic, he said.

"They tend to fail in crisis situations primarily because, generally speaking, they are way too low.

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# Communi

## More than just talk.

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Continued from previous page  
statements filed this year, insurers are required to disclose risk-based capital information.

"RBC is much more appropriate because it evolves and changes as companies get involved in different risks," he said.

But even good regulations should be supplemented with good market intelligence and subjective judgment, Mr. Levin said.

Regulators also should be more willing to share information among themselves if they are to improve regulation throughout the states, he said.

The fear of federal regulation has been one of the driving forces in regulatory reforms in the United States, and that has changed now with the election of a Republican majority in Congress, according to David M. Spector, a partner at Chicago law firm Mayer Brown & Platt.

"Insurance regulation in the U.S. has always seemed to me to be driven by an element of paranoia...there is widespread fear of federal regulation," Mr. Spector said.

But the fear has subsided with mid-term elections, Mr. Spector said.

Now states are concerned that in the fight against federal regulation, they gave up too much power to the National Assn. of Insurance Commissioners, he said.

In Britain, the regulation of Lloyd's of London is under review.

While Lloyd's generates a lot of interest in Britain and overseas, its importance should be kept in perspective, said Jonathan P. Spencer, head of the insurance division of the Department of Trade and Industry, which regulates insurance in Britain.

"Lloyd's is but one, relatively small part of the British insurance

scene," Mr. Spencer said.

Lloyd's currently is self-regulated but last month, a British Parliamentary committee called for external regulation of Lloyd's (BI, May 29).

Government ministers currently are considering the proposal. But in the past, the U.K. government has opted for self-regulation of Lloyd's, Mr. Spencer noted.

The government also might be unwilling to act to change the regulations Lloyd's has worked through coming changes.

"In about five years time, the bulk of Lloyd's capital will be corporate so it is difficult to know what to do. If it all becomes corporate, we may be able to rely on regulations that apply to companies generally," Mr. Spencer said.

The session was moderated by Lynda Milligan-Whyte, partner at law firm Milligan, Whyte & Smith in Hamilton, Bermuda. **BI**

## For the Record

### Life insurers lose antitrust immunity

SAN FRANCISCO—One more line of insurance is no longer immune from antitrust suits in California after the State Supreme Court ruled earlier this month that life insurers are subject to liability under state antitrust and unfair business practices statutes.

Life insurers join their property/casualty counterparts, which lost their immunity from antitrust liability in 1988, when voters approved Proposition 103.

Writing for a unanimous court, Justice Marvin R. Baxter said the state's appeals courts have been mistaken over the last two decades in assuming that the insurance in-

dustry has been exempt from the California Cartwright Act and Unfair Competition Act since 1968.

The high court's June 1 ruling in *Manufacturers Life Insurance Co. vs. Superior Court* upholds a 1994 San Francisco Court of Appeal decision that allowed Weil Insurance Agency of Oakland to sue several insurers, brokers and trade associations.

Weil contends the defendants disparaged and boycotted the brokerage until its settlement annuities brokerage and consulting business was destroyed.

Some life insurers objected to Weil's practice of providing information on the actual costs of settlement annuities to plaintiffs and their attorneys, since that made it harder for insurers to settle personal injury claims for less than their cash value, the brokerage's suit claims.

*Manufacturers Life Insurance Co. vs. Superior Court*, California Supreme Court; SO31022, June 1, 1995.

### Blues plan to settle suit by physicians

WASHINGTON—Blue Cross & Blue Shield of the National Capital Area will not have to pay any monetary damages in its settlement of a suit brought against it by the Medical Society of the District of Columbia for alleged discrimination in how it selects physicians for a preferred provider network.

The medical society sued the health insurer last summer, alleging that the insurer unfairly favored doctors who charge low rates when determining which physicians could join its Select Preferred Provider Plan (BI, July 11, 1994).

The society sought to abolish the Select plan and to recover \$3 million in damages.

In a settlement announced last week, the medical society will receive no cash and the Select program will remain.

In return, the Blues will establish two physician advisory committees consisting of representatives of both organizations and other physicians from the Washington area.

The Quality Improvement Advisory Committee will review the Blues' quality improvement programs and practice guidelines and make recommendations concerning them. The Credentials Advisory Committee will review the Blues' credentialing policies and make recommendations regarding credentialing and network selection.

The Blues also will establish an appeals process for doctors who are not admitted to the plan.

### Washington enacts anti-fraud law

OLYMPIA, Wash.—A new law in Washington state stiffens penalties against insurance fraud.

Washington state's new law, S.B. 5617, clarifies current laws by better defining insurance fraud and gives insurers immunity from libel in reporting suspicious behavior.

The legislation also increases the penalties for fraud and makes filing false claims and trafficking in insurance claims more serious crimes.

The law "will help us crack down on the kind of auto insurance fraud rings that we have seen trying to move into the Northwest from California, where they have flourished in recent years," Insurance Commissioner Deborah Senn said.

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## For the Record

Continued from page 17

### California health care research project

SAN FRANCISCO—A new health outcomes research program involving Blue Shield of California and the medical centers of Stanford University and the University of California at San Francisco will try to develop and evaluate ways to treat and prevent major health problems.

"One of the key objectives of our efforts will be to design, study and make available a range of medical management programs to assist Blue Shield member physicians in improving the quality of their care," explained Dr. Albert R. Martin, vp of clinical systems devel-

opment.

"We will also develop specific self-help approaches that patients can use to manage chronic diseases, like coronary heart disease, hypertension and diabetes," he added.

One part of the program will be a two-year study of heart disease. Stanford researchers will evaluate the effectiveness of various work-site programs that incorporate aerobic exercise, a low-fat diet, smoking cessation, stress management, drug therapies and other components.

### Managed care lobby forms in California

SACRAMENTO, Calif.—A new coalition of California employers, insurers, health maintenance organizations and preferred provider organizations will fight legislation they feel would weaken managed care.

The group, Californians for Quality Patient Care, will work to promote managed care among state residents and will lobby against legislation that they believe would undermine the ability of managed care plans to provide quality and affordable health care.

To contact the coalition in Sacramento, call 916-774-0635.

### Nevada court upholds pollution exclusion

CARSON CITY, Nev.—The Nevada Supreme Court has become the third state high court to find that the absolute pollution exclusion clause in commercial general liability policies bars coverage for environmental contamination.

By ruling in favor of the insurer in *Aerolite Chrome Corp. vs. Hartford Insurance Co.*, the court joins the Connecticut and Texas Supreme Courts in finding that the absolute pollution exclusion should be enforced to bar coverage for environmental contamination claims, according to the Washington-based Insurance Environmental Litigation Assn. The IELA is a trade association of 20 major insurers that presents insurers' views on environmental coverage issues.

The May 26 decision stemmed from a suit that Reno, Nev.-based Aerolite filed against its insurer, seeking coverage under its CGL policy to pay \$375,000 in hazardous waste cleanup costs. Aerolite had agreed to pay the sum to settle a civil action brought in connection with a criminal conviction of an employee who illegally discharged hazardous waste into a toilet at Aerolite's Reno, Nev., plant.

Despite Aerolite's contention that coverage was not barred because the policyholder had failed to sign the absolute pollution exclusion endorsement, the Nevada Supreme Court found that the endorsement did bar coverage because Aerolite "never paid for pollution coverage; the exclusion was part of the policy in the previous two years; and the exclusion was referenced on the declaration pages of the policy."

### Information in brief

New Jersey has become the third state to consider legislation aimed at giving the **state oversight authority over the National Assn. of Insurance Commissioners**. Assemblywoman Clare M. Farragher, R-Monmouth County, has introduced a bill, A-2942, that is similar to those introduced in Vermont and New York... Robert Y. Barham, president and chief executive officer of Greenwich, Conn.-based Insurance Value Added Network Services Inc., or **IVANS**, died of a heart attack May 29. Mr. Barham, one of the founders of IVANS, was 65 years old. **BI**

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## Insurers not ready to pay tab

### Financing remains stumbling block to retrofitting quake-prone buildings

By JOANNE WOJCIK

**W**hile many insurance industry experts remain skeptical that retrofitting is a worthwhile property loss control investment, structural engineers insist that shoring up existing buildings is the most cost-effective way to help insurers withstand another Northridge quake or Hurricane Andrew.

Unfortunately, owners of properties damaged by these and other recent catastrophes can't rely on insurance to finance these retrofitting projects since most commercial property policies only will pay to repair structures to meet existing building codes, many of which have proved inadequate, engineering experts say.

However, insurers in the long-run may find it less costly to pay for retrofitting, rather than having to finance the rebuilding of structures that collapse when the next Big One hits, some experts say.

While insurers mull those options, public officials in catastro-

phe-prone areas are becoming increasingly concerned about the safety of older buildings as well as those whose structural integrity may have been compromised by the recent catastrophes.

In Los Angeles, for example, a recently passed ordinance requires reinspection and retrofitting of some 500 buildings suspected to have been damaged by the 1994 temblor.

In addition, after witnessing the devastation from the January quake in Kobe, Japan, the engineering community worldwide is working feverishly to find the formula for a truly catastrophe-proof building before the next disaster strikes.

But just who will pay to strengthen structures in the recession and catastrophe-riddled Los Angeles area?

Certainly not property insurers. After having picked up the tab for some \$11.7 billion in quake damage, insurers' generosity is running out and many have cut back their earthquake writings.

Most insurance policies—even commercial difference-in-conditions policies with code upgrade

endorsements—only will pay for retrofitting to meet existing building codes, regardless of whether city officials strengthen those minimum standards after a catastrophe.

And, while the new Los Angeles ordinance requires reinspection and reinforcement of all steel-framed buildings in the quake-affected area, building owners can only be forced to bring the structures up to code, which the engineering community says often are not stringent enough.

In addition, the ordinance leaves the decision of how many welding connections to inspect up to the structural engineer hired by the property owner.

So far, 10% of total connections is the figure engineers are tossing around, said Henri Koza, an associate in the Irvine, Calif., office of earthquake engineering consulting firm EQE International Inc.

With a typical seven-story, 150,000-square-foot building having between 80 and 100 welded connections, opening the walls and examining 10% of them would cost between \$16,000 and \$20,000 based on an average inspection price tag of \$2,000 per connection, he estimated.

The city of Los Angeles also has

adopted emergency regulations that no longer permit the type of welded connections that were used in the moment steel-frame buildings damaged in the 1994 temblor.

While the engineering community applauds this decision, the regulations have put the onus on them to come up with an alternative to the moment steel-frame construction method, which consists of beams and columns joined by a combination of welding and bolting, that was long regarded as one of the premier lateral-force resisting systems.

"We don't have something that the whole structural engineering community has agreed to," said Elwood Smetana, senior vp in EQE's Irvine office.

Senior EQE staff are working to develop new earthquake engineering standards as part of a joint venture project with the Structural Engineers Assn. of California, a professional organization comprising some 4,500 practicing structural engineers; the Applied Technology Council, a non-profit organization that performs research relating to structural engineering; and the California Universities for Research into Earthquake Engi-

neering, or CUREe, a consortium of major universities in California with expertise in earthquake engineering.

The SAC Joint Venture, made up of the above three organizations, has given a high priority to resolving the issues surrounding steel-frame buildings damaged by the Northridge quake. It will have to reach a consensus soon or risk holding up potentially lucrative new building projects or worse, considerable damage from another major quake.

In a separate project, researchers at the University of Texas in Austin are conducting a limited structural testing program that is partially funded by the owner of a damaged building that was under construction at the time of the Northridge quake.

However, engineers not associated with the testing have been critical of its effectiveness.

In particular, conditions in the Texas laboratory did not sufficiently re-create the kind of unique movement that occurred in the Northridge earthquake, they say.

Results from similar earlier  
See **Retrofit** on page 20B



# Retrofit

Continued from page 20A  
tests—most of which were financed by the steel industry itself—led structural engineers to decide steel-frame construction was the most likely to withstand earthquake jolts, Messrs. Koza and Smietana explained.

Doubtful of the effectiveness of such tests, EQE and other earthquake engineering firms are adopting their own repair and retrofitting techniques on a case-by-case basis, taking into consideration the age of construction and location, with soil texture being a significant factor in the

analysis.

The most popular, and conservative, of the techniques being employed is that of strengthening joints with additional triangular "ribs" and installing steel cover plates at the top and bottom of each connection.

Repair costs usually run between \$5,000 and \$20,000 per connection and retrofitting would add approximately 10% to 20% to that cost, Mr. Koza estimated.

Another retrofitting technique being applied in Los Angeles is derived from the 200-year-old sliding-friction technology discovered by British physicist Sir Isaac Newton.

"Sliding-friction technology permits us to install, both in new construction and in retrofit, low-cost friction brake shoes that can be thought of as calibrated 'earthquake barrier fuses,'" explained Los Angeles structural engineer Marc S. Caspe. Think of it as a horizontal brake shoe or shock absorber, he suggested.

The cost of such protection adds less than 2% to the cost of new construction and can be retrofitted at an equally reasonable cost, according to Mr. Caspe.

Such a system was installed for about \$6 per square foot in 1991 as part of the retrofitting of a 30-year-old 10-story Wilshire Boulevard building, he said.

Unfortunately, "resistance is high against requiring that 2% be spent" up front, he said.

But, such an investment in "proactive risk mitigation is worth it," insists EQE's Mr. Koza, especially since "it's common knowledge that these buildings are vulnerable now."

Furthermore, the Los Angeles building inventory has not been subjected to a major quake, he said. A major quake is considered 7.0 or higher on the Richter scale.

But, there have been more catastrophes with insured damage exceeding \$1 billion in the last 10 years than ever before, according to the Property Claims Divi-

sion of American Insurance Services Group Inc. of Rahway, N.J. (BI, Feb. 7, 1994).

With continued population increases in coastal and earthquake-prone areas, the trend undoubtedly will continue.

Today, seismologists warn that nowhere within 62 miles of a fault is safe, no matter how "quiet" a region has been.

Recognizing this exposure, the Southern California engineering community has joined with other experts throughout the world to promote the development and enforcement of new, more rigorous building codes in catastrophe-prone regions.

Current building "codes are only intended to define the legal borderline between 'negligence' and 'barely adequate,'" said Mr. Caspe. This "inherent flaw...came to public view for the first time after the very moderate Northridge earthquake."

But "the flaws in today's codes will be corrected, either in whole or in part by engineers now working to get ready for the next code edition" in 1997, Mr. Caspe believes.

In the meantime, hazardous buildings must at least be retrofitted to meet current code standards, he said.

And even though insurance policies are not likely to be a ready source of funding for retrofitting projects, the industry is beginning to recognize the loss control potential of such mitigation measures.

"I've never seen a case where it's more economical to rebuild" than to retrofit, Mr. Smietana pointed out.

As an example, he cited a San Fernando Valley commercial building that had collapsed from the inside. Even though the insurer was ready to write it off as a total loss, "repair costs were 40% of replacement costs."

Even though the engineering community strongly supports retrofitting, insurance contracts do not provide for upgrading damaged structures beyond existing building codes.

While the Boston-based Insurance Institute for Property Loss Reduction has formed a Retrofit Committee to study these mitigation measures, so far the response from insurers has been lackluster. The committee is just getting started.

The insurance industry has not yet been converted to the engineers' faith in retrofitting for specific structures.

"It's not like crash tests where you can keep the variables the same. There are too many variables with catastrophes like earthquake and hurricane," said a spokesman for the IIPLR.

Eventually, the insurance industry may develop a full-scale testing facility like that used for automobile crash tests. But, "it's hard to re-create an earthquake or a hurricane inside a building," he said. The only real test will be another catastrophe. **BI**

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By MICHAEL BRADFORD

There's a hurricane moving into the Gulf of Mexico and land-fall is expected in about eight hours; your office is in the projected path.

Do you:

- Protect vulnerable windows from high wind?
- Make sure records are safe from rain, wind and debris?
- Update and back up important computer files and transport them to a safe location?
- Run screaming into the night shouting, "The sky is falling"?

If you picked option D, there is a good chance for disappointment at your next performance review.

However, if you realize that the first three options are all correct responses, then you are probably familiar with the checklist that your company uses to prepare for and recover from catastrophes.

Insurers are becoming more concerned with practicing what they preach when it comes to catastrophe planning and the checklists that they have long touted for policyholders have become an important in-house tool.

The lists, which are compilations of tasks that employees must complete in preparation for a potential catastrophe or when recovering from one, began taking on particular importance about 25 years ago.

"That's when crisis planning became a more formalized part of management," said Gene Jeffers, executive director of the Western Insurance Information Service in Los Angeles.

Before crisis planning evolved into its more formal shape, "there were special-event kinds of things" that were centered on actions communities should take if catastrophe struck, Mr. Jeffers explained. For example, nuclear war drills in the 1960s had school children ducking under desks and adults noting the locations of evacuation routes and shelters, he pointed out.

By 1970, disaster planning was becoming more routine, with "most companies of reasonable size developing some sort of plan," said Mr. Jeffers.

Some insurers have been late in grasping the notion of protecting their own property even though the nature of their business is to advise others to protect theirs.

Only in the 1990s have insurers begun to realize that they have to take a close look at how they will recover from a disaster that affects their business operations, said William B. Gaines, senior vp of consulting operations for SunGard Planning Solutions Inc. in Wayne, Pa.

SunGard helps insurers and other clients put together disaster recovery plans, and Mr.

## Practicing what they preach: Insurers develop disaster plans

Gaines said interest currently is high. "We've seen a groundswell in the last several months in the insurance industry. They are be-



ginning to practice what they preach but are still behind banks" and other financial services industries, he added.

Disaster recovery plans provide a series of checklists that lay out a logical order of functions to be addressed in the event of a catastrophe and how those tasks should be accomplished.

"The key part of a plan is that when an incident occurs, planning and quick response" will make the event manageable, Mr. Gaines advised.

"A good plan has a series of checklists," he said. "They identify the resources to accomplish recovery and the sources of those resources. But the recovery will still depend on people who are knowledgeable in the company and the industry."

That means there is a lot of groundwork that goes into establishing a plan that can be held together by comprehensive checklists.

SunGard's approach is to help insurers complete a "business impact analysis" that looks at all key operating units of the company to determine how a disaster in each area would affect the entire operation.

For example, many insurers feel that policyholder confidence is vital to the company's success, Mr. Gaines pointed out. Therefore contacting policyholders quickly in the wake of a disaster that could affect service is a critical area that must be covered by those insurers' disaster plans.

When all key operating areas are examined, a plan can be written and checklists developed that will serve as guides to putting the plan into operation.

Mr. Gaines stressed that there are no boilerplate plans that can be handed to insurers. "If we do an insurance company today and one tomorrow, the list of priority functions will be different in each company. There are no industry standards."

Industrial Risk Insurers offers its policyholders a loss prevention program called Overview, which is customized for catastrophe planning in the insurer's own offices.

Among the checklists in Overview are those that cover tasks to

be carried out in the event of flooding, earthquakes or hurricanes. The insurer stresses to policyholders and its own staff the necessity for shaping the lists to fit the property and operations that could be affected.

"A checklist, to be really effective, has to match up with what you're evaluating," said Mark Tschiegg, vp of loss prevention at Hartford, Conn.-based IRI.

The insurer found its clients were having a hard time developing checklists from blank paper and therefore developed lists that could be customized, Mr. Tschiegg explained. IRI uses the same approach internally at its 11 technical service centers.

"Each center is responsible for a disaster plan for their operations and for their clients," he pointed out.

That means each of the insurer's centers has a different plan, based partly on geography. The Los Angeles office is prepared for an earthquake while one in Atlanta is more concerned with hurricane season.

"Each of these technical service centers have established emergency management procedures they have fine-tuned to their specific geographical area," said Ben K. Smith, manager of field services in IRI's Atlanta office. "They have all customized specific checklists that can be used to respond to a disaster in their own backyard."

Following the January 1994 Northridge earthquake, IRI found its checklist and procedures were up to snuff. The Los Angeles office was operational very soon after the ground stopped shaking.

"Most of the things that we do

in our offices can be started up again easily," said Deborah Boice, manager of field services in IRI's Los Angeles office. Computer files are duplicated and stored offsite in case some are lost and cellular telephones provide communications capabilities.

All the IRI technical service centers are equipped with cellular telephones that can be used in the event local phone lines are interrupted in a catastrophe.

As insurers come to realize the importance of catastrophe planning, some are finding to their dismay that checklists are lying undisturbed in dusty manuals.

"Unfortunately, many plans sat on the shelf," said Mr. Jeffers of Western Insurance Information Service. The plans became outdated and information in some cases was incorrect. "There is a need to refresh these plans." Pennsylvania National Insurance Group in Harrisburg, Pa., has knocked the dust off its manual and is upgrading the procedures that will be in place if catastrophe strikes.

The insurer had put together a business disaster plan and one for its data systems in 1972. While the data systems plan has been updated and kept active with mock disasters, the other has suffered from neglect, according to Brent Parrett, risk manager for the multiline property/casualty insurer.

Mr. Parrett spent six months studying how to update and keep current a plan that would allow Penn National to continue operating with a minimum of interruptions if catastrophe struck. Eventually, he settled on SunGard as a vendor to help design

and implement a plan.

"We're an insurance company and we understand risk," he said. "But we don't have a staff that understands putting together a disaster plan."

With SunGard's help, the insurer began analyzing the key areas of its operation to determine which were critical to keeping the business running if a catastrophe hit.

The plan, which is expected to be completed in around nine months, will consider the nitty gritty details of tasks like arranging backup electrical service if power is unavailable from local utilities and making sure telephone communications are available from alternate sources if necessary.

Once the plan is built, critical functions will be outlined as part of a checklist that management will refer to, Mr. Parrett explained.

United Services Automobile Assn. in San Antonio is another insurer that is improving its business resumption plan.

Like Penn National, USAA is using an impact analysis to determine what tasks key operating units must perform in an emergency.

"We're looking at it from worst-case scenarios," said Dianne Steffey, strategic planning analyst at USAA. The process will determine areas of weakness in terms of recovering from a disaster and correct those deficiencies.

"We are developing task lists based on the critical functions" that have to be continued to keep the company running if a disaster occurs, Ms. Steffey remarked. And, she stressed, training is an essential ingredient to ensure that employees are familiar with the tasks that will have to be performed in a crisis.

Ms. Steffey said the new plan should be in place by the end of the year. **EI**

## Finding the address of catastrophe risks

### ISO system helps insurers improve underwriting

By REGIS COCCIA

Determining catastrophe exposures quickly and accurately and setting premiums accordingly may be getting easier with a system developed by the Insurance Services Office Inc.

ISO's Geographic Underwriting System lets insurers examine the exposures facing a given risk based on its address. Developed about two years ago with DataMap Inc. of Eden Prairie, Minn., GUS is a personal computer-based system designed to make underwriting faster and more accurate, thus increasing insurers' revenues and productivity.

A spokesman for New York-based ISO said the system is intended to help insurers get a clearer picture of their books of business, balance out

their exposures and to make the underwriting process more efficient. "It's a work in progress, but it really seems to be taking off," he said.



One area where such efficiency can pay big dividends is in returning quotes on a given risk. "While price and service are very important factors in placing business, another factor is how quickly an insurer can provide a quote," the spokesman said. GUS dramatically reduces the time it takes to issue quotes.

GUS allows underwriters to get exposure data on any address in

the United States with just a few keystrokes at a computer. Typing in the address of a prospective risk calls up a menu of exposure categories, from windstorm to fire.

The system provides a historical database of catastrophic events—like a windstorm, for example—in the proximity of the risk's address and indicates its distance from the storm center. GUS also lets an underwriter know at a glance exactly how far the risk address is from bodies of water.

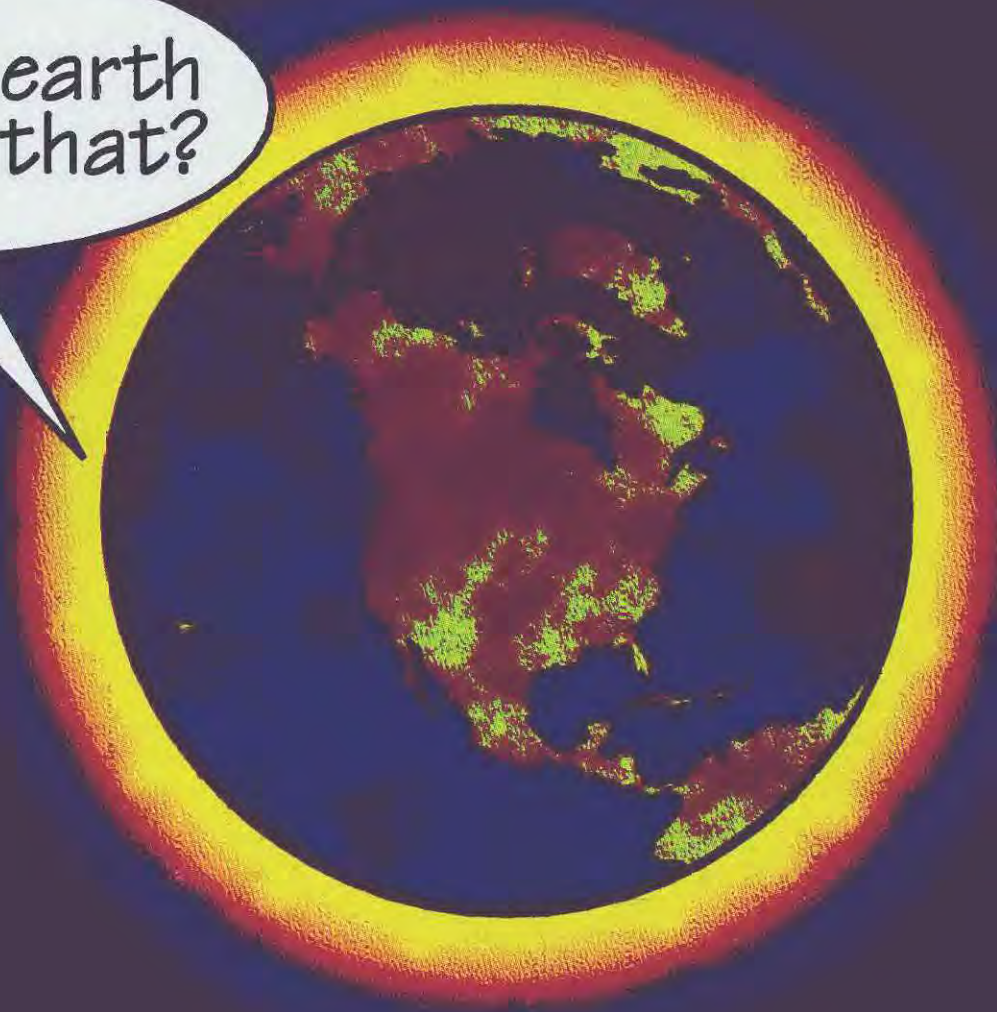
Other exposures that GUS can measure include:

- Crime.
- GUS shows the potential risk of personal and property crimes for given addresses throughout the United States.
- Personal and commercial auto.

GUS can identify exact driving distances between residences and places of business, making underwriting auto risks more accurate.

See GUS on page 20G

Where on earth  
can I find that?



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Issue Date	Directory
Feb 7	Third-Party Administrators
Feb 21	Utilization Review Providers
Mar 7	Risk Management Consultants
Mar 21	Employee Benefits Information Systems
Apr 18	Captive Managers
Jun 6	Property Loss Control Consultants
Jun 27	EAPs & Mental Health Networks
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# Wrapping up after catastrophe strikes

## Specialist company helps insurers limit extra loss costs

By MICHAEL SCHACHNER

Two of property insurers' biggest enemies are hurricanes and tornadoes.

When these storms hit, the result to buildings and homes is usually dire. But what can make an already bad situation worse for insurers is when subsequent rain dumps buckets of water on exposed properties.

Rain and wind causing further damage to injured buildings is a multimillion dollar headache for property insurers. Since the turn of the century, insurers have had some success mitigating these added losses by promptly covering damaged property in order to preserve structures and contents until loss adjusters can complete their work and repair teams can be hired.

Insurers generally hire local contractors and roofers to cover roofless and windowless buildings damaged by fire or severe weather. The problem with these methods, though, is that when these contractors simply place boards over broken windows or nail down thin plastic as a makeshift roof, subsequent high winds or storm conditions can rip those coverings off, allowing rain to soak a building's interior and contents.

But now there might be a bet-

ter way.

Anthony Seraphin, who some might consider the Christo of



the insurance industry, believes that he has the solution to the insurance industry's problem of how to protect and preserve damaged buildings. Using technology he perfected over the last 15 years wrapping boats and airplanes for storage, Mr. Seraphin's company now is wrapping damaged buildings in strengthened plastic and then heat-sealing the wrapping to prevent buildings exposed to the elements from sustaining further damage.

Having been in business only since May 1994, Mr. Seraphin's Global Wrap & Services Inc. in Montgomeryville, Pa., outside Philadelphia, is a relatively new company uniquely performing a loss control procedure that is fairly common in the insurance arena.

But, while all insurers hire contractors to cover damaged buildings, Mr. Seraphin claims to do it differently.

His formula consists of setting up a series of buckles and cables that form a frame around the damaged structure. His crews wrap an industrial-strength,



GLOBAL WRAP & SERVICES INC.

When a fire destroyed the roof of this home in northern New Jersey last year, Global Wrap & Services constructed a dome over the exposed section, protecting the building from further harm by the elements.

0.008-inch thick sheet of plastic over the frame and then heat-seal that plastic in order to form a taught, airtight covering. Vents are included to prevent rot and the buildup of moisture.

Over the last year, Global Wrap has picked up a number of contracts from insurers to go to sites where extensive property damage has occurred and wrap buildings in plastic to protect contents from further damage. Mr. Seraphin estimates that Global Wrap will do about \$750,000 in sales this year, most of that derived from insurers.

Global Wrap went to Pascagoula, Miss., in 1986 to do wrap work on building-size battleship modules at the Ingalls Shipyard. The Department of the Navy,

which had to send the modules by barge to other naval centers, was worried that the module's sensitive electronics could be damaged if exposed to the weather. Global Wrap solved that problem, and "the Department of the Navy was tickled to death," Mr. Seraphin said.

His crews also have wrapped dozens of houses across the country that have been damaged by fire and storms.

And just last month, his crews went to Oklahoma where a series of May tornadoes ripped through the town of Ardmore, causing serious damage to a local high school and the Uniroyal/Goodrich tire plant there.

Kemper National Insurance Cos., which insures the Uniroyal/Goodrich's tire plant, hired Mr. Seraphin's firm to come in and secure the portions of the plant left exposed by the tornadoes.

Successful protection and preservation of damaged sites can save major commercial insurers millions of dollars per year, Mr. Seraphin said.

"It's getting on toward hurricane season, so we're really gearing up. And now is tornado season in the Midwest. It's a busy time of year," he said.

Realizing that his staff of 15 cannot go to every site in America, Mr. Seraphin also operates a training school from his company headquarters that teaches local fire restoration companies and contractors how to employ his wrapping technique.

"We've trained 81 different fire restoration companies how to do this. They can then do the smaller jobs like a house or a small business. We do the larger commercial jobs ourselves," he said.

At this point, Global Wrap is operating on a case-by-case, contract basis, but Mr. Seraphin says he may soon have to go to retainers in order to guarantee that certain insurers have access to his services in case of a disaster.

## Arkwright to offer enhanced systems for evaluating its customers' risks

By DON LEWIS KIRK

Arkwright Mutual Insurance Co. is developing new information systems to provide a better exchange of loss control information between the insurer and its policyholders.

Waltham, Mass.-based Arkwright plans to unveil these systems in the United States starting this summer.

"Insurers are rich in data...but making it accessible in a meaningful and cost-effective way has been a challenge," said Nigel Grimm, vp and claims manager of Arkwright International Ltd. in London.

He discussed information systems at a recent risk management conference.

One new Arkwright system, called "Red Flag," analyzes data from the insurer's inspections and detects changes from one inspection to the next, Mr. Grimm said.

The system looks for drops in quality ratings or boiler and ma-

chinery ratings, an increase in maximum feasible loss of 10% or any new recommendations with a



loss expectancy in excess of \$1 million. Other "red flags" include personnel changes that could affect an operation's safety, or an inspection that is more than 60 days overdue.

"The idea is to provide information for action," says Mr. Grimm. "New processes or expansion, productivity enhancement or new material can create new areas of concern, which must be pinpointed."

When changes are detected, the system recommends courses of action for loss control engineers, such as ordering an inspection or sending a message via electronic

mail, fax or letter to a customer. Those courses of action are monitored, along with any notes the engineer inputs directly.

The most important function of the system is reducing the time it takes to get and circulate information about changes in clients' risk environments, said Mr. Grimm. "Our inspections are tuning up new or changed data and Red Flag is analyzing it and making it accessible to us and our customers. Rather than waiting three weeks for paperwork, information can be back to the field office in a matter of hours."

The system does not automatically affect coverage or premiums. If clients have not addressed new risks come renewal time, though, premiums could be raised or coverage restricted.

Eventually Arkwright hopes to be able to compare its inspection data against industry trends in loss patterns and alert a company when it becomes vulnerable to emerging exposures.

See Arkwright on next page

"We can't do every house in a hurricane's path. That's why we also train insurers and local contractors in our school. The other thing we need to stress is that we can't warehouse the couple million dollars worth of raw materials it would take to do repairs after a hurricane. On that front, the insurers have to step in and have the equipment ready in the prone areas," Mr. Seraphin explained.

So far, Global Wrap has done work for Kemper, Aetna Casualty & Surety Co., Farmers Insurance Group Inc., and several other insurers. Some insurers, including The Travelers Insurance Group Inc. and United Services Automobile Assn., haven't used Global Wrap but say they would consider doing so.

Maryland Insurance Co., a Zurich Insurance Group unit, hasn't employed Mr. Seraphin yet, but Rich Carter, home office catastrophe coordinator in Irving, Texas, said that after taking part in a demonstration of Global Wrap's methods, he would call the company when the need arose.

"His technology has a lot of potential for the insurance industry, especially after a hurricane," said Mr. Carter. "If we can get an exposed dwelling covered and dried out, it lets us take time to pick the right contractor to do the repairs, which is important because there is generally a real shortage of good contractors after a disaster."

Tim Householder, associate property claims manager with Kemper National in Long Grove, Ill., said that Kemper is getting its money's worth from hiring Global Wrap.

"He's currently got a unique procedure to do something we've always done. So far he has performed as advertised. He says he'll cover things and they won't get wet. And they haven't," Mr. Householder said. But, he added, "others have also done it. He charges a premium price and at this point it's still too early to tell if his service is better and worth the higher price. It will take more time to see if he has built a better mousetrap."

But Mr. Seraphin insists that his technology is unequalled and he's also willing to be an advocate of the insurance industry when it comes to mitigating losses.

"You wouldn't believe the conflict we work under. The insurer wants us to cover the building as quickly and as securely as we can, while sometimes the owner wants to see damage as extensive as possible to increase the claim, especially in cases where business isn't going too good," Mr. Seraphin said. "We want to get in, do the job, and move on."

For more information, contact Global Wrap & Services Inc., 111 Park Drive, Montgomeryville, Pa. 18936; 1-800-645-6225 or 215-283-6077.

# Arkwright

*Continued from previous page*

Another tool that Arkwright will introduce is "Engineering Priorities," a system to help identify important engineering recommendations on reducing potential property losses, Mr. Grimm said. "One thing our system has done too well is provide a list of engineer recommendations," he said. "These lists have been comprehensive and exhaustive...but they have not recognized strategic context and budgetary constraints."

As a result, Arkwright will add a guidance option, which assigns weights to different factors and effectively lists recommendations in order of importance to a company.

It also plans to introduce in August a new, early warning system to alert customers to impending weather patterns. The "Nat Cat" System will link global weather trending systems with Arkwright's customer database.

When a major snowstorm or typhoon takes shape, the system's mapping tool identifies customer locations in the predicted path of the storm. The system extracts a list of contact names, locations, addresses and fax numbers and automatically faxes a letter to customers with property in the re-

gion that identifies the location likely to be affected.

"What's important is not the new information but providing information in such a timely way that it can help make better decisions," Mr. Grimm said.

Technology makes it possible for "Nat Cat" to tell a risk manager in Belgium that a major typhoon threatens his facility in Burma, which means risk managers can take necessary precautions.

Arkwright says it will have the new system up and running by August. With the aid of the Internet, Mr. Grimm hopes to utilize weather tracking services around the world to provide early warning information for flood, snow or freezing anywhere in the world.

The most wide-ranging and powerful of the new Arkwright tools is a system called ArkRisk, which allows a company to input risk management data and generate a wide variety of analyses and reports. It can be customized.

Arkwright is developing ArkRisk in a joint venture with a French software company called EffiSoft Ltd., which makes a system called GestRisk. Companies in France and England have been using Paris-based EffiSoft's GestRisk product since 1993.

ArkRisk marries the GestRisk software shell with Arkwright's

database, which provides a basis for comparison and analysis. The system is designed to help speed up the decision-making process and ensure that policyholders don't lose sight of risk management under competitive pressure.

GestRisk, developed by EffiSoft with the help of the French national risk management association, the Assn. pour le Management de Risque et des Assurances de l'Entreprise, or AMRAE, is available in five languages and can be modified for specific corporate terminology.

The system can handle and interpret data from a variety of sources. It is designed as a tool to manage not only property programs but also product and employer liability coverages.

"While a number of products exist for the workers compensation field, this is one of the few analytical software programs that addresses a wide range of exposures," Mr. Grimm said.

"Massive databases, better collection methods, better software, couldn't come at a better time," says Roy Mahlstedt, senior account executive at Arkwright International GmbH in Frankfurt, Germany. "Today we have any number of new and frequently unexpected exposures brought about by new materials and processes and by changes in political and social values." BI

# GUS

*Continued from page 20D*

• California brush fire. ISO's system verifies whether a property risk is within a hazardous fire zone.

ISO plans to add other services to GUS in the future, including earthquake risk, hurricane loss estimation and environmental hazard.

The information contained in GUS comes from various sources, and is updated continually. Data-Map was subsequently acquired by VISTA Information Solutions Inc. of San Diego. ISO currently contracts with: Risk Management Solutions Inc. of San Francisco for windstorm and quake data; and CAP Index Inc. of King of Prussia, Pa., for crime data.

About 105 property/casualty companies currently use the system, many of them among the

largest in the country. Subscribers include Aetna Life & Casualty Co., Allstate Insurance Co., CIGNA Property & Casualty Co., Farmers Insurance Group, General Reinsurance Corp., St. Paul Fire & Marine Insurance Co., Travelers Insurance Co. and USF&G Corp.

GUS is available through ISO's ISOTEL online network or ISO's Entree software. There are no special computer system requirements to run GUS. The cost includes an access fee and varies based on usage. ISO bills subscribers insurers only for the data options they choose in evaluating a given risk. Discounts are available for high-volume use, and batch processing for bulk information is available.

For more information on GUS or ISOTEL, contact the Insurance Services Office Inc., 7 World Trade Center, New York, N.Y. 10048-1199; 800-888-4476. BI

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April 10 ..... March 29

May 29 ..... May 17

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October 2 ..... September 20

November 6 ..... October 25

# Insurers' SIUs evolving with the times

By Bill Kizorek

**A** RECENT STUDY by the California Workers' Compensation Institute is making its way like wildfire through the claim departments of U.S. insurers.

Of 11,785 fraud cases referred to prosecution, there were 251 arrests and 110 convictions, the CWCI study found. In the months ahead, some tough questions might be asked about these results.

Considering that the 11,785 cases were probably the most blatant and convincing examples of insurance fraud, one might expect a higher number of convictions. A rough calculation indicates that less than 1% of these potential crooks were actually found to be criminals.

Although the study might shock those who had expected a much greater conviction rate, it does reinforce some important thoughts about the most appropriate role of special investigative units: to not only evaluate questionable claims for prosecution but also to review files for problems that could reduce indemnity payouts.

There are some harsh realities that explain why the conviction rate in the CWCI study was not higher. One is that there are already about 1.5 million Americans in jail.

Another is that insurance fraud has not captured the attention of some prosecutors. Although claimants and some health care providers have engaged in criminal activity that has seriously affected many businesses, as well as the

## IT Perspective

economy in general, the impact has not been so traumatic as to motivate district attorneys throughout the states to devote significant resources or interest to the problem.

Do not expect this attitude to change significantly in the near future.

As a result, the longevity and effectiveness of an insurance company SIU team should not hinge so much on the number of criminal prosecutions they are able to come up with, but on their contribution to the overall claims evaluation process.

If an SIU has a budget of \$300,000 and puts a couple of people in jail, that department might have difficulty justifying its existence at the turn of the century. But, if there are successful prosecutions, coupled with savings of several million dollars of reduced indemnity payouts on other cases reviewed by the SIU, there is a much greater chance that its funding will be fiscally justified.

The proliferation of special investigative units is the most significant change to insurance claims handling in the United States since the transition from street adjuster to telephone claims handler. There is no question that, when properly funded and managed, SIU staffers can create considerable value for an insurer.

Important questions for insurers, therefore, include: What is the role of the SIU? What is expected of its people? Where do they come from? How will they assist the claims

adjuster?

In my book "SIU 101," I address some of these issues (*IT*, Oct. 17, 1994). According to Scott Finger, co-author of the book, "the SIU investigator can use his or her expertise through this process, counseling the adjuster in what is believed to be the best way to handle the file. This continuous interface will result not only in a claims adjuster more aware of insurance fraud and the steps needed to ensure a proper investigation, but also a claims adjuster who is more likely to increase the volume of referrals to the SIU."

Prior to the book's publication, about 40 advance copies were sent out for comment. One comment in particular was from an executive of the International Assn. of Special Investigative Units, who said that a few of the IASIU members were offended by some of the ways the book portrayed special investigative units. One such illustration, for example, showed an SIU staffer with a gun, handcuffs and a billy club attached to his belt.

After having a long discussion about the potentially offensive sections of the book, and seeing the need to continue to reinforce the value of SIUs in general, two illustrations as well as a page of text were removed. New copy stressed the importance of SIU investigator/claims adjuster relationships.

The insurance industry also should be alert to the image of SIUs.

It was Mahatma Gandhi who said, "The world contains enough for every man's needs, but not enough for every man's greed." We know that thorough SIU investigations are a critical

component in making certain that greedy individuals with bogus claims do not succeed in sucking money out of the pockets of good-willed policyholders.

It is also true that selected prosecutions, especially when covered by the media, can teach the public that insurance fraud costs all of us.

What is needed, therefore, is a continued refinement of the role that special investigative units play within the insurance company claim department.

This can be done by continually reinforcing the proposition that investigative units coordinate their efforts with the claims department to make certain that the indemnity dollar savings are maximized, and that the SIU is not given poor grades just because of a scarcity of original convictions.

To accomplish this, there certainly will be some cultural readjustment in the years to come.

Many of those chosen to staff special investigative units come from law enforcement backgrounds, which may account for why many SIUs are focusing so much on obtaining prosecutions.

Assignments coming our way from SIUs used to always involve finding out the level of disability of a claimant. More and more, though, surveillance assignments coming in are dedicated to potentially prosecuting a claimant, with less emphasis on the overall claim evaluation process.

Preparing a criminal case for prosecution is very time-consuming, which limits the investigator's ability to look at a larger volume of claims files for potential savings. This emphasis is mildly distressing, especially when taken in light of the CWCI study.

As a result, we have seen a tremendous increase in much more limited surveillances. SIU investigators used to watch claimants for 10 to 12 hours, but now more surveillances are only four hours in the morning—or just long enough to see whether a claimant is going to another place of employment. When we suggest that the investigator calling in the case might be interested in physical activities the claimant may do late in the morning or throughout the afternoon, the response is that there is not as much interest anymore in the "extent of physical activity."

Instead, more interest is often placed upon documentation of specific activities that could lead to prosecution for claims fraud. One problem here is that so many claimants continue to collect disability benefits and insurers may be losing out on

the type of evidence they had used earlier to mitigate false claims.

Previously, all of our work would come from the claims handler whose mission was to evaluate the claimant in its entirety. Now, more work is being funneled through investigators within the claim department whose interest, at times, seem significantly narrowed to the criminal prosecution quest.

Again, a quote from "SIU 101": "The majority of claimants are honest. Insurance fraud investigators should not be frustrated because only a small percentage of investigations reveal criminally fraudulent behavior or result in a prosecution.

"Keep in mind that the investigative efforts of special investigative unit personnel more often than not result in information showing that a claimant has exaggerated some portion of the claim. The savings in indemnity dollars by not paying out on a bogus claim may help to fund future fraud investigations."

Where will SIUs be by the year 2000? I hope there will be the type of equilibrium that insurers are seeking. After thousands of prosecutions for insurance fraud, I predict consumers will be more honest when they submit their claims. Those companies that will have chosen the SIU path will have already done so, and the SIUs that will still be in place will be those that have shown their overall value not only in educating society but also in reinforcing the mission of the claim department as well as helping guard the bottom line of the insurance company. **BI**

Bill Kizorek is president of InPhoto Surveillance in Naperville, Ill.

He has written seven books on insurance-related topics, including "SIU 101."



## IT Briefs

### Maatman fellowship

WORCESTER, Mass.—Worcester Polytechnic Institute recently established an insurance fellowship in honor of a retired insurance executive known for his commitment to fire safety.

The Gerald L. Maatman Fellowship in Fire Protection Engineering, honoring the recently retired chairman and chief executive officer of Kemper National Insurance Cos., provides an annual stipend of \$5,000 to an outstanding student in WPI's graduate fire protection engineering program.

Mr. Maatman, an executive at Long Grove, Ill.-based Kemper National for 29 years, is a former chairman of the fire protection engineering department at the Illinois Institute of Technology.

Worcester Polytechnic Institute offers a program in post-graduate fire protection engineering, fire research and technology transfer. WPI offers bachelor's and master's

degrees and doctorates in fire protection engineering.

For more information, contact the Center for Firesafety Studies, Worcester Polytechnic Institute, 100 Institute road, Worcester, Mass. 01609; 508-831-5593.

### Officers elected

SAN ANTONIO—The Insurers Public Relations Council recently elected four officers.

Jean B. Lawyer, director-corporate communications at Country Mutual Insurance Co. in Bloomington, Ill., was elected president of the San Antonio-based IPRC.

The other officers are: Keith Lane, vp/manager-corporate communications at Erie Insurance Group in Erie, Pa., elected vp; Joan Bianco, communications director at Crum & Forster Insurance Co. in Parsippany, N.J., secretary; and George W. Tye, vp-corporate communications at United Services Automobile Assn. in San Antonio, treasurer.

The Insurers Public Relations

Council was established in 1973 to improve public relations and communication within the property/casualty industry.

### Charitable Fund

SAN FRANCISCO—The Insurance Industry Charitable Fund has raised about \$100,000 so far in 1995.

San Francisco-based IICF provides funds for disaster preparedness and relief and to Northern California organizations serving children and youths, the poor, the disabled and senior citizens. The IICF also supports organizations that promote conservation, health care and research, education and the arts.

IICF supporters include insurers, agents and brokers and professional organizations.

For more information or to contribute, contact the Insurance Industry Charitable Fund, 1 Embarcadero Center, Suite 400, San Francisco, Calif. 94111; 510-935-7695. **BI**

## Insurer Topics

# ADVERTISER INDEX

### Issue of June 19

ADVERTISER	PAGE #
Business Insurance .....	20E
International Bus. Forum .....	20C
Global Focus .....	20G
Lecor, Inc. ....	20G
Scudder Ins. Asset Mgmt. ....	20B

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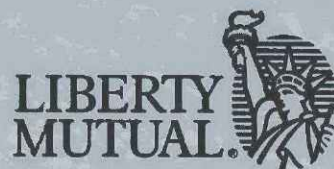
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Case Manager, Camden County Board of Social Services

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# Controlling product liability exposure

This question and answer is drawn from the Associate in Risk Management designation's curriculum, awarded by the Insurance Institute of America. They represent the types of questions asked on, and possible answers to, the three examinations for the ARM designation.

**Q:** Destiny Airlines is the primary customer of Aunt Melinda's Cookie Co. Aunt Melinda's provides Destiny with a weekly average of 50,000 individually wrapped chocolate chip cookies that are served to Destiny's passengers with their meals. Aunt Melinda's owns one bakery, and it is located in the city that is the major midwestern hub of Destiny's system of flight routes. Twenty employees work at the bakery. A company hired by Destiny picks up cookies three times a week for wrapping and delivery to the airport. Cookies are sent weekly aboard Destiny's planes to other hubs throughout Destiny's international flight system.

Aunt Melinda's was founded five years ago as a three-woman partnership to market locally the cookies that each partner baked in her own home. The company expanded dramatically when a senior executive of Destiny Airlines happened to purchase a package of Aunt Melinda's cookies and convinced Destiny's food service department to contract with Aunt Melinda's Cookie Co. to supply all of Destiny's in-flight cookie needs. The partners, recognizing that they could lose the contract with Destiny as quickly as they won it, are seeking to broaden their customer base. For this purpose, the advertising on every cookie wrapper gives a telephone number that Destiny passengers may call to order more cookies.

One of the partners is very concerned that some Destiny Airlines' passengers could become sick after eating Aunt Melinda's cookies. The cookie company does not have control over its products after they leave its bakery, and lawsuits could stem from conditions for which the cookie company is not responsible. The cookie company asked Destiny Airlines to hold it harmless from any liability claims, but the Destiny Airlines' legal department refused.

A. Aunt Melinda's Cookie Co. could suffer a substantial net income loss if Destiny Airlines' fleet were grounded or if its contract with the airlines were canceled. Describe in detail how the three partners who own Aunt Melinda's Cookie Co. should estimate each of the following:

1. The severity of the net income loss to their company if Destiny Airlines' fleet were grounded for two months.
2. The effect of losing Destiny Airlines' account.

## ARM Exercises

B. Aunt Melinda's Cookie Co. also could suffer a major net income loss if a fire damaged either or both of the large ovens in its bakery. Describe how the company could use each of five risk management techniques to protect its net income from loss due to such a fire.

C. Describe how Aunt Melinda's Cookie Co. could apply each of four risk management techniques, other than hold harmless agreements, to protect itself against product liability claims from Destiny Airlines' passengers.

D. Is Destiny Airlines' refusal to enter into a hold harmless agreement good risk management for Destiny Airlines? Justify your answer.

E. Destiny Airlines maintains a risk management information system for its major loss exposures and all of its claims. Would any of the information in Destiny's RMIS be useful to Aunt Melinda's Cookie Co. in managing any of Aunt Melinda's loss exposures? Justify your answer.

**A:** 1. If losing Destiny's account would not force Aunt Melinda's Cookie Co. to close permanently, an appropriate procedure for estimating the resulting net income loss for these two months would be first to determine the portions of Aunt Melinda's revenues and expenses attributable to the Destiny account in order to estimate the loss of net income revenues less expense to Aunt Melinda's for each day of the two months' shutdown.

The next step would be to estimate any additional expenses Aunt Melinda's would incur each day during this period. Aunt Melinda's daily net income loss would be the reduction in the company's daily net profit plus the company's daily additional expenses during the shutdown. This estimated net income loss could be adjusted downward if Aunt Melinda's is able to stockpile cookies for Destiny to use when it resumes flying.

On the other hand, the net income loss might be greater if Aunt Melinda's needed extra time to resume normal operations after Destiny begins flying again.

A. 2. Permanently losing the Destiny account would leave Aunt Melinda's with only the revenues and expenses attributable to other customers. Loss of Destiny might force Aunt Melinda's to close, causing loss of the entire value of the enterprise.

- B. Possible risk management techniques are:
- Loss prevention: Stop bakery fires, perhaps by producing some dessert that requires less heat during preparation.
  - Loss reduction: Hasten resumption of normal operations.
  - Separation of exposure units: Open more bakeries in widely separated cities.
  - Contractual transfer of risk control: Subcontract baking operations with the requirements that subcontractors deliver to the packaging firm.
  - Retention: Maintain operations, in temporary substitute facilities if necessary, by drawing on Aunt Melinda's retained earnings.
  - Insurance: Purchase business interruption insurance covering fire damage.

C. Four risk management techniques might include:

- Aunt Melinda's could practice loss prevention through more careful manufacturing and distribution of its cookies.

- The company could practice loss reduction by practicing good claims management to reduce the average cost of each claim.
- Aunt Melinda's could retain losses through funded reserves by establishing appropriate reserves for private liability claims.
- The company also could insure by purchasing adequate product liability insurance.

D. It is probably not good risk management for Destiny to refuse a hold harmless agreement to Aunt Melinda's. Destiny is in a better position than Aunt Melinda's to control liability losses and to pay claimants.

E. Yes, much of Destiny's RMIS data could be useful to Aunt Melinda's. For example, Destiny's projections of passenger numbers would help Aunt Melinda's forecast its net income loss exposures. And, knowing the conditions and lengths of time cookies might be stored at Destiny terminals would help Aunt Melinda's determine how to best package its cookies to keep them wholesome. **B**

The sample questions and answers used in this column are taken from the Associate in Risk Management designation curriculum of the IIA.

For more information on the content of the ARM program, write Dr. George L. Head, Vp, Insurance Institute of America, 720 Providence Road, P.O. Box 316, Malvern, Pa. 19355-0716, or telephone the IIA at 800-644-2101.

# The complex calculations of risk management

"Risk-Based Management: A Reliability-Centered Approach"

By Richard B. Jones

Published by Gulf Publishing Co., P.O. Box 2608, Houston, Texas, 77252-2608; 713-529-4301  
\$55.00

By Kevin M. Quinley

We have all heard the adage, "You can't judge a book by its cover." Add to that a corollary, "You can't judge a book by its title." Just because a book title contains the word "risk" doesn't necessarily mean that it is a useful tool for insurance and risk managers.

Case in point: a new release from Gulf Publishing and author Richard Jones, "Risk-Based Management: A Reliability-Centered Approach." Trimming risk means saving lives, time and money. This book attempts to show how to successfully manage and significantly reduce risks inherent in all managerial and industrial endeavors. Based on the principles of reliability-centered maintenance, the book tackles the concerns of assessing, quantifying and managing risk in a variety of real-life situations.

Author Richard Jones, Ph.D., has spent over a decade applying risk analysis techniques to a wide variety of

## Books & Ideas

industrial and business problems. He currently formulates risk-based strategies in loss prevention and benchmarking for Hartford Steam Boiler Inspection & Insurance Co.

One theme that emerges very clearly in this rather technical book is that risk reduction is a complex exercise in balancing the constant demands of equipment, personnel, production and service. Packed with figures, tables, charts, exhibits and references, this book may find a more suitable home on the bookshelves of engineers, which may be more its target audience.

One caveat: The text is heavy sledding, weighted with some rather turgid quantitative formulae. The chapter on "Responsible Statistics" takes the reader through linear regression and contains some demanding material that may daunt all but the most hard-core "quants." This is not a text for new risk managers, and even seasoned risk professionals may have a tough time slogging through to find the practical applications.

Packed with mathematics, statistics and forbidding formulae, "Risk-Based Management" may evoke pleasurable memories of high school calculus, or of a

particularly scintillating college trigonometry course.

Readers may fare better taking somewhat of a "buffet" approach. While much of the text is impenetrable to all but the most mathematically inclined, some chapters may be more accessible, such as Chapter 8, "On the Nature of Risk"; Chapter 10, "Operational Risk Management"; and Chapter 11, "People: The Newest Measure in Risk." Otherwise, the material is very humbling.

"As long as there are pop quizzes in math," one pundit observed, "there will always be prayer in schools." "Risk-Based Management," in its highly mathematical approach to risk analysis, may evoke some of that anxiety. Sifting through the engineering approach, however, readers and risk managers may garner insights which help improve safety and trim their overall cost of risk. **B**



Kevin M. Quinley is vp of risk services for MEDMARC Insurance Co. Inc. and subsidiary Hamilton Resources Corp., both of Fairfax, Va. Mr. Quinley holds the Chartered Property & Casualty Underwriter and Associate in Risk Management designations.

# New liabilities threaten public officials

By RODD ZOLKOS

SEATTLE—With no industry standard for public officials liability policies and numerous possible exposures, public entity risk managers need to look closely at their insurance to make sure officials are covered adequately.

And public officials liability coverage is taking on added importance, according to Cheryl L. Duryea, a partner at the Lane Powell Spears Lubersky law firm and general counsel to the Washington Governmental Entity Pool, both in Olympia, Wash.

"Public officials liability is a growing and developing area of the law," Ms. Duryea said earlier this month as part of a panel on "Public Officials Liability: What's Covered, What's Not" at the annual Public Risk Management Assn. conference.

Ms. Duryea said she believes the increased exposure of public officials isn't simply a matter of public entities' perceived deep pockets, but also involves a growing anti-government sentiment in the country.

## Adequately covering possible exposures can be tricky

"This translates, I think, into juries being inclined to think the very worst about public entities," Ms. Duryea said. The result is "there's a higher standard of care required of public officials but there is a lower standard of credibility afforded to them, for example, when they're on the witness stand."

Another panelist, John Crawford, executive director of the Olympia, Wash.-based Washington Counties Risk Pool, noted that Best's Municipal Underwriting Guide rates public officials liability at a 10 out of 10 on its hazard index. It also cites a laundry list of exposures officials face, including civil rights law violations, failure to follow legally mandated procedures, failure to file or maintain files, actions taken beyond the power of the office or failure to fulfill a duty of the office, and fraud or bad faith/gross abuse of discretion.

"How do you risk manage these things? You pretty much do the common sense things," said Mr. Crawford.

That, he said, includes putting

policies in writing, making sure minutes reflect exactly what was said and done at meetings, having legal counsel review all ordinances and administrative policies, defining public officials' duties so they understand the limits, following state due process requirements and avoiding negligence under state law.

As new areas of potential liability develop, there should be one person in the organization responsible for tracking the nature of the exposures, claims and litigation against the jurisdiction, what sort of information may be admissible in court and whether any of the risk can be transferred, Ms. Duryea said. "That person should be the general counsel."

"The personal vulnerability of elected officials is one of the major differences with other kinds of liability," Ms. Duryea said. "If the mayor says, 'You get me out of this and you get me out of this now,' how does that affect the settlement ability of your defense attorney?" The general counsel should be the one who can answer that question, she suggested.

Another reason that a general counsel should play the central role is that "most often, elected officials tend to listen to attorneys more than they listen to risk managers," she said. "Especially if their name's on a complaint that's been filed."

Ms. Duryea said it's also important that the general counsel and the defense counsel not be the same person, though the general counsel and the risk manager should get feedback from the defense counsel regarding "how you can take what they've done and prevent the same thing from happening again."

Carl Oswald, an assistant vp at Genesis Underwriting Management Co. in San Francisco, warned risk managers that his examination of numerous public officials liability policies showed there are frequently "gray areas" in coverage. A key gray area is what constitutes a "loss," he said. In some policies, the loss can be indemnity payments; in others, indemnity payments plus expenses; and still others, expenses only.

"In some cases, what appears to

be similar can be very dissimilar," Mr. Oswald said.

Different policies may also treat professional liability claims differently, he said. Some will exclude coverage of losses from claims made against attorneys, architects or engineers acting in a professional capacity or due to the rendering or failure to render professional services.

Some policies also will have exclusions related to claims involving employment practices and back pay.

However, there is one factor that will reassure public entity risk managers. "The thing to remember is that the duty to defend will be present in all the policies I saw if there is an allegation against the public entity," Mr. Oswald said.

He also told the risk managers that there are two things they should remember in reviewing insurance forms: "Don't just read the policy forms, compare them to others. Things are not always what they seem," Mr. Oswald said. And, "coverages and exclusions are not always staring you in the face. They may be hidden throughout the policy." **EI**

## Oklahoma

Continued from page 1

The panelists, who also included Harold Pumford, chief executive officer of the Oklahoma Municipal Assurance Group, and Aden Hogan Jr., assistant to the city manager of Oklahoma City, discussed the immediate response to the tragedy, the recovery effort over the days that followed and risk management lessons to be learned from the city's and state's experiences.

"Obviously, from the standpoint of risk management, things like this happen again," Mr. Zakariassen said. "It doesn't have to be a bomb explosion. It can be a tornado, a hurricane, whatever."

"As you grab your disaster plans, do you have a backup system?" he asked. "As you go back and start to review your plans, what can and will happen, check and see that you have a backup plan for everything."

"One thing we learned in Oklahoma City is you have to look beyond the traditional thinking for emergency operations and emergency response when you have a disaster of this magnitude," Mr. Hogan said.

The Oklahoma City bombing points out the necessity of planning for disaster, Mr. Hogan said. That includes having a plan for taking care of emergency response personnel and volunteers and the need for communication alternatives.

Today, many police communications take place over cellular phone systems, he said, but the huge volume of cellular call traffic immediately after the bombing overwhelmed the city's system.

"Our communications went down for the first hour-and-a-half or two hours of the event," Mr. Hogan said. "I would impress on you to have an alternate plan for communications."

Oklahoma City's problem was eased by help from Cellular One Inc., one of many companies to volunteer assistance with the recovery. Public entities' communication alternatives could involve some sort of advance agreement with local telecommunications companies for such assistance, Mr. Hogan said.

And the disaster plan also must address organizational concerns,

among them having someone clearly designated as "in charge" in the event of a catastrophe.

That said, often the success of the recovery depends on the ability of employees to respond appropriately before they receive guidance from their leaders, he said.

"Do what you can do to make sure your organization works well before you face a situation like that," Mr. Hogan said. "This kind of situation accentuates your strengths and weaknesses."

One critical decision made immediately following the bombing was by a fire company commander, Mr. Hogan said. "He directed his crew to work on putting out the fires rather than saving the victims," Mr. Hogan said. Even though survivors were calling from windows for help, "concentrating on putting out the fires probably saved three or

four blocks," the city official said.

Another such response stemmed from the memory of lessons learned from the 1981 Kansas City, Mo., Hyatt Regency Hotel skywalk collapse disaster, where emergency vehicle gridlock was blamed for a greater loss of life. With that in mind, Oklahoma City emergency crews kept streets clear, allowing rescue equipment to get in and out easily.

During the course of the recovery, local officials also paid considerable attention to protecting the safety of rescue workers entering the weakened structure, seeking to avoid any additional loss of life.

"The building moved continuously throughout the event," Mr. Hogan said. Often sections of what remained of the damaged building needed to be shored up before rescue teams were allowed to enter,

and a safety officer was assigned to each search and rescue team as it entered the building.

"Safety was a primary concern. We didn't want to lose the rescue teams," he said. "We simply would not put the rescuers at risk."

Over at the Journal Record building, Oklahoma's risk management department hired a private disaster recovery firm to help pack up and recover risk management documents and assets, and all state assets from the damaged offices were moved to a warehouse.

There Mr. Zakariassen's office established a security system, "not just to protect the assets of the state in the storage facility," he said. "We were having problems very early on from a mass influx of employees wanting to converge and go in and just get their stuff."

To alleviate confusion, the state

risk manager asked each department head for a list of people authorized to enter the warehouse and issued them photo IDs. "You're not denying any people access to their stuff, you're just setting up an organized system of going in and getting it," he said.

Mr. Zakariassen encouraged other risk managers to review their insurance contracts to make sure they don't have terrorism exclusions. The state's comprehensive all-risks policy with American International Group Inc.'s Commerce & Industry Insurance Co. unit does not, he said, and risk managers finding such exclusions in their coverage should ask to have them removed since many policies don't include them.

Based on the experience, Mr. Zakariassen's office has prepared "A Quick and Easy Guide for Disaster Recovery," which includes a list of suggested actions and management advice.

"I'm not proclaiming this the Bible on recovery," the state risk manager said. "But I do think it could help."

To prevent such incidents in the future, many people are recommending greater security at government buildings. Not Mr. Pumford.

"Most people are saying more security—restrict access to buildings. I think that is entirely the wrong way to go," Mr. Pumford said. "The warning we were given on April 19 is there is a large segment of our population that is alienated from mainstream society. The more we restrict government access, the more we're going to fuel that alienation."

"I tend to agree with Harold in a lot of respects. I don't know how you can plan or protect for this kind of thing," Mr. Hogan said. "But I could assure you everybody in Oklahoma City looks at things a little bit differently today."

Since the bombing, local officials have received many more reports of suspicious packages, abandoned vehicles and the like, Mr. Hogan said, and he thinks that kind of increased vigilance is key to minimizing potential damage.

"That's the message I would give your security people: Open your eyes up a little bit," he said. "Don't get complacent." **EI**

## Quick decisions key to managing a disaster

SEATTLE—The successful handling of a disaster like the bombing of the Alfred P. Murrah Federal Building in Oklahoma City requires a disaster plan, training the necessary personnel and sound management decisions, according to a consultant.

State and local officials who responded to the Oklahoma City disaster get high marks on their performance, according to Thomas T. Gillespie, a partner with Criminal Justice Training & Consulting Services in Santa Fe, N.M.

A key factor in the successful response in Oklahoma City was that emergency workers made the right decisions immediately after the bombing.

"The decisions that are made early on when an incident occurs often determine whether that incident will be managed successfully," Mr. Gillespie said at the Public Risk Management Assn.'s annual conference held in Seattle earlier this month.

"All too often what we see is that the person who is out there at two o'clock in the morning on a Sunday doesn't have a clue as to what our community's plans are," Mr. Gillespie said during a presentation titled "When Everything Goes Wrong: The Critical Incidents Process."

And for a manager responding to a crisis, "it's important that you make clear, decisive decisions when dealing with a critical incident," he said. "You don't have time for participatory management techniques."

Improving the odds that the right decisions will be made requires not just planning but training as well, Mr. Gillespie said, and the more realistic the training the better.

If done in a multiagency context, that kind of training also will make public officials more aware of the sorts of resources other departments might have that can be called upon in response to a crisis.

Mr. Gillespie cautioned that while disaster plans are necessary, they can't be seen as an end in themselves. He warned against "the Plan Syndrome," in which "there's some tendency to become complacent 'because we have a plan.'"

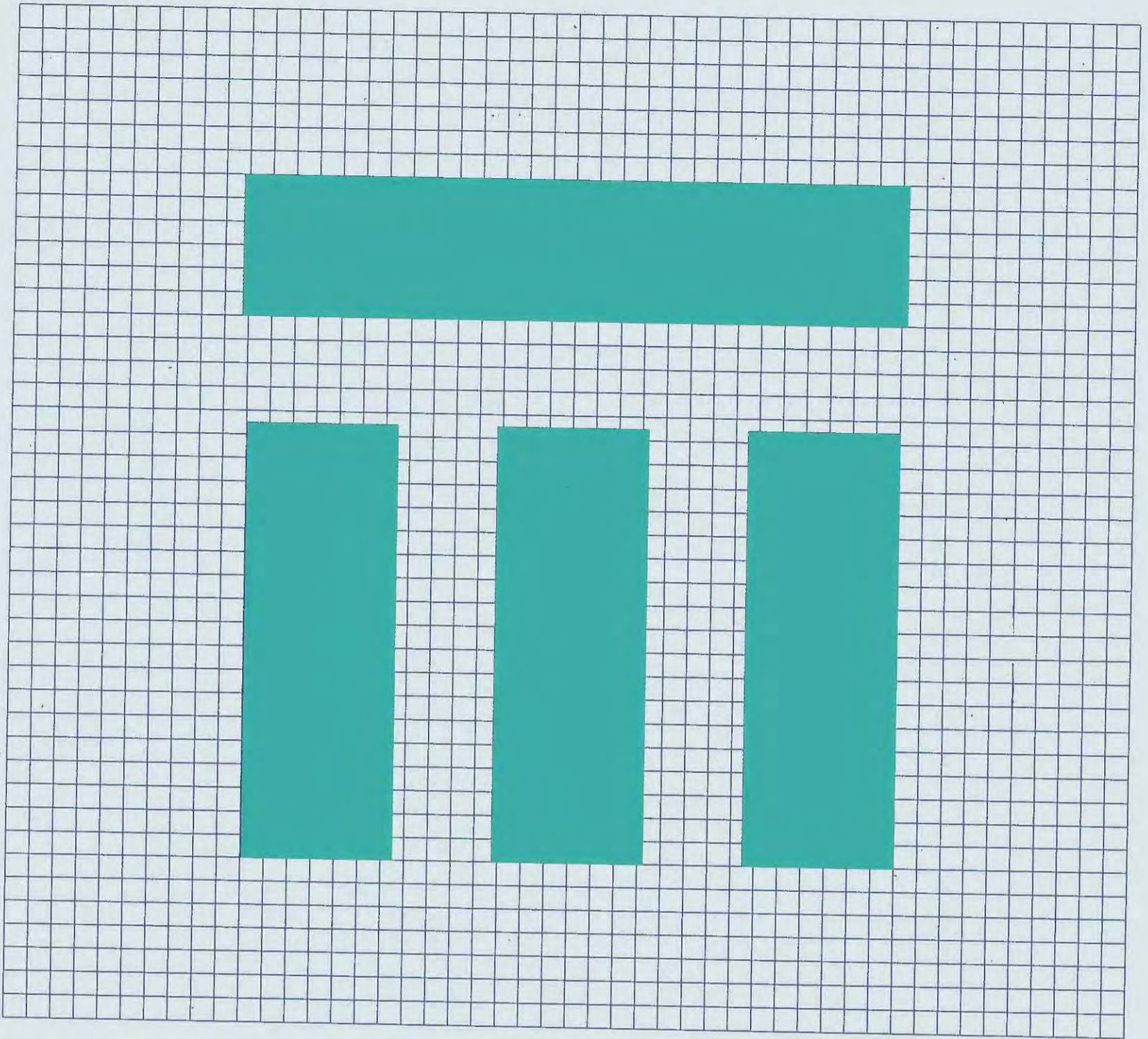
Risk managers should become involved in developing jurisdictions' disaster plans. "I would urge you to become involved simply because you have expertise (other officials) don't have," Mr. Gillespie said.

And once an incident has occurred, it's important to go back and see what can be learned from it, as officials in Oklahoma City have. "All too often we let incidents occur in our community and don't go back and talk about lessons learned," Mr. Gillespie said.

Public officials also should sit down with local news media managers to discuss critical incident response and develop some sort of media policy before a crisis occurs, Mr. Gillespie said.

News media demands will be considerable during a critical incident, and "No comment" is rarely a satisfactory response. Working out a policy in advance for crisis situations, however, can help ensure that the needs of the press are met in a way that doesn't interfere with the emergency response.

—By Rodd Zolkos



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# Managing risk in a political environment

By **RODD ZOLKOS**

SEATTLE—Government risk managers must understand the management style driving their entity's organization as well as the role politics play in the jurisdiction's management if they're to successfully advance their risk management agenda.

One important consideration is that the entity's senior management must take a macro view of the organization's operations. Senior management has little time for the details of each department, and the broad "perception is reality," said Aden Hogan Jr., assistant to the city manager of Oklahoma City.

Mr. Hogan, who spoke at the Public Risk Management Assn.'s annual conference held in Seattle June 4-7, has seen the issue from both sides. He was risk manager for the city before moving into his current position in the manager's office, and his current experience prompts him to liken managing an organization to a cattle drive.

"Some of the cattle require a little more attention than others, but the goal is to get them all to the end of the cattle drive," he said. "When I was a risk manager, risk management was the No. 1 priority to me. Now that I've moved into the manager's office, I still know risk management is there. It's still important to me, but I've got to look at all these other things."

"In this era of rightsizing, of

multiple job descriptions, it's important that you know risk management but that you also understand your organization," said Eugene Cornelius Jr., senior administrative officer for Redondo Beach, Calif.

And, with management ultimately answering to elected officials, the risk manager must understand the impact politics have on the process of running a public entity.

"The right business decision may not be, and often times is not, the correct political decision," Mr. Cornelius said.

"It's incredible the amount of time the political process takes," said Mr. Hogan, adding that Oklahoma City's manager "probably spends 90% to 95% of his time dealing with political issues," while the city's assistant managers deal with most of the operational matters.

That makes it necessary for the risk manager to choose carefully which battles are worth fighting, and to avoid crying "wolf," only bringing real "crises" to the top manager's attention, Mr. Hogan said. "Understand that if every time you go to senior management it's a 'crisis,' it's 'critical,' you're going to wear them out after a while. They're going to glaze over."

Given the multiple demands on the attentions of top management, it is "incredibly important" to build internal support for risk management programs, Mr. Hogan said.

"Spend some time trying to win the hearts and minds of the people you're trying to serve. Senior managers will perceive things differently if a few of your department heads are willing to throw their hats in there with you," he said.

Senior management is particularly interested in a risk manager

who is a team player today, Mr. Cornelius suggested, because public risk management in the 1990s involves educating people throughout the organization on risk management and selling them on the idea of implementing risk management concepts.

That kind of approach ultimately makes the risk manager's job easier, Mr. Hogan suggested. "You develop that support lower in the organization and your product gets pulled through the organization," he said. "You don't have to spend nearly as much time pushing it."

Mr. Hogan offered risk managers several "keys to positive risk manager perception by executive management." In addition to choosing battles carefully, they include: no surprises; flexibility and responsiveness; taking macro viewpoints; talking in big-picture terms but offering micro solutions with fallback positions if the manager doesn't agree; and offering options and alternatives that include "hooks" that give people in the organization incentives to implement the risk manager's program.

Another key Mr. Hogan suggested was to "be a student of public management." Risk managers without a formal management background should "take a course, read a book."

It's essential that risk managers understand their organization's management model and know how to blend their approach with that model, Mr. Hogan said. They also should understand where they fit in the organization and how that affects their ability to get their message across.

And, if risk managers haven't been reviewing their entities' annual statements and auditors' reports, they should, Mr. Hogan said. "The reports can tell you what's going on in your organization."

Risk managers also need to understand their jurisdictions' budgets. "You'd better understand how your organization finances itself and how its budget processes work," Mr. Hogan said. "That will give you clues as to how you can impact your organization."

He encouraged risk managers to keep any written material they present simple, to the point and jargon-free.

"I will not bring to the city council of Oklahoma City anything that's over two pages because they simply aren't going to read it," Mr. Hogan said.

Mr. Cornelius suggested the key skill for a risk manager in the '90s is the ability to make decisions, adding that upper managers are looking for risk managers to be willing to manage the processes that result from their decisions and to know whom those decisions will affect.

That requires the risk manager to understand the factors that influence the jurisdiction: federal and state legislation, public interest, economics, city management style and human resource issues, such as staff size and expertise.

In making decisions, Mr. Cornelius said, the risk manager must consider the senior manager's opinion on the issue, any political impact the decision might have, the outcome of similar issues brought before the council previously, the decision's financial impact, whom it will most affect, what influence those affected may have on the organization and whether it's really a battle worth fighting. **BI**

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## ADVERTISER INDEX

### Issue of June 19

ADVERTISER	PAGE #
Acstar Insurance	40
Alexsis Incorporated	16-17
American Business Info.	33
American Re-Insurance Co.	14-15
Brownyard Group	28
Business Insurance	13
Carvill America, Inc.	33
Employers Reinsurance Corp.	26-27
Equipment Insurance Mgrs.	32
Fireman's Fund	20
General Accident Ins.	4
HIAA/Health Ins. Assoc.	28
Johnson & Higgins	10-11
Liberty Mutual	5,21
Lindsey Morden	12
Met Disability	9
Minet Inc.	7
Olsten Kimberly Qualitycare	22
Practical Risk Management	12
Right Rx, The	32
RLI Corp.	36
Sherwood Insurance	6
Swiss Re America	25
Tempest Re	18-19
Zurich Prof. Liability	30

# Pensions

Continued from page 3

Under Internal Revenue Service rules, non-highly compensated employees can contribute as much as they like to 401(k) plans—subject to any limits imposed by their employers and the annual IRS maximum 401(k) plan deferral limit, which is now \$9,240. Highly compensated employees, though, often cannot make the maximum contribution because of other IRS rules that limit their contributions if rank-and-file employees make relatively small deferrals.

- Change the so-called corrective distribution rules, which govern the return of excess contributions to highly compensated employees when a 401(k) plan fails the non-discrimination tests.

Currently, corrections are made by returning excess contributions to employees, beginning with those who have deferred the highest percentage of pay.

That method, the administration notes, "illogically" favors the privileged few: the most highly paid of the highly compensated employees.

That is because contributions of that elite group—as a percentage of pay—are likely to be lower than the percentage contributions of lower-paid highly compensated

employees, even if the dollar contributions are higher.

For example, take the case of an employee earning \$67,000 who contributes \$5,000, which is 7.5% of pay. His contribution would be reduced before that of an employee earning \$150,000 who contributes \$9,000, which is 6% of pay.

The administration, by contrast, would require excess contributions to be distributed first to those highly compensated employees who deferred the highest dollar amount for the year.

The administration also proposes repealing the so-called family aggregation rule, which now can reduce pension benefits and contributions of an employee who owns at least 5% of a company's stock, or is one of a company's 10 highest-paid employees, and who has a family member, such as a spouse, who also works at the same company.

Under this rule, compensation of family members working for the same company is aggregated when determining pension benefits and contributions—even if only one of the individuals is in the 5% shareholder category or is one of the 10 highest-paid employees.

Take the case of a family where the husband earns \$150,000 a year and is one of the 10 highest-paid

employees and the wife earns \$50,000. Under tax law, only the first \$150,000 of an employee's compensation can be considered in calculating pension benefits and contributions. Because of the family aggregation rule, even though the husband and wife had \$200,000 in compensation, only \$150,000 of compensation would be considered in determining pension benefits and calculations.

## Many other parts of the administration's pension proposal are virtually the same as those in earlier simplification packages.

The administration characterizes that result as unfair.

Many other parts of the administration's pension proposal are identical or virtually the same as those in earlier simplification packages considered by Congress. Those include:

- Prior-year testing. Employers running the 401(k) non-discrimination test would have the option of comparing the deferrals made by lower-paid employees during the previous year to contributions made by higher-paid employees

during the current year.

IRS rules now require employers to compare current-year contributions of the two groups. This requires employers to monitor constantly the contributions of the two groups.

If lower-paid employees do not contribute as much as expected, employers in mid-year may have to go through the trouble of cutting back on contributions by highly paid employees or returning excess contributions to those workers.

By using prior-year contributions by lower-paid employees, employers would know at the start of the plan year how much highly paid employees could contribute to the plan without failing the non-discrimination tests, noted Gerald Uslander, a principal with William M. Mercer Inc. in Washington.

- Safe harbors for 401(k) plans. Employers that beef up contributions to their 401(k) plans would not have to run non-discrimination tests.

The required contributions, though, are so rich that few employers would utilize them, benefit consultants say. One safe harbor, for example, would require employers to match 100% of employees' contributions up to the first 3% of compensation and match at least 50% of employees'

contributions between 3% and 5% of employee compensation.

That is far richer than the typical 401(k) plan design in which employers match 50% of employees' contributions up to the first 6% of employee pay.

Other provisions in the administration package would eliminate certain "half-year" requirements that govern the year that employees must make certain benefit decisions.

For example, employees generally now must be at least age 59½ to receive lump-sum pension distributions without being hit with special taxes; the administration proposal would round off this age requirement to 59.

In addition, the package would require multiemployer pension plans to use the same fast vesting schedules—typically five-year cliff vesting for defined benefit plans and seven-year graded schedules for defined contribution plans—that single-employer plans now use. Under current law, multiemployer plans can use a 10-year vesting schedule.

The package also would allow tax-exempt organizations to establish 401(k) plans and—down the road—set up electronic filing of Form 5500, the annual benefit plan financial report employers file each year with the government. BI

# NAIC

Continued from page 3

element in the nationally required annual statement blank.

State insurance regulators also repeatedly criticized the NCOIL committee's analysis of accreditation problems faced by both Texas and New York, which the NAIC argues stemmed from different factual situations. For example, Texas' accreditation recently was affirmed after the NAIC granted it an extension to pass a needed law on the reporting of extraordi-

nary dividends. In the interim, the Texas insurance commissioner implemented a reporting program to essentially meet the requirement's goals.

The NAIC also criticized state legislators for holding closed party caucuses. In addition, the NAIC pointed out that many parties have a role in making laws, including constituents and governors.

NCOIL welcomed the response and is considering some of the regulators' comments.

"It's a good response. It will contribute to the dialogue be-

tween state insurance legislators and the NAIC," said Robert Mackin, NCOIL's executive director.

He currently is reviewing the brief and said he may recommend that the committee amend some of its findings before formal adoption by the NCOIL Executive Committee.

The NAIC also appears to be adopting a conciliatory approach.

"This response in no way alters the intention of the NAIC to seek to achieve unity once again with NCOIL on the accreditation program and other NAIC initiatives," said NAIC President Lee Douglass, who is the insurance commissioner from Arkansas.

The NAIC also took several other actions at its recent summer national meeting.

- Regulators discussed recent developments involving Lloyd's of London in closed sessions and individually but did not hold open discussions focusing on either Lloyd's new plan or its agreement with the New York Insurance Department to restructure its U.S. trust funds (BI, May 29).

Louisiana Insurance Commissioner James H. Brown, chairman of the NAIC's Surplus Lines Task

Force, said his state is analyzing the agreement, in part to determine whether the NAIC should get involved in a national response to the situation.

- The Accident and Health Insurance Committee recommended that the NAIC membership vote in September to formally adopt three, health-related model laws.

The Off-Label Drug Use Model Act would apply when a drug prescribed for one condition also is used to alleviate another condition. The model act would require "a health benefit plan that provides coverage for drugs to provide coverage for any drug prescribed to treat any covered condition so long as the drug has been approved by the Federal Drug Administration for that condition."

The proposed act also sets standards for payment or reimbursement of costs associated with prescription drugs.

"Denial of payment or reimbursement for off-label drug use can interrupt, or effectively deny access to, necessary and appropriate treatment for persons being treated for life-threatening illnesses," noted Mr. Douglass of the NAIC.

In addition, the committee also is recommending that the NAIC adopt in September the Stop-Loss Insurance Model Act.

The act clarifies the definition of stop-loss insurance in order to help regulators clamp down on insurance companies that are selling stop-loss policies that circumvent state health insurance regulations.

The committee also is recommending the NAIC adopt the Private Health Care Voluntary Purchasing Alliance Model Act, which contains guidelines for establishing competitive purchasing groups to help small employers obtain economical health care coverage.

- A working group codifying statutory accounting principles responded to criticism about its closed-door deliberations by agreeing to disclose more information about the status of its project at quarterly meetings and provide more opportunities for public comment.

- Illinois regulators agreed to redraft a proposal for an interstate compact for regulation of non-U.S. insurers to meet criticisms that the draft was unworkable. BI

## Business Insurance

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# Vermont

Continued from page 3

the accreditation process, he said.

While Vermont's accreditation could take some wind out of the sails of accreditation reform, Mr. Harkavy said interests outside the alternative market also have begun to take issue with the accreditation process, and their efforts to reform the NAIC accreditation process will continue.

He cited the move by some states to follow Vermont's lead in considering legislation aimed at giving the states oversight of the NAIC (BI, April 24; Jan. 30), the report by the National Conference of Insurance Legislators taking the NAIC to task over various issues (BI, March 3) and moves by newer NAIC members to reform various aspects of the way the organization does business (BI

March 20) as encouraging signs to those seeking accreditation reform.

"I'm taking a great deal of comfort in not only the state legislators rebelling (against the NAIC), but also some of the state commis-

## Recent moves at the NAIC show the organization is moving the right way, says John Primmer.

sioners talking about boycotting," Mr. Harkavy said.

Even if Vermont is accredited, Mr. Primmer believes accreditation reform efforts will continue.

"I wouldn't think Vermont's accreditation will take off all of the

pressure that's on (the NAIC) to do everything right," he said. Besides ongoing issues related to the accreditation of states like New York and Texas, "there will be new issues coming along," Mr. Primmer said.

Mr. Salisbury agreed, saying the risk retention group question "is just one of the accreditation issues. There are lots of others bothering people."

The recent NCOIL report, for example, raised issues over "fundamental questions of who's in charge here," he said.

But Mr. Primmer said he does believe recent moves at the NAIC show the insurance commissioners' organization is moving the right way.

"It's a new wind blowing through the NAIC," he said. "And I think if they keep in that direction they will be doing everybody a lot of services." BI

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book at us.”**



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## Insured losses expected to be small from quake in Greece

By EDWIN UNSWORTH

ATHENS, Greece—As Greek rescue efforts continued following an earthquake about 90 miles northwest of Athens late last week, insurers said early indications are that insurance claims will be minor.

A spokeswoman in the Athens office of Munich Reinsurance Co., one of the major reinsurers in the area, said that consultations with insurers have shown that they "don't expect any serious insurance ramifications."

The quake, which struck at 3:16

a.m. local time June 15, measured 6.2 on the Richter scale. Its epicenter was undersea in the Gulf of Corinth. Although the shock was felt throughout Greece, the land area closest to the quake is mainly rural.

Two towns suffered damage—Aiyion and the small port of Eratini.

Early reports were of two badly damaged buildings, a 12-year-old apartment block and the Eliki Hotel, on the coast.

There were at least 14 deaths, mainly in the two buildings, though the Munich Re spokes-

woman said the death toll was expected to rise. Some guests at the hotel were still unaccounted for, including a number of French tourists.

The spokeswoman said the hotel was "probably insured" for earthquake damage.

The area affected by the quake is on a known fault line, which means some property owners also probably would have purchased earthquake insurance, the spokeswoman said.

However, Theodore Dritsas, an underwriter specializing in the Greek market for Swiss Reinsur-

ance Co. in Zurich, Switzerland, said there are also many older stone buildings in the affected area, for which insurers would not have provided coverage.

Mr. Dritsas said that while it is too early to be certain of the quake damage, "I don't think it's going to be much of a problem for us."

He pointed out that after an earthquake measuring 6.6 on the Richter scale hit the Kozami area of Greece on May 13, insurers received no claims.

The purchase of earthquake insurance, though uncommon in

Greece, is increasing since prices have fallen due to the Greek government's gradual elimination of high fixed insurance tariffs to conform to European Union regulations.

In fact, removal of the tariffs has considerably reduced the cost of many kinds of property/casualty insurance in Greece.

But, the Union of Greek Insurance Cos. is currently conducting a study to establish equitable earthquake premiums because its members believe rates have fallen too low with the abolition of the tariff. **BI**

## Consolidation, specialization seen as future of reinsurance

By STACY SHAPIRO

LONDON—The future of the global insurance and reinsurance business looks rosy to some in the market.

Executives predict that in 10 years, the insurance market will be dominated by a few large players looking for alternatives to standard reinsurance programs.

The London market will still be around, though if Lloyd's of London were to fail, the market would be a much weaker player, they say.

And the whole market will be dominated by the need to satisfy capital backers looking for adequate returns on their investments.

At least, that's the picture painted by market executives speaking to about 150 people at the Third International Reinsurance conference held in London June 7-8 and sponsored by DYP, Lloyd's of London Press Ltd.

While today there are thousands of small general insurance entities, "10 years from now, there will only be a few large global players in the marketplace," predicted Detlef Steiner, senior executive vp of Zurich Insurance Group in Zurich, Switzerland.

These future insurance companies working in a deregulated market will be much more specialized in certain market segments and will be focused on the needs of their customers, said Mr. Steiner. Today there are only a few of these types of insurers in the marketplace, but "they will outperform the industry," he said.

Reinsurance products—which may be different than they are today—will have to be tailored to these customers' needs, he added. These may be traditional reinsurance products or avant garde risk transfer products or a combination of both, he said.

The future will look quite different from today and will belong to the "specialized" reinsurer, agreed Herbert Haag, president and chief executive of Partner Reinsurance Co. in Bermuda, who has spent 24 years with Partner Re shareholder, Swiss Reinsurance Co.

The top 10 insurance groups worldwide already command 20% of the world's insurance premiums, said Mr. Haag. Of these, four are Japanese, three are U.S. companies, one is German and two are French, he said.

The global reinsurance market totals \$150 billion in premium, of which 29% is derived from the United States, 16% from Germany, 11% from the United Kingdom and 8% from Japan, he said. However, "this is the past. The future will look quite different."

Even in the reinsurance market, the concentration has continued and there will be fewer, larger global reinsurance groups, he predicted. Every reinsurer below the top 10 is up for sale, said Mr. Haag. "Bigger is better," he said, because the larger companies' capital bases are stronger.

Consolidation already has taken place in the United States, where the number of reinsurance companies fell to 54 in 1992 from 129 reinsurers in 1982. There also have been cross-border mergers, such as

See **Future** on page 33

## China's market likely to grow but at a continued slow pace

By MARIA KIELMAS

LONDON—The Chinese insurance market offers potentially some of the greatest growth opportunities worldwide, though its progress is likely to be slow.

The domestic insurance market has been undergoing a slow process of change for the last decade, with very limited openings for foreign insurers. In particular, fundamental problems remain with the legal system and insurance education. Furthermore, China's entire social security and welfare systems require radical changes.

These were the themes discussed at a conference sponsored by Sedgwick Group P.L.C. and a British publisher in London last month on the future of the Chinese insurance market. Delegates and speakers expressed concern that a proposed insurance law was being delayed seemingly indefinitely, though some said that they expected it to be approved before the end of the year.

However, long-term fears about the success or otherwise of China's experiment in a "social market economy" and the political fallout from the economic change remain.

Sir Percy Craddock, former British ambassador to China, said he views the future of China with "trepidation." The policy of economic growth within political obedience proposed by Deng Xiaoping, leader of the ruling Communist Party, has had some success but is a "brittle formula," said Sir Percy. He warned that a "semi-liberated economic system and a closed political system will create long-term problems for China."

Reform in the Chinese insurance sector is based on four measures, said Yang Wenyu, director of foreign financial institutions and the People's Bank of China. The measures are to:

- Provide and complete the legal framework for insurance.
- Reform insurance institutions and create a state reinsurance company.

- Separate the management of the insurance industry into life and non-life sectors.

- Encourage competition.

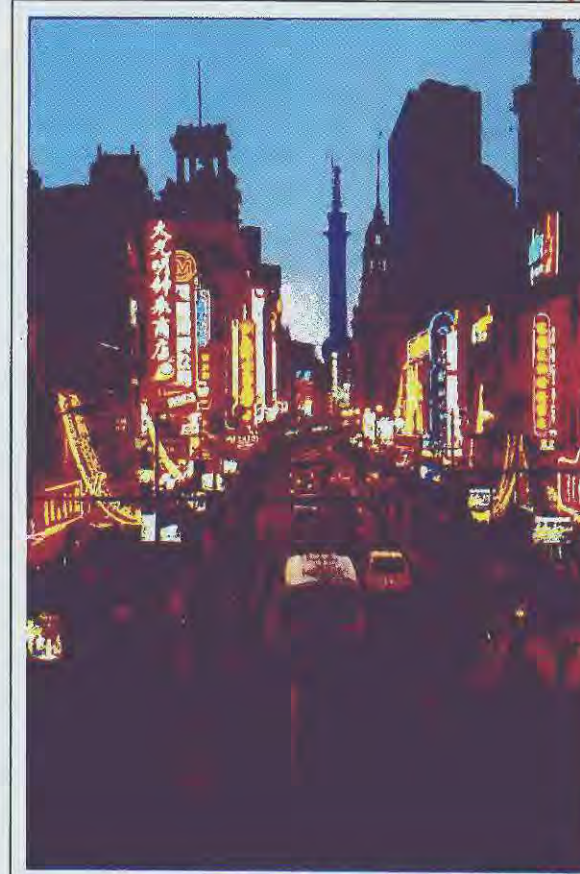
"China's insurance market in terms of its depth and width is still at the stage of the world insurance market in the 1950s and 1960s," Mr. Yang said. Up to the mid-1980s, the insurance market was a monopoly held by the People's Insurance Co. of China. Licensing of new companies since that time has meant that at the end of 1994 China had 28 insurance companies and an annual premium revenue of about 63 billion renminbi yuan (\$7.59 billion), which increased by 16.6% from 1993. The total sums insured in 1994 were 1.12 trillion yuan (\$132.6 billion), compared with 880 billion yuan (\$151.45 billion) in 1993.

The most important change of the last decade for foreign investors came in 1992 with the "Shanghai Interim Management Regulation for Foreign Insurance Institutions," or Shanghai Regulation, which permitted foreign insurance institutions to establish branches and joint venture insurance companies in China.

Also in 1992, American International Insurance Co., a division of American International Group Inc., set up a branch in Shanghai. In July 1994, another license was granted by the People's Bank to the Tokio Marine & Fire Insurance Co. Ltd., also for a branch in Shanghai.

As it stands, the regulation permits foreign institutions to open offices only in certain cities.

Insurance companies must run a representative office in China before they can apply for any operating license.



GRANT V. FAINT/THE IMAGE BANK

Foreign insurers and brokers hope to tap insurance opportunities in China through cities like Shanghai.

By the end of 1994, there were 71 representative offices of 43 foreign insurance institutions in China, representing 12 foreign countries.

"Frankly, since the insurance market has just taken shape in China, the management of the market, the operating mechanism, the intermediaries as well as the self-discipline of the participants in the market remain in their infancy," noted Shao Dang Di, director and executive.

See **China** on next page

## Studying U.K. insurance buyers

By STACY SHAPIRO

Anything one might want to know about the behavior and attitude of British insurance buyers can be found in a new study.

The three-part study, simply called "The Insurance Report" and based on responses from 1,500 consumers and 324 small businesses with fewer than 50 employees, reveals that in the non-life sector:

- Premium is the most important factor when purchasing insurance coverage,

### Price No. 1 concern

both for individual consumers and small businesses.

But, while 66% of small businesses think price is very important, about 61% also believe that comprehensive coverage is equally important.

- More than 70% of small businesses buy their policies through a commercial broker, while less than 10% purchase their coverage directly from an insurance company.

Buying insurance coverage through a

broker "is still a very dominant factor," explained Martin J. Henson, senior underwriter for Swiss Reinsurance Co. U.K. Ltd., which jointly conducted the study with market forecaster The Henley Centre in London.

However, nearly 30% of consumers in the United Kingdom in the survey now buy their non-life insurance directly on the telephone. Direct insurance selling via the telephone is taking Europe by storm following the success in the United Kingdom of "Directline," a service from

See **Buyers** on page 33

## INTERNATIONAL

# China

*Continued from previous page*  
 tive deputy general manager of the China Pacific Insurance Co. in Shanghai. "Since the insurance agent and broker system is not yet approved, the Chinese market is not well developed. Insurers cannot make decisions on funding operations autonomously, the Chinese people have a rather limited purchasing power for insurance products, and there is a marked shortage of insurance professionals," Ms. Shao added.

But all will not be roses when the

new insurance law is passed, warned Max Lewis, director of Sedgwick Payne Insurance Strategy in London. "It must be recognized that the proposed new insurance law is designed to control the insurance industry and, in particular, new entrants. It is not designed to encourage openness in the industry. It is well worth remembering Deng Xiaoping's comment on observing the open door policy that 'when you open the window, flies and mosquitoes come in.'"

Although there is no official English translation of the proposed law, Mr. Lewis said the main points will include the following:

- All insurance activities must abide by the law.
- Only licensed insurers and intermediaries may conduct insurance business, and insurance may only be purchased from licensed insurers and brokers.
- Concepts of "utmost good faith," insurable interest and disclosure of information is in the legislation, together with mechanisms for determining disputes, penalties and compensation.
- How and when claims must be notified to insurers.
- The circumstances under which insurance contracts may be canceled.
- The right to carry out risk management surveys and charge higher premiums if measures recommended are not carried out. The final draft is expected to spell out insurers' and policyholders' rights in this regard.
- A rule that only the central regulatory authorities can establish a new insurance company.
- Guidelines on obtaining a license.
- Investment guidelines. For example, 20% of capital must go into a special reserve fund.
- Procedures for terminating a license.
- Reinsurance purchasing guidelines. Attempts must be made to purchase reinsurance from Chinese companies. If the Chinese reinsurer cannot accept the business, or the

terms and conditions from overseas companies are "clearly better," then reinsurance can be arranged outside China.

• Rules governing agents and brokers and the types of records they must keep.

Mr. Lewis said a number of people will be unhappy with the new law, including, "Unlicensed insurers, many of whom are based in Hong Kong, who are carrying on the business of insurance in China; unlicensed intermediaries, some of whom are based in Hong Kong, who are carrying on the business of insurance in China; unlicensed intermediaries, some of whom are plac-

ing risks for Chinese clients with insurance companies outside of China; and non-licensed brokers, some of whom operate out of hotel rooms and some of whom accept premiums in cash, and who will be outlawed." All unlicensed activities will be outlawed.

The insurance laws of 16 countries were examined in the course of preparing the legislation, said Tim Freshwater, a partner in law firm Slaughter & May in London. Since the Chinese legal system was dismantled between 1954 and the late 1960s, it has been a massive task over the last 15 years to build up a new one. **BI**

## China think tank aims to aid in reforms

A fundamental change in economic and social security structures is necessary as China moves from a centrally managed economy to a socialist market economy.

With this in mind, Sedgwick Noble Lowndes is seeking funds to establish a foundation that will act as a think tank to formulate proposals for a new welfare system.

Sedgwick Noble Lowndes, the Memphis, Tenn.-based benefit consulting branch of Sedgwick P.L.C., now is fully licensed to operate in China and currently has offices in Beijing, Shanghai and Shenzhen.

The primary objective of the foundation, which does not yet have a name, is to formulate proposals for the future structure, financing, investment and regulatory framework within which employers could provide adequate support to employees in retirement, disability and unemployment, and in meeting the cost of health and medical services.

"There's no infrastructure in China to develop the provision of social benefits," said Peter Brew, group managing director-Americas and Asia Pacific of Sedgwick Noble Lowndes Ltd.

Sedgwick hopes the foundation

will help in forming such an infrastructure and eventually permit Sedgwick Group to conduct brokerage and employee benefits business in China, he said.

The benefit consulting branch will draw on the experience it has gained in the restructuring of the social security and pension system in Chile.

Sedgwick hopes to draw membership for the foundation from both domestic and foreign employers in China. It is canvassing members from the Chinese enterprises with which it has a business relationship and its multinational client base in Europe, North America and Asia Pacific.

To support the foundation's aims, Sedgwick will ask multinational corporations to contribute \$10,000 a year for three years as part of membership requirements, Mr. Brew said.

Sedgwick estimates the total costs of the foundation will be \$500,000 in the first year, but a more precise figure will be calculated when formal budgets are prepared for members.

Chris Leung, of Sedgwick Noble Lowndes' Hong Kong office, has been appointed full-time secretary of the foundation in China.

—By Maria Kielmas

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Scheme Creditors (as defined in the Schemes of Arrangement) may attend in person or they may appoint another person, whether a Scheme Creditor or not, as their proxy to attend in their place.

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## INTERNATIONAL

## Future

Continued from page 31  
those of Cologne Reinsurance Co. and General Reinsurance Corp., and Frankona Re and Employers Re.

Ceding companies in the future will realize that they only need to buy reinsurance to cover catastrophic exposures, be they property, liability or financially oriented, said Mr. Haag.

Brokers will act as consultants and "Lloyd's will survive, at least I hope so."

Already, buyers have changed their requirements, noted Dennis Mahoney, deputy chairman of Alexander Howden Group Ltd. No longer are other brokers Howden's major competitors.

"My biggest competition is my in-

sureds and reinsureds" who are increasingly taking higher retentions, he said.

Buyers, said Mr. Mahoney, want security and solvency in their underwriters; utmost good faith; stability of pricing; and adequate terms and conditions. They also continually complain that underwriters do not differentiate enough in pricing between the "bad risks and good risks," he said.

As for the underwriters and brokers of the future, Mr. Mahoney said, "either be large and global; or small and niche."

Nearly all of the executives during the two-day conference expressed the hope that Lloyd's would continue to exist in the future in some form.

"London without Lloyd's would be very much weaker," said Jim Bannister, chairman of consulting

firm Jim Bannister Developments Ltd. and former owner of DYP.

Lloyd's, for all its weaknesses, is still the only market of its kind in the world and "there is no serious

**'When you sit at a poker table and you don't know who the (sucker) is, it's you,' says Elvin Patrick.**

contender unless we give it to them," warned Mr. Bannister.

Most people in the London market say, "Yes, Lloyd's will survive," added Jerome Faure, managing director of French reinsurer SCOR (U.K.) Reinsurance Co. Ltd. in Lon-

don. But, then they pause and typically add, "One way or another."

If Lloyd's fails, there will be a tremendous impact on the rest of the London market, he predicted. "But the shock waves would go beyond London" and affect U.S. buyers especially, who would find it difficult to get claims paid, he predicted. Mr. Faure expressed hope that Lloyd's plan will succeed.

Lloyd's underwriter Elvin Patrick, chairman of Bankside Underwriting Agencies Ltd., warned that big is not always best.

Innovation comes from smaller players that are hungry, but "the problem is no one wants to do business with smaller players," said Mr. Patrick. If the London market ends up with "too few" and "too similar" larger players, then London will lose policyholder attraction.

Mr. Patrick also warned the fu-

ture reinsurance market: "When you sit at a poker table and you don't know who the mug (sucker) is, it's you. This applies to reinsurance."

In the past 20 years of dealing in insurance and reinsurance, there's been a "merry-go-round of mug-marks being taken to the cleaners," he said. Bermuda and captives got burned, then the Japanese insurance industry, then underwriting agencies in London acting for foreign companies, then managing general agents and then "famously and spectacularly, it was Lloyd's," said Mr. Patrick.

"So the big question is, 'Where is the mug market now?' The answer is, 'I don't know.'" However, reinsurers that work in a global market must make sure they aren't one of the next wave of suckers, Mr. Patrick said. **BI**

## Buyers

Continued from page 31  
the Royal Bank of Scotland that sells auto and homeowners insurance over the phone.

But, based on the research, it doesn't appear that small British businesses are ready to discontinue using brokers and start buying their insurance policies directly via telephone, said Paul Martin, marketing analyst with Swiss Re U.K.

Some insurers have investigated offering commercial insurance by phone, but "they haven't seen any mileage in it," added Stephen Riley, managing director of Swiss Re U.K.

• Small businesses are most worried about theft and 89% of those surveyed purchase property and business interruption policies. But 15% of buyers also feel that they could be at risk from a public or product liability claim in the next 12 months. Nearly

93% buy public and product liability insurance, while only 27% buy professional liability coverage.

The Swiss Re/Henley study also focuses on consumer attitudes toward the life insurance industry, which reveal some need for growth in the British employee

**Small British businesses aren't ready to discontinue using brokers, according to Paul Martin.**

benefits sector.

Most of those surveyed still believe the British government should have the main financial responsibility for all types of social benefits, from pension to medical care.

For example, 88% of those sur-

veyed feel the state should provide the finances for emergency hospital care, while only 3% think employers should.

The Swiss Re/Henley report notes, however, that the "role of the employer is changing rapidly" as the state tries to transfer social benefits to the private sector to ease the financial burden and as employees request more benefits.

A total of 56% of those surveyed, for example, would like their employers to offer private medical insurance and 83% want an employer-sponsored pension.

Research also shows that "70% of employees would be interested in buying a range of insurance covers via their employer through payroll deduction," the survey adds.

"The Insurance Report" is available for £175 (\$279) from Swiss Re's Marketing and Client Services Department; 011-44-171-623-3456; fax: 011-44-171-929-4282.

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**JUNE**

**JUNE 25-28. Benefit Plan Professionals Institute** in Steline, Nev., sponsored by the International Foundation of Employee Benefit Plans; \$685 for IFEBP members, \$775 for non-members. International Foundation of Employee Benefit Plans, Registrations Department, P.O. Box 69, Brookfield, Wis. 53008-0069; 414-786-6710 ext. 257.

**JUNE 25-28. Creating a World of Difference** annual conference and exposition in Orlando, Fla., sponsored by the Society for Human Resource Management; \$700 for SHRM members, \$900 for non-members. SHRM 95, P.O. Box 79482, Baltimore, Md. 21279-0482; 800-283-7476.

**JUNE 26-27. Annual Benefits Sympo-**

**sum 1995** in New York, sponsored by the International Business Forum; \$695 for plan sponsors and employee benefit or risk managers, \$1,095 for others. International Business Forum, 7 Penn Plaza, Suite 901, New York, N.Y. 10001; 212-279-2575.

**JUNE 26-27. Minimizing & Managing Credit Risk for OTC Derivatives** conference in New York, sponsored by the Institute for International Research; \$1,295. Conference Coordinator, Institute for International Research, 708 Third Ave., 4th Floor, New York, N.Y. 10017-4103; 800-345-8016.

**JUNE 26-27. Developing Outcomes Measures and Return-to-Work Guidelines** in New Orleans, sponsored by International Business Communications; \$1,195. IBC USA Conferences Inc., 225 Turnpike Road, Southborough, Mass. 01772-1749; 508-481-6400.

**JUNE 26-28. Analysis and Implemen-**

**tation of Ergonomic Solutions in Simulated Work Situations** workshop in Orlando, Fla., sponsored by Managed Health Resource Inc.; \$465. Also **July 20-22** in Las Vegas. Managed Health Resource Inc., 3417 Timberline, Eugene, Ore. 97405-1274; 503-484-5853.

**JUNE 26-30. Environmental Litigation** summer course in Boulder, Colo., sponsored by ALI-ABA and University of Colorado Law School; \$895. The American Law Institute-American Bar Assn. Committee on Continuing Professional Education, Registrar, 4025 Chestnut St., Philadelphia, Pa. 19104-3099; 800-253-6397.

**JUNE 27. Workers Compensation: Finding a Better Way** seminar in Chicago, sponsored by FA•CT; \$395. Also **June 29** in Livonia, Mich. FA•CT, P.O. Box 5936, Kent, Wash. 98064; 800-356-4680.

**JULY**

**JULY 10-11. Compensation & Finan-**

**cial Incentives for Providers in Managed Care** conference in Boston, sponsored by the Institute for International Research; \$1,295. Conference Coordinator, Institute for International Research, 708 Third Ave., 4th Floor, New York, N.Y. 10017-4103; 800-345-8016.

**JULY 10-11. 12th Annual Illinois Conference Personnel Law Update 1995** conference in Chicago, sponsored by Council on Education in Management; \$495. Council on Education in Management, 325 Lennon Lane, Walnut Creek, Calif. 94598-2418; 510-934-8333.

**JULY 10-11. Risk Management in Managed Care** conference in Las Vegas, sponsored by the American Society for Healthcare Risk Management of the American Hospital Assn.; \$365 for ASHRM and host chapter members, \$365 for AHA institutional members, \$485 for all others. American Hospital Assn., P.O. Box 92247, Chi-

cago, Ill. 60675-2247; 312-622-5648.

**JULY 10-12. Benefit Conference for Public Employees** seminar in Boston, sponsored by the International Foundation of Employee Benefit Plans; \$685 for IFEBP members, \$775 for non-members. International Foundation of Employee Benefit Plans, Registrations Department, P.O. Box 69, Brookfield, Wis. 53008-0069; 414-786-6710, ext. 257.

**JULY 11-12. Achieving Better Medication Compliance: Everyone Benefits** seminar in Kansas City, Mo, sponsored by the Ellis Management Marketing Group's Managed Care Training Institute; \$895. Also **Nov. 7-8** in Kansas City. EMMG, 4520 Madison, Suite 303, Kansas City, Mo. 64111; 1-800-835-7860 or 816-931-6469.

**JULY 12-13. Business Interruption Insurance** course in Sevenoaks, England, sponsored by the Chartered In-

*Continued on next page*

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A copy of the pre-qualification form may be requested in writing from Risk Insurance, Illinois State Toll Highway Authority, One Authority Drive, Downers Grove, Illinois 60515. Forms are due July 10, 1995.

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**Financial:**

Chief Financial Officers and Vice Presidents of Finance ..... 3,539  
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**Risk/Employee Benefits:**

Vice Presidents, Directors, Managers, and other related department personnel of: insurance, risk, employee benefits, personnel, compensation, pension, safety, security, industrial relations, human resources and employee/labor relations ..... 15,529

**Sub-total** ..... 30,001  
Associations ..... 343  
Government, Unions and Educational Institutions 950

**Commercial Consumers**

**Sub-total** ..... 31,294  
Insurance Agents and Brokers ..... 8,285  
Insurance Companies ..... 7,687  
Accountants, Actuaries, Attorneys & Consultants ..... 3,563  
Adjusters, Appraisers, TPA's, Captive Managers & Health Care Providers ..... 1,844  
Others Allied to the Field ..... 1,028

**Total Qualified** ..... 53,701  
Non-qualified ..... 74  
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**TOTAL CIRCULATION** ..... 53,781

★ *Source: Business/Occupational breakdown of qualified circulation, November 28, 1994. Issue, as submitted to BPA for December 1994 BPA Publisher's Statement*

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**JULY 12-13. Employment Regulations**  
 in Illinois workshop in Chicago, sponsored by the Institute of Business Law of California State University in Los Angeles; \$595. Dept. FJ-IL, Institute of Business Law, California State University, Los Angeles, P.O. Box 3488, Santa Monica, Calif. 90408; 310-450-0500.

**JULY 14-15. Managed Care in Dentistry** conference in Chicago, sponsored by the American Dental Assn.; \$220 for ADA members, \$295 for non-members. American Dental Assn., Accounting Department-Cashier, 211 E. Chicago Ave., Chicago, Ill. 60611-2678; 312-440-2749.

**JULY 17-18. Creative Proposals for Superfund Settlements** seminar in San Francisco, sponsored by the King Communications Group Inc.; \$895. King Communications Group Inc., 627 National Press Building, Washington, D.C. 20045; 202-662-9728.

**JULY 17-19. Environmental Regulation** course in Chicago, sponsored by Executive Enterprises; \$1,195. Executive Enterprises, 22 W. 21st St., New York, N.Y. 10010-6990; 800-831-8333.

**JULY 17-19. The National Healthcare Claims Congress 95** in Boston, sponsored by the Institute for International Research; \$1,295. Conference Coordinator, Institute for International Research, 708 Third Ave., 4th Floor, New York, N.Y. 10017; 800-345-8016.

**JULY 18. CEBS Information Meetings** in Chicago, sponsored by the CEBS Program of the International Foundation of Employee Benefits Plan; no charge. Also July 19 in Houston; July 20 in Dallas; July 24 in Detroit; July 25 in St. Louis; July 26 in Minneapolis; July 27 in Milwaukee; July 31 in Indianapolis; Aug. 1 in Cincinnati; Aug. 2 in Cleveland and Los Angeles. CEBS Program, IFEBP, P.O. Box 1270, Brookfield, Wis. 53008-1270; 414-786-6710, ext. 565.

**JULY 18-20. National Workers Compensation & Occupational Medicine Seminar** in Hyannis, Mass., sponsored by Workers Compensation Monthly and Occupational Medicine Digest; \$425. SEAK Inc. P.O. Box 729, Falmouth, Mass. 02541; 508-548-7023.

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# AT&T

Continued from page 3

The \$40 would be waived, though, if an employee were admitted to the hospital.

In addition, the contract would improve the preventive benefits under the POS plan, including coverage for routine physicals and other primary care services.

The new plan also would cover mammograms for women as young as 35. Under AT&T's former health plan, most preventive services were not covered, and the plan covered mammograms only for women age

50 or older.

Annual out-of-pocket expense limits for employees seeking care from network providers would decrease to \$750 from \$1,000 under the new agreement.

Employees who seek care from non-network providers would have to pay a \$400 deductible and would be responsible for paying 20% of eligible medical expenses. The annual out-of-pocket maximum for these employees would be \$2,500.

"Our focus was to shift employees into managed care," said David Carver, district manager of benefits planning and analysis for AT&T in Morristown, N.J. "Right now, about

60% of active employees use the managed care network. We'd like that to increase to 80% to 85%," he said.

The company also is encouraging retirees to use managed care providers. Under terms of the new contract, retirees younger than 65 who retired prior to March 1, 1990, could retain their former indemnity plan coverage or they could enroll in the POS plan. Workers who retired after that date would have to enroll in the POS plan, unless they live outside the managed care plans' service area.

Like active employees, retirees who choose the POS plan would

pay no deductibles or coinsurance and would pay modest fees for office visits. The monthly cost to each retiree for this coverage option would range between \$5 and \$20.

Retirees who remain in the indemnity plan option would pay no copayments for office visits but would pay high coinsurance and deductibles.

To help all retirees pay for their own health plan contributions, AT&T created a Care Account, which retirees can use to offset coinsurance or copayment costs. A typical retiree younger than 65 who has family coverage would receive \$250 annually. Retirees who retired

after March 1, 1990, can use the fund to cover completely the monthly payment for their health care or could use the money to cover other expenses, like hearing exams and prescription drug copayments.

Mr. Carver said AT&T does not expect the changes to decrease its health care costs, but officials hope wider use of managed care will control cost increases. In 1994, the telecommunications giant spent approximately \$1.3 billion on active and retiree health care.

Other health care improvements contained in the new contract include providing employees and dependents organ transplant coverage through so-called "centers of excellence" and the development of a national managed mental health and substance abuse network.

The contract also would give participants in AT&T's 401(k) plan more investment options and more frequent statements and updates on daily cash balances.

And, AT&T will provide \$7.5 million to pay for improvements in its Family Care Development Fund. Created in 1989, the fund provides elder and day care benefits, among other things. AT&T also increased its adoption expense reimbursement to \$3,000 from \$2,500.

Pension benefits under the new contract would increase 12% effective July 1, 1995, for workers retiring after May 28, 1995, and for the first time, a minimum monthly pension—varying among retirees based on age and length of service—would be established for all current retirees. **BI**

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## Hartford

Continued from page 2

ITT Hartford "has never had to rely on ITT Corp. If anything, it was the other way around," said John F. Snyder, senior vp with Best. "The insurance units have generated capital and strong earnings for ITT Corp. Therefore, if anything, this is a plus for Hartford. It's totally responsible for its own management and compensation scheme."

Jay Cohen, an analyst with Salomon Brothers Inc. in New York, said ITT Hartford will be stronger on its own than it was as a member of a \$25 billion conglomerate.

"Hartford will be a more nimble company and can avoid any of the bureaucracy of dealing with a large parent. It can react quicker to changes in the market and can control acquisitions on its own. Hartford can also now compensate its employees with its own stock, which means more than holding shares in casinos or Madison Square Garden," he said.

ITT Corp. said Hartford's senior management team will remain intact. Donald R. Frahm will continue as chairman and chief executive officer, while Ramani Ayer will oversee the property/casualty operations and Lon Smith will head up the life operations.

A large number of ITT Corp. employees also will benefit from the break up. About 45,000 employees who had been accruing stock in a six-year-old Employee Stock Ownership Plan likely will receive more than 1 million shares from the plan, which was terminated last week.

A corporate spokesman said the stock—now worth about \$130 million—is now in the hands of a trustee, who likely will distribute it to all participating employees, regardless of their vesting status, once the plan's debt is paid off. The spokesman said the plan carried a five-year vesting schedule, but all participants will receive their full entitlement even if they hadn't participated for five years. **BI**

# Bonds

Continued from page 1

Argonaut Insurance Co. of Menlo Park, Calif.—is also seeking a bond from reinsurers at Lloyd's.

The companies are taking advantage of established but little-used state statutes that require non-admitted insurers to post a bond prior to a coverage dispute.

For example, Section 1616 of the California Insurance Code says: "Before any non-admitted foreign or alien insurer shall file or cause to be filed any pleading in any action, suit or proceeding instituted against it, the insurer shall either (1) procure a certificate of authority to transact insurance in this state; or (2) give a bond in the action, suit, or proceeding in an amount to be fixed by the court sufficient to secure payment of any final judgment which may be rendered in the action, suit or proceeding."

Forty-seven states require some pre-answer security, said Robert M. Horkovich, of Anderson Kill Olick & Oshinsky, a policyholder law firm in New York.

"The purpose of the bond is to protect policyholders from the potential insolvency of foreign underwriters and insurers," he said.

Using one of the laws, Travelers Insurance Co. last year petitioned a New York state court seeking a bond from its reinsurers at Lloyd's (BI, March 21, 1994). The dispute was settled prior to a bond being required.

Recently, several policyholders have taken similar action.

In one case, a Superior Court judge in Santa Ana, Calif., next week will consider a petition by Lockheed Martin to require Lloyd's underwriters to post a \$450 million bond to cover pollution claims, said Barry Bunshoft, of Hancock, Rothert & Bunshoft in San Francisco who represents the underwriters.

And separately, Raytheon won a California appeals court ruling seeking a \$30 million bond for a pollution claim relating to its Mountain View, Calif., manufacturing site, he said. Lloyd's underwriters are now appealing the ruling to the California Supreme Court. Initially, Raytheon's request was rejected by a trial court.

Separately, in March, a Superior Court judge in Los Angeles ordered Lloyd's syndicates led by syndicate 545, managed by Sturge Aviation Syndicate Management Ltd., to post a bond for \$2.3 million to secure pollution claims made by Hughes Aircraft, said Gregory D. Granger, of Lane Powell Spears Lubersky in Los Angeles, who represents Sturge.

The Lloyd's syndicates have posted the bond, Mr. Granger said, but will ask a court to consider the assets of the Lloyd's U.S. trust funds as adequate security. Recently Lloyd's agreed to a major restructuring of those funds in a deal with New York regulators.

"Hopefully we will have a declaration that will satisfy the court...the bond issue is a nightmare for underwriters," he said.

And in another March ruling, a U.S. District Court in Los Angeles ordered Lloyd's underwriters to post a \$3.1 million bond for a reinsurance claim by Argonaut Insurance, which wrote coverage for Hughes Aircraft.

The underwriters, led by syndicate 48, which is managed by Methuen (Lloyd's Underwriting Agents) Ltd. did post the bond, said Katherine Smith Dedrick, of Hinshaw & Culbertson in Chicago, who represented Argonaut.

Policyholders are taking advantage of the state statutes because they fear that insurers may become

insolvent, said Anderson Kill's Mr. Horkovich.

The bonds have become necessary due to the deluge of insolvencies and closures of insurance companies in London, he said. "The need in the London company market is already obvious. You only have to look at the KWELM companies, Orion Insurance and other significant insurers that have gone out of business."

In such cases, policyholders often have to wait several years and then payments are seldom for the entire amount claimed, Mr. Horkovich said.

So policyholders, before litigation or negotiation begin, are seeking protection against the risk of insolvency, he said.

Concern over payments by Lloyd's syndicates has grown since Lloyd's became embroiled in litigation with members and the adequacy of its U.S. trust funds came under scrutiny by New York insurance regulators.

In a report published last month, the New York examiners found the U.S. trust funds had net deficiencies of \$7.75 billion, or more than \$18 billion before reinsurance recoveries, at the end of 1993 (BI, May 29). The trust funds are intended to pay claims and related expenses for U.S. dollar-denominated risks.

"Who knows which insurers will be around tomorrow?" asked Mr. Horkovich. "Prudent policyholders that have significant claims with London market insurers should look into whether they should require the foreign insurers to post a bond."

Lawyers for Lloyd's underwriters counter that the bonds are unnecessary as the claims are well reserved. They say the policyholders are using the bonds as a tactic to have claims paid before disputes are resolved in court.

"Any claim that exists is already well reserved," said Mr. Bunshoft.

Lloyd's reinsurance-to-close mechanism ensures that outstanding claims are reserved for prior to a year of account being closed, he said.

In addition, Lloyd's syndicates have often been successful in defending pollution claims, he noted.

"The (policyholders) see that the road to success might not be in litigating the matter to conclusion but through trying to force a settlement," Mr. Bunshoft said.

The bonds usually cost between 1% and 1.5% of the total amount posted and the cost can put pressure on underwriters to settle the disputes prior to litigation, he said.

There is also a limited market for security bonds. Lloyd's syndicates may not find sufficient capacity to purchase the bonds required by court judgments and be forced to settle, Mr. Bunshoft said.

Legislation that has been passed by the California Assembly and is pending before the state Senate would exempt approved surplus lines insurers from having to post pre-answer bonds in California.

The bill, A.B. 328, is sponsored by Assemblyman David Knowles, R-Placerville, and is supported by London insurers.

The laws requiring bonds "are antiquated statutes that have not been used for 50 years and they are currently being used by big corporate litigants for settlement leverage," said Bill Marcoux, a partner at Lebouef, Lamb, Green & MacRae in San Francisco, which also represents Lloyd's.

"The punitive bonds are not needed and are being used as a stick to beat up on insurers that California has been reliant on and needs to keep in the market place," he said.

If the bonds are required, the cost will be passed back to policyholders through increased premiums, Mr. Marcoux said. ■

# Cat fund

Continued from page 2

separate events that will likely result in industry gross losses of at least \$1.5 billion, adjusted annually in accordance with the percentage change in the Consumer Price Index, shall be aggregated to reach the 15%."

Any insurer that had paid premiums to the pool could apply for reinsurance payments and receive payments of 95% of its losses in excess of 15% of its consolidated surplus. In addition, an insurer that sustained losses of at least 20% of its consolidated surplus to one of the named perils could receive 95% of those losses in excess of the 20%, even if the overall industry did not lose 15% of its combined surplus.

If the reinsurance payments exceed its available funds, the bill calls

for the corporation to borrow additional funds from the U.S. Treasury at market rates.

Insurers have praised the bill, whose lead sponsors are Reps. Bill Emerson, R-Mo., and Norman Mineta, D-Calif.

"We look forward to working with Congress and other interested groups and individuals in addressing the problems associated with disaster assistance, hazard mitigation and the insurance issues," said Frank Nutter, president of the Reinsurance Assn. of America.

"This legislation will safeguard insurer solvency and stabilize financial markets which are at risk of collapse in the wake of a grave natural disaster, particularly if it hits a heavily populated area," said Lowell R. Beck, president of the National Assn. of Independent Insurers in Des Plaines, Ill.

The concept also got a boost from delegates to the White House Conference on Small Business, which called upon Congress to enact legislation that would "include a private-sector all-risk property insurance program offered through a newly created private non-profit organization to reinsure catastrophic losses." That was one of the group's 60 final recommendations (see story, page 2).

The Risk & Insurance Management Society Inc. has taken no position on the matter.

The measure does, however, contain what is certain to be a point of controversy. The bill specifically would exempt the corporation from state and federal rate regulation of any sort regarding homeowners catastrophe rates. That power would be vested in a board of independent actuaries appointed by the secretary of the Treasury. ■

# IPOs

Continued from page 1

ulating a private placement memorandum for a new Bermuda-based reinsurance holding company to be called CORE Holdings Ltd.

The public offerings have a variety of aims, ranging from capitalizing a start-up reinsurer in Normandy's case to paying off debt in Renaissance's case.

While the market's reaction to these offerings remains to be seen, investors' appetite for reinsurance stocks generally is good.

"The investment community is interested in the reinsurance market because the reinsurance market has successfully been able to decouple itself from the volatility of the primary market," noted Alan Levin, managing director of Standard & Poor's Insurance Rating Services in New York.

"With every catastrophe, they move farther and farther from the results of the primary industry, and that's a very sellable idea to the marketplace," he said.

Whether the reinsurance market needs the capacity that some of these offerings would bring is questionable. "It won't harden the market, will it?" Mr. Levin commented.

Pru Re Holdings last Thursday filed amended offering documents with the Securities and Exchange Commission to sell 20 million shares, or a 40% stake, to the public.

The holding company—which controls Pru Re, the largest broker market reinsurer in the United States, and subsidiaries Prudential National Insurance Co. and Le Rocher Reinsurance Ltd. of London—is now wholly owned by PRUCO Inc., a unit of Prudential Insurance Co. of America.

PRUCO would receive the proceeds of the offering. The SEC filing does not include a per share offering price or estimate of total proceeds.

The offering amends an original 1993 IPO filing in which Prudential planned to spin off a 40% stake in Pru Re for \$420 million.

That offering followed Prudential's failed efforts to find a private buyer for the entire company at an offering price of \$1.2 billion (BI, Nov. 22, 1993).

Like the original IPO filing, the latest offering describes Prudential's efforts to limit Pru Re's exposure to losses on its existing business. These include a stop-loss agreement written by Prudential unit Gibraltar Casualty Co. providing up to \$375 million in reinsurance to Pru Re.

The offering also describes steps Pru Re has taken to improve its performance, including the hiring of current Chairman Joseph V. Taranto and others; a 30% staff reduction and other moves to trim expenses; improved management of catastro-

phe exposures; and a new underwriting strategy focusing on specialty risks like medical malpractice, directors and officers liability and errors and omissions coverages.

Investors' response to the offering remains to be seen, Mr. Levin suggested.

"If you think big is good, they're big," he commented.

Omaha-based Normandy America last month filed a registration statement for an offering of 10.5 million common shares, which at a proposed maximum offering price of \$25 per share would raise \$262.9 million.

About \$200 million of this would be contributed to Normandy Re Inc., a newly formed Nebraska-domiciled broker market reinsurer that would focus on writing long-tail casualty treaty reinsurance, according to the prospectus.

The rest of the proceeds would be used for various corporate purposes, including buying a broadly licensed inactive property/casualty insurer that would then be merged with Normandy Re to give the reinsurer admitted status in a number of states. Buying the shell company, for which Normandy America is seeking candidates, will cost between \$4 million and \$7 million, depending on the number of state licenses it holds, the prospectus reports.

Normandy America is headed by Christopher K. Bagdasarian, a 29-year-old Omaha money manager who has recently been touted as the next Warren Buffett.

Until last year, Mr. Bagdasarian headed Criterion Holdings Inc., an equity portfolio manager for high net worth investors.

Before that, he managed his own portfolio and third-party funds, the prospectus says. That portfolio started at \$36.9 million 10 years ago, when Mr. Bagdasarian was a 19-year-old college undergraduate, and had grown to \$599.4 million at the end of last year. It generated average annual return of 29.1% over the decade, according to Normandy's SEC filing.

Mr. Bagdasarian will act as chairman of Normandy America while his wife, Victoria Briggs, acts as vice chairman.

Peter A. Bengelsdorf, former chief financial officer of Underwriters Reinsurance Co., will serve as president of the holding company and Normandy Re.

The company has also lined up several high-powered directors: William B. Little, a founding partner of Forstmann Little & Co.; Peter V. Ueberroth, former commissioner of Major League Baseball; William H. McCartney, former Nebraska insurance commissioner; and Robert Fisher, managing director of Wertheim Schroder & Co.

The offering is being underwritten by Salomon Bros. Inc., Alex. Brown & Sons and Wertheim Schroder

The prospectus reports that Normandy Re will focus on low-layer excess-of-loss casualty treaty business with "risk-limiting features" like loss ratio caps, aggregate dollar caps and sliding-scale ceding commissions tied to profitability.

Departing from industry practice of investing mainly in fixed-income securities, Normandy Re will invest most of its money in stocks, the filing says.

The company expects to get a higher rate of return with its equity investment strategy and has less need for liquidity because of the long-tail nature of its business and the "low" 0.5-to-1 net premium-to-surplus ratio it plans to maintain, according to the filing.

Apart from the investment risk, though, the strategy has drawbacks: Under generally accepted accounting principles, the equity portfolio will not generate the investment income that a bond portfolio would. Thus, Normandy Re's results will depend largely on its underwriting performance, a situation that could lead to "significant net losses" under GAAP because of the soft casualty market, the filing reports.

Normandy Re's investments will be handled by Criterion Securities Inc., a firm owned by Mr. Bagdasarian and Ms. Briggs. Normandy America's board will also have oversight rights to monitor "potential and actual conflicts of interest" between Normandy's investment portfolio and the personal portfolios of Mr. Bagdasarian and Ms. Briggs, the filing reports.

Meanwhile, RenaissanceRe is returning to the market with a planned offering of 1.8 million shares that the company hopes will raise slightly more than \$50 million.

The proceeds would be used to help pay off a \$120 million revolving credit facility that was drawn down to redeem RenaissanceRe preferred stock, according to a preliminary prospectus filed with the SEC last month.

The company would then be able to use the credit facility to increase the capital of reinsurer Renaissance Re as needed. The catastrophe reinsurer's capital stood at \$426 million at March 31.

After the offering, public shareholders would own 10.7% of RenaissanceRe. Control of the company would remain with founding institutional investors Warburg Pincus Investors, USFG Corp. and two investment affiliates of General Electric Corp.

RenaissanceRe Holdings originally filed plans for a \$218.5 million IPO in late 1993 but shelved the plan because of poor stock market conditions.

The reinsurer's original investors instead committed another \$100 million to the company (BI, Dec. 27, 1993). ■

# OSHA

Continued from page 1

scheduled hearings on the bill for June 20 and June 28. The Senate Labor and Human Resources Committee also will hold OSHA-related hearings this week.

Even before the panels formally take up the topic, the agency put its long-awaited ergonomic safety standards on the back burner.

"In the face of congressional intervention in OSHA standard-setting, it is not now possible to publish a standard which has the breadth necessary to attack this problem. Given the magnitude of the problem, OSHA must continue development of a standard which will have support from reasonable people. OSHA also will use its resources to support education, training, consultation and enforcement activities to address this workplace epidemic," OSHA Administrator Joseph A. Dear said in a statement.

Initially, the agency—which estimates that work-related musculoskeletal disorders affect more than 700,000 workers each year—planned to introduce an ergonomic standard last fall. Some businesses and members of Congress countered that the OSHA research was flawed and that the proposal appeared likely to go too far.

Rep. Ballenger and his 55 co-sponsors seem to feel that the agency goes too far in many other areas as well.

"OSHA has become fundamentally misdirected," he said. "Instead of promoting and encouraging workplace safety and health, OSHA has become known for issuing silly regulations and is preoccupied with collecting fines from unsuspecting employers. It's time to add some common sense to OSHA's regulations and focus on promoting safety in the workplace."

Rep. Ballenger's bill would require OSHA to put at least 50% of its funding into consultation, education, training and compliance assistance programs within three years of the bill's enactment. It also would create a voluntary compliance program in which employers could have advisory health and safety reviews done by

"certified individuals" and then be exempt from random OSHA inspections for a year.

In addition to requiring that the Occupational Safety and Health Act be amended to include the regulatory risk assessment and cost/benefit analysis reforms already approved by the House, the bill would require that the risk assessment and cost/benefit analysis be industry-specific. The bill also would create a petition process to review existing regulations under certain circumstances.

The bill also would revamp the OSHA penalty system. For example, certain paperwork violations would no longer be subject to pen-

pects of the proposal.

"One is obviously making the voluntary protection program a central part of OSHA's overall program and mission. Basically, if an employer can show that if he has proper programs in place, then OSHA will come in and basically waive inspections under certain circumstances," he said.

Second, RIMS particularly favors the requirement that OSHA devise industry-specific risk assessment and cost/benefit analyses, added Mr. Soles, who is group director-insurance and safety for the Sheet Metal & Air Conditioning Contractors National Assn. in Chantilly, Va.

## 'It's time to add some common sense to OSHA's regulations and focus on promoting safety in the workplace,' Rep. Cass Ballenger says.

alties "except where there is a direct threat of injury or intent to mislead or deceive employees of OSHA." The bill also would give employers the right to fix violations before citations are issued, except in cases of a death or serious injury.

Also, the bill would: create exemptions from inspections for small businesses with below-average injury rates; requiring employees to inform their employers of workplace hazards before contacting federal authorities; give more anti-discrimination protection to employees who point out health and safety concerns to their employers; encourage but not require employee participation in workplace safety programs.

The merging of OSHA and the Mine Safety and Health Administration and OSHA's assumption of the duties of NIOSH are included in the bill as money-saving measures.

Rep. Ballenger's proposal drew expected praise from the business community.

Tom Soles, chairman of the Risk & Insurance Management Society Inc.'s health and safety committee, particularly praised two as-

"Rep. Ballenger's OSHA reform bill strikes the right balance between education and enforcement and will enhance worker protection much more than the current wayward system," said Jerry Jasnowski, president of the National Assn. of Manufacturers in Washington.

"Rather than trying to govern through the use of penalties, inspectors and citations, this bill would emphasize a partnership between OSHA and employers and employees," said Mr. Jasnowski. "Employers would feel free to ask OSHA for help, without fear of being penalized."

Much of what Rep. Ballenger proposes to do legislatively, President Clinton had proposed doing through administrative channels (BI, May 22). Business groups tend to favor the former approach because they consider it more difficult to change.

Organized labor did not join in the praise of the bill. The Washington-based AFL-CIO called the bill "a direct attack on the working men and women that puts their lives in danger." The labor federation promised to "do everything possible to oppose this cruel and regressive measure." ■

standard also will be applied to statutory capital.

Another factor weighing on capital accretion are various outstanding encumbrances—specifically, toxic and environmental exposures, reinsurance recoverable problems and downsizing charges. There is a tendency for insurers to categorize such charges as one-time events and exclude them

## The industry, and some insurers in particular, continue to have great difficulty in accreting statutory capital.

from their operating earnings calculations. Any time a company takes a charge, it in essence is admitting that it overstated prior results. Why is that an unusual charge?

Taking this a step further, insurers are implying the same on pending toxic and environmental charges. If we remember correctly, most insurers took credit for the premiums when the contract was written. Hence, why not

take credit for the charge-offs now? Little by little, the industry's ability to use creative accounting techniques is being curtailed. We think the pace should be faster.

• For all practical purposes, the industry is being regulated by the rating agencies. In general, they have become more active in terms of making rating adjustments—mostly downgrades as of late. The rating agencies have become more sensitized to catastrophe exposures, environmental exposures, leverage and retention levels, capital shifts among various inter-company operations and insurers' ability to accrete statutory capital.

The industry clearly is poised for some major consolidation moves. Before all of the dust settles, there most likely will be more The Home Insurance Co.-type debacles and more mergers like Continental/CNA, where 1 + 1 will equal eight-tenths.

It is difficult to believe that the dislocations that emerge from consolidation will not play into the hands of the stronger insurers. Insurance companies cannot be all things to all people. Smaller is not necessarily bad, if it is followed by enhanced profitability. ■

## Updates

### Judge overturns receivership

TALLAHASSEE, Fla.—A Florida appeals court has thrown out an order appointing the state Insurance Department as receiver for Provident Capital Indemnity Ltd., an offshore insurer that operated through a Florida office and was capitalized with allegedly bogus certificates of deposit.

Reversing a lower court, a three-judge panel of the state's 1st District Court of Appeal ruled that the department has no authority under state receivership statutes to take over an insurer that is not domiciled in the state or that does not have trustee assets in the state.

In a statement, Harold C. Maridon, PCI's Costa Rica-based president, said the insurer now is considering "remedial action" against the Insurance Department, without elaborating.

The California Insurance Department barred PCI in 1992, after finding that its assets consisted largely of CDs from a non-existent Hong Kong bank (BI, Nov. 2, 1992).

Florida regulators shut down PCI's Delray Beach, Fla., office in 1993 and leveled criminal charges against several of its officers. Former PCI President Robert C. Roy pleaded no contest to a felony charge of selling insurance without a license. Three others—Mr. Maridon, Grahame Sanders and Kathryn Elliott—fled to Costa Rica, where PCI has continued to operate.

Mr. Sanders returned to face unrelated federal charges and was convicted on 64 fraud and conspiracy counts (BI, April 10).

### Louisiana Blues settlement

BATON ROUGE, La.—Blue Cross & Blue Shield of Louisiana will refund more than \$21 million to tens of thousands of policyholders to resolve two class-action lawsuits over claims-paying practices.

The settlement excludes self-insured groups that had agreements with BC/BS to administer their claims.

The Blues plan, Louisiana's largest health care insurer, was accused in 1993 of "discounting," in which policyholders' copayments are based on the full amount of a service, but the insurer paid its portion of the bill based on negotiated discounts with providers.

Blue Cross & Blue Shield organizations in Ohio and South Carolina have also come under fire for the practice (BI, March 27).

BC/BS of Louisiana will refund \$5.1 million to 35,000 policyholders who had hospital claims between Jan. 1, 1988, and Dec. 31, 1994, but many more will benefit because the plan agreed to stop discounting as of Jan. 1, 1995, said plaintiffs attorney Steve Thompson, of Moore, Walters, Shoenfelt & Thompson in Baton Rouge.

Most of the settlement—\$16.1 million—will go to 12,000 individuals who bought cancer and serious disease policies from BC/BS but whose benefits were reduced by the amount Medicare paid. Each should receive the same benefits as a person with the same policy who was not covered by Medicare, Mr. Thompson argued. The settlement does not apply to Medicare supplement policyholders.

### New England Blues alliance

BOSTON—A new alliance of New England's Blue Cross & Blue Shield plans expects to have new managed care products available to the six-state market by the end of the year.

The regional products will link the plans' local provider networks to try to attract business from multistate employers.

"As independent plans, we have worked for decades to serve our distinct, and in many ways unique, populations," said Douglas McIntosh, president of Blue Cross & Blue Shield of Rhode Island. "Now, as our region changes, we are identifying goals and needs that are common to all of the people we serve and are working together."

The alliance also will help the plans collect and analyze information about practice patterns and outcomes data. About 28,000 physicians and 200 hospitals are in the plans' combined networks.

### Briefly noted

Nationwide Mutual Insurance Co. has named Peter F. Frenzer acting president of its **Scottsdale Insurance Co.** unit, succeeding Vickie F. Karchner, who resigned "to pursue other interests" earlier this month. Mr. Frenzer is executive vp of investments for Nationwide, which is conducting a search for a permanent successor. . . . Seven state regulators last week signed off on **Zurich Insurance Group's** bid to take over more than \$1 billion of Home Holdings Inc.'s business without taking over its past liabilities. Zurich's final deal centered on a reinsurance contract in which Zurich promised to pay up to \$1.59 billion if Home assets are exhausted before all its claims are paid (BI, May 22). . . . Shareholders last week approved Chattanooga, Tenn.-based **Provident Life & Accident Insurance Co. of America's** reorganization into a Delaware holding company, Provident Cos. Inc. . . . Indianapolis-based **Acordia Inc.** signed a letter of intent to acquire The McElroy-Minister Co., a Columbus, Ohio-based broker with annual revenues of about \$12 million. Terms were not disclosed. . . . **Zurich Reinsurance Centre Holdings Inc.** last week promoted Richard F. Smith to president from chief operating officer and executive vp. He remains chief operating officer and takes over the presidency from Chairman and CEO Steven M. Gluckstern. . . . **Florida Gov. Lawton Chiles** has called a special legislative session on health care to be held before September. The Florida Legislature failed to enact Gov. Chiles' Health Security Act during the 1994 and 1995 regular sessions and during a special session last year. He also vetoed a bill that would repeal Florida's year-old law enabling the state to sue tobacco manufacturers. . . . Federal prosecutors have ended their investigation of **Mississippi Insurance Commissioner George Dale**. Mr. Dale was investigated as part of a larger FBI probe of the state's insurance industry (BI, Aug. 29, 1994). . . . **Massachusetts Mutual Life Insurance Co.** and **Connecticut Mutual Life Insurance Co.** on Friday announced they are discussing a possible merger, subject to completion of a feasibility study.

# Picout

Continued from page 39

theory that is not universally shared.

In fact, if so many primary insurers were as flush with capital as they purport, why have they agonized so much over various downsizing charges and charges for toxic and environmental exposures? And why have so many buy-back programs been nothing more than toothless tigers? The fact remains that the industry, and some insurers in particular, continue to have great difficulty in accreting statutory capital.

• Unless there is a dramatic shift in pricing, it is difficult to see any substantive accretion of capital unless the bond market catches fire and/or investors develop a new penchant for investing new money into some of the older, tired insurers.

With respect to the bond market, it may not be easy for some insurers to translate bond gains into capital increments. This relates to asset liability matching and reinvestment rates. At this juncture, FASB 115 relates to GAAP financials only. The day may be approaching when the

# Future not what it used to be for insurers

By MYRON M. PICOULT

Special to Business Insurance

In today's stock market environment, if an insurance company is not involved in a major restructuring of its operations and/or a substantive buy-back program, the likelihood is that investors are ignoring the stock. This pretty much sums up the performance of the group of insurance stocks thus far this year. With few exceptions, the performance of "quality perceived insurance equities" has lagged the performance of many of the "wanna-bees."

One of the reasons for the laggard performance of many of the sacred cows was valuation hang-ups and the belief by many institutional investors that they had to broaden their holdings to take advantage of a possible bond market rally in the stocks. Interestingly enough, the stocks have not reacted to the bond market rally with as much gusto as expected. Furthermore, there was the age-old belief that when water comes into the canal, all the boats would float at a higher level. We do not agree with this thesis due to the numerous changes taking place in the property/casualty business. Simply put, the future is not what it used to be.

There are clearly numerous structural changes occurring that are more than offsetting the traditional cyclical factors that historically influenced the industry's underwriting and pricing cycles. These changes indicate that the traditional underwriting cycle may never surface again but will be replaced by minicycles within lines and the business as a whole. The industry's needs in terms of management expertise, expense controls and business focus seem to mirror what the banking business went through a decade ago, and we are now beginning to see the fruits of their labors via consolidation. The structural changes that we are referring to include the following:

- The property/casualty industry is a bifurcated industry between the "haves" and the "have-nots." The key here is that the underwriting performance and overall profitability of the haves has widened materially vis-a-vis the have-nots. Successful property/casualty companies have two common threads. They are disciplined and focused underwriters and they have been good investors. The consistency of their underwriting records has been such that there has never been a need to get involved in exotic

investing.

In general, the returns on equity for the haves are greater than 10% and they have strong credit ratings. The have-nots have returns on equity below 10% and low credit ratings. The companies that need rate increases the most—the have-nots—are unable to implement them without driving their better risks to the haves or the alternative risk transfer market.

Hence, many of the have-nots have turned to major corporate restructurings to dig their way out. Such a modus operandi is an indication that managements did not keep abreast of the changing industry dynamics. It would be fallacious to believe that restructured insurers would be on par with the quality insurers once the restructuring has been completed. For the quality insurers, re-engineering is an ongoing process and not a stop-and-go game. Hence, the gap between the haves and have-nots is expected to widen.

- The commercial insurance product is becoming increasingly commoditized. The product is being unbundled into risk transfer and servicing components. Not all insurers are set up to effectively handle this unbundling.

- Approximately 45% of the domestic casualty market now is written in the alternative risk and captive markets. The better risks are the first to leave the traditional market and, once gone, rarely return. Furthermore, this shift significantly reduces the pricing power of insurers as the demand curve for commercial insurance has become more price elastic.

There is yet another wrinkle that seems to be developing. Several reinsurers are becoming more aggressive in the alternative marketplace, raising the level of competition. This further puts the squeeze on the traditional insurers that cannot compete effectively.

- The involvement of financial entrepreneurs in the insurance business is also producing marked changes. On the plus side, insurers owned by financial companies are likely to be better managed with greater focus on expense control and profitability. In short, there is a closer alignment of the financial interests of executives with those of corporate owners. The industry cannot compete effectively for business with a 30% expense ratio. However, for the most part, these financial entrepreneurs have access to latent pools of capital that can

be put to work quickly. Hence, demand/supply distortions in the marketplace are likely to be short-lived.

- Traditionally, the modus operandi in the business was for insurers to grow their way out of a problem. Many a time, the executive fiat was "grow the top line and don't worry about the bottom line." The sluggish premium growth dynamics of the business make this a much more difficult task to achieve. In the 1960s, 1970s and 1980s, the industry's premiums increased at respective rates of 7.4%, 12.1% and 8.8%. Thus far in the 1990s, premiums have grown a few percentage points. Besides the pricing box some insurers have put themselves into, part of the premium slowdown can be ascribed to reduced inflationary pressures, some subtle changes in tort costs, the need for some insurers to correct unusually heavy property exposures in earthquake- and hurricane-prone areas and pressures from the rating agencies to reduce leveraged ratios.

- The "London Market Phenomena" also is involved here. The turmoil in the London marketplace does not accrue to everyone's benefit. Opportunities to write business are likely to remain elusive for insurers without sufficient capital. Moreover, there may well be reinsurance recoverables that will have to be scrutinized more closely. The current penalty in the convention blanks put into place several years ago was to focus on slow-paying recoverables, many of which were coming out of London. Such write-offs come right out of the statutory capital base.

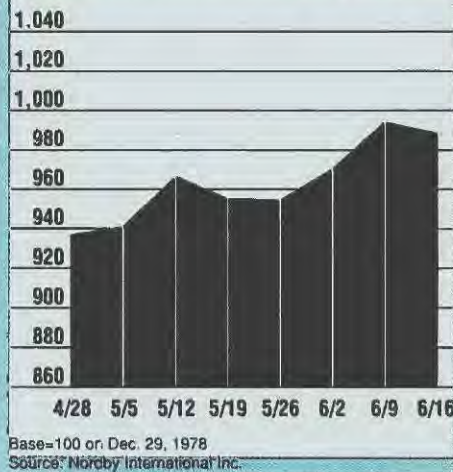
- Over the past 13 or 14 years, we have gone through what is likely to be one of the greatest runs in the value of financial assets. Notwithstanding this, many property/casualty insurers find themselves in a capital squeeze. This is a

See Picoult on page 38



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## BI Insurance Index



## Catastrophe insurance option call spreads

As of June 16			Eastern September 1995			Western Annual 1995		
Call spread	Price bid/ask	Rate on line %	Call spread	Price bid/ask	Rate on line %	Call spread	Price bid/ask	Rate on line %
45/65	6.5/7	32.5/35	20/30	—/—	—/—	30/40	0.3/—	3/—
50/70	5.9/6.1	29.5/30.5	30/50	—/—	—/—	30/50	—/—	—/—
60/80	4/6	20/30	50/70	0.6/—	3/—	—/—	—/—	—/—
100c	8.5/12	8.5/12	60/80	—/—	—/—	—/—	—/—	—/—
150c	4.5/5.5	9/11	—/—	—/—	—/—	—/—	—/—	—/—

Total volume: 24 Total open interest: 2,368  
For quotes, call the CBOT trading floor at 312-341-3342. For general information, call 312-435-3674.  
Source: Chicago Board of Trade

## British Issues

June 15 Companies	Price	P/E	Div. yield	1 week high-low	
Comml Union	609	12.2	33.0	5.4	609-601
Genl Accident	619	9.1	36.3	5.9	619-600
Gdn Royal Exch	197	N/M	10.3	5.2	201-196
Independent	290	8.1	11.9	4.1	290-288
Royal	324	6.1	15.0	4.6	324-316
Sun Alliance	344	11.6	19.7	5.7	344-337

Brokers	Price	P/E	Div. yield	1 week high-low	
Bradstock	63	7.1	7.1	11.3	63-63
Fenchurch	154	10.8	10.0	6.5	157-154
CE Heath	221	13.9	20.0	9.0	238-221
JIB Group	128	11.1	9.4	7.3	132-128
Lloyd Thmpson	170	11.8	9.8	5.8	182-170
Lowndes Lmbrt	151	8.9	10.4	6.9	152-151
Nelson Hurst	148	11.5	8.3	5.6	148-148
PWS Holdings	17	N/M	0.8	4.7	18-17
Sadgwick Grp	145	13.2	8.1	5.6	148-142
Steel Bri Jones	93	10.9	11.3	12.1	93-93
Willis Corroon	157	N/M	8.3	5.3	160-157

Source: Philip Olsen, London \* Estimated 1994 data

# BI Industry Stock Report JUNE 12, 1995, THROUGH JUNE 16, 1995

BROKERS	Price	Weekly % change	Year to date % change	Annual		Vol.(000)	\$ Div.	% Yield	P/E	Book value	Mkt./Bk. value	Price	Weekly % change	Year to date % change	Annual		Vol.(000)	\$ Div.	% Yield	P/E	Book value	Mkt./Bk. value			
				High	Low										High	Low									
Acordia Inc.	NYS	31.13	1.63	-7.09	34.50	24.63	8	0.72	2.31	15	13.24	2.35	NAC Re Corp.	NDO	30.50	1.67	-8.96	35.25	24.25	232	0.20	0.66	15	19.75	1.54
Alexander & Alexander	NYS	24.00	0.52	29.73	26.44	15.63	273	0.10	0.42	-13	6.08	3.95	National Re Corp.	NYS	31.63	1.61	20.48	32.00	22.25	79	0.16	0.51	18	17.31	1.83
E.W. Blanch Holdings Inc.	NYS	18.88	3.42	-8.48	23.00	17.50	184	0.40	2.12	15	4.55	4.15	Navigators Group	NDO	15.00	0.00	3.45	19.75	12.75	6	0.00	0.00	-19	10.21	1.47
Gallagher Arthur J. & Co.	NYS	35.13	2.18	9.77	36.38	29.00	48	1.00	2.85	15	8.48	5.42	Nobel Insurance Ltd.	NDO	9.94	0.63	20.45	10.00	7.63	12	0.20	2.01	4	6.84	1.45
Hilb, Rogal & Hamilton	NYS	12.75	0.00	5.15	12.88	10.50	68	0.56	4.39	15	4.72	2.70	Ohio Casualty Corp.	NDO	31.38	-0.40	11.06	34.25	27.00	224	1.52	4.84	11	24.68	1.27
Marsh & McLennan	NYS	80.50	1.58	-1.58	88.38	71.25	483	2.90	3.60	16	19.40	4.15	Old Republic Int'l	NYS	26.00	1.46	22.35	26.38	18.88	400	0.52	2.00	10	24.60	1.06
Poe & Brown	NDO	24.25	3.74	11.49	24.25	19.00	41	0.48	1.98	16	4.49	5.40	Orion Capital Corp.	NYS	39.38	2.27	11.70	39.75	28.13	39	0.80	2.03	10	25.86	1.52
BROKERS AVERAGE			1.9	6.0					2.5	11			Partner Re Holdings Ltd.	NDO	25.00	3.09	20.48	25.50	18.50	755	0.40	1.60	8	N.A.	N.A.
ACE Ltd.	NYS	28.00	3.70	19.79	28.38	20.75	833	0.58	2.00	-12	22.45	1.25	Penn-America Group Inc.	NDO	9.27	-2.47	25.64	9.75	6.50	183	0.12	1.30	11	6.21	1.49
Acceptance Insurance Cos.	NYS	14.25	-2.58	-5.00	18.00	12.63	79	0.00	0.00	8	9.83	1.45	Philadelphia Cons. Holding	NDO	14.19	1.34	15.82	14.38	9.50	84	0.00	0.00	14	8.43	1.68
AEON N.V.	NYS	33.75	-1.10	32.87	34.63	20.41	50	3.60	10.67	13	43.84	1.45	Phoenix RE Corp.	NDO	23.50	3.30	-16.81	29.25	21.00	236	0.60	2.55	4	22.86	1.03
Aetna Life & Casualty	NYS	61.88	2.27	31.30	62.63	42.25	2045	2.76	4.46	12	57.21	1.08	Provident Life	NYS	24.00	0.52	10.34	29.88	20.50	110	0.72	3.00	11	27.09	0.89
AFLAC Inc.	NYS	43.63	1.75	36.33	44.75	31.63	277	0.52	1.19	15	57.21	0.77	Reliance Group Holdings	NYS	6.50	1.96	25.30	6.75	4.88	436	0.32	4.92	10	3.48	1.87
Allied Group Inc.	NDO	29.00	0.87	17.17	31.00	22.00	58	0.68	2.34	6	23.43	1.08	Relistar Financial Corp.	NYS	38.13	-0.97	31.47	39.50	27.00	211	1.00	2.82	11	24.81	1.54
Allmerica Prop. & Casualty	NYS	21.00	0.60	24.44	21.88	14.25	55	0.16	0.76	9	19.45	1.24	RLI Corp.	NYS	27.25	2.83	32.93	27.63	19.88	16	0.64	3.35	11	20.51	1.33
Allstate Corp.	NYS	30.00	3.45	26.32	31.63	22.63	1442	0.78	2.80	10	19.60	1.53	St. Paul Companies	NYS	49.25	0.00	10.06	51.88	38.50	1150	1.60	2.35	9	31.88	1.54
American General	NYS	34.63	2.97	22.57	35.50	25.63	1221	1.24	3.58	14	20.39	1.70	SAFECO Corp.	NDO	58.44	1.63	12.38	59.75	46.75	726	2.12	3.63	12	46.94	1.24
American Heritage Life Ins.	NYS	20.38	3.82	7.24	20.38	16.25	28	0.68	3.34	11	12.42	1.53	SCOR U.S. Corp.	NYS	8.63	-4.17	2.99	12.25	7.50	17	0.20	2.32	15	13.60	0.63
American Indemnity/Fin'l	NDO	10.50	-2.33	3.70	12.75	10.00	3	0.28	2.67	3	15.92	1.64	Seibels Bruce Group	NDO	0.88	0.00	-65.00	0.88	0.88	52	0.00	0.00	-1	1.05	0.83
American International	NYS	113.38	0.11	15.69	119.50	86.38	2393	0.51	0.45	16	49.75	0.66	Selective Ins. Group	NDO	32.25	0.00	27.72	32.75	23.25	182	1.12	3.47	10	23.36	1.38
American Re Corp.	NYS	38.25	3.38	18.80	39.88	25.25	418	0.32	0.84	15	16.85	2.28	Sphere Drake Holdings	NYS	15.75	2.44	13.51	16.50	10.75	24	0.16	1.02	8	13.15	1.20
Aon Corp.	NYS	36.13	-0.34	12.89	38.00	29.25	770	1.36	3.76	11	21.96	2.27	TIG Holdings	NYS	24.25	0.00	29.33	24.50	17.00	339	0.20	0.82	22	17.25	1.41
Argonaut Group	NDO	30.75	2.50	8.85	31.25	27.00	81	1.32	4.29	11	29.80	2.27	Titan Holdings, Inc.	NYS	10.63	0.00	8.97	11.00	7.38	47	0.24	2.26	8	9.31	1.14
AVEMCO Corp.	NYS	17.63	2.17	14.63	18.25	13.38	17	0.44	2.50	14	6.30	1.65	Torchmark Fire & Fire	NDO	56.00	-1.10	-7.82	65.63	49.88	13	0.44	0.79	-	57.72	0.97
Baldwin & Lyons Inc.	NDO	16.25	0.00	10.17	17.63	14.00	2	0.32	1.97	12	13.56	1.03	Torchmark Corp.	NYS	39.50	1.28	14.49	41.50	32.38	475	1.12	2.84	11	17.49	2.26
Berkley W.R. Corp.	NDO	35.38	-0.35	-5.67	40.88	32.50	255	0.48	1.36	19	36.47	1.20	Transatlantic Holdings	NYS	64.63	1.77	15.66	65.50	47.75	39	0.40	0.62	13	32.43	1.99
Berkshire Hathaway Inc.	NYS	22300.00	0.00	9.31	25200.00	16100.00	0	0.00	0.00	55	9157.79	2.44	Transnational Re Corp.	NDO	19.88	0.63	-15.43	25.50	18.75	83	0.00	0.00	6	N.A.	N.A.
Capital RE Corporation	NYS	25.13	-0.99	-8.22	27.38	20.00	6	0.20	0.80	9	21.48	1.17	Travelers Corp.	NYS	42.00	1.20	29.73	45.00	30.38	2722	0.80	1.90	11	24.26	1.73
Capsure Holdings Corp.	NYS	14.00	5.66	-4.27	16.13	12.13	45	0.00	0.00	13	13.72	1.02	Trenwick Group Inc.	NDO	43.75	-0.57	3.24	45.75	36.00	44	1.12	2.56	11	29.20	1.50
Chubb Corp.	NYS	81.75	0.00	5.65	85.25	68.63	625	1.96	2.40	12	48.40	1.69	United Fire & Casualty	NDO	29.00	1.75	4.82	29.81	26.25	1	0.80	2.76	8	28.96	1.00
CIGNA Corp.	NYS	75.13	2.21	18.07	78.88	59.00	853	3.04	4.05	7	80.98	1.96	Unitrin	NDO	48.75	0.00	13.37	51.50	38.50	207	2.00	4.10	15	38.64	1.26
CNA Financial Corp.	NYS	85.63	1.18	31.98	85.88	60.00	41	0.00	0.00	20	73.83	0.93	UNUM Corp.	NYS	46.75	1.91	23.84	50.00	35.13	1011	1.06	2.27	24	27.78	1.68

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