

MAY 27, 1985

# business insurance

update

## Oregon judge blocks plan to spin off part of North-West

PORTLAND, Ore.—A group of Louisiana-based employers and insurance agents failed to convince a Multnomah County Circuit Court judge that its plan to save a portion of Oregon-based North-West Insurance Co. had "any basis in law."

In an opinion issued May 16, Judge R.P. Jones said the court has no right to interfere in the liquidation of North-West. The insurer was placed

*Continued on next page*

Reporting weekly for corporate risk, employee benefit and financial executives/\$1.50 a copy: \$52 a year

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## Federal report urges restrictions on FSAs

By JERRY GEISEL

WASHINGTON—Flexible spending accounts should be prohibited because they actually undermine health care cost containment and reduce federal tax revenues, an unreleased government study says.

Because of FSAs' adverse effects on health care cost containment and the loss of federal revenues caused by their use, "The natural, sound policy response to these arrangements is to prohibit them," says a draft of an unreleased report prepared by the Department of Health and Human Services and obtained by *Business Insurance*.

But, because FSAs have become so widespread, the HHS study suggests that it would not be politically feasible to ban them. Instead, "Policies that seek merely to restrict the use of FSAs will be advanced."

During the past several years, hundreds of employers have established FSAs, which are individual spending accounts funded by employers and/or employees that provide for pretax reimbursement of certain non-taxable benefit expenses.

FSAs often are set up by employers to make more palatable their efforts to shift health care costs onto employees.

The study suggests that, at a minimum, FSAs should be barred from reimbursing employees for their share of health plan premium contributions. In addition, FSAs should not be used to reimburse employees for health-related services—for instance, vision care—that are not covered under a health plan, the study says.

These findings and recommendations are contained in the HHS study entitled "A Study of Cafeteria Plans and Flexible Spending

*Continued on page 79*

## Delta Holdings asks court to void Elkhorn purchase

By DOUGLAS McLEOD

NEW YORK—Delta Holdings Inc.—whose loss-ridden Delta America Re Insurance Co. subsidiary faces rehabilitation in Kentucky—is suing one of its own shareholders in order to rescind its 1983 purchase of Delta Re.

Delta Holdings charges in a lawsuit filed earlier this month that National Distillers & Chemical Corp., Delta Re's previous owner and now a Delta Holdings shareholder, understated the reinsurer's loss reserves, overstated its net worth and fraudulently concealed the company's true financial condition in the sale negotiations.

National Distillers said at the time of the Sept. 30, 1983, sale that the net worth of Delta Re—then known as Elkhorn Re Insurance Co.—was \$18 million.

But Elkhorn actually was insolvent at the sale date—based on subsequent loss development—by \$48 million, the complaint charges.

Delta Holdings' lawsuit asks for a rescission of the sale, return of the \$18 million purchase price and damages of more than \$36 million intended to restore the holding company to its financial position prior to the acquisition.

Failing that, Delta Holdings is demanding a variety of damages amounting to more than \$120 million.

National Distillers was expected to file an answer to

the complaint last Thursday denying all of Delta Holdings' allegations.

Meanwhile, the Kentucky Department of Insurance has filed for a court order directing rehabilitation of Delta Re, which the department says was insolvent by \$66.7 million at the end of 1984.

The board of directors of Delta Holdings did not voluntarily seek rehabilitation for Delta Re, according to Edward L. Fossett, the department's general counsel.

However, Delta Re admitted in an answer to the department's rehabilitation petition that it is insolvent.

Delta Re voluntarily stopped underwriting earlier this year following an Insurance Department examination (BI, March 4).

The department had offered to allow Delta Holdings to run off Delta Re's business rather than force the rehabilitation, according to Mr. Fossett.

But, Delta Holdings did not agree to the offer's terms, one of which was the injection of additional capital into Delta Re, he said.

Delta Holdings, an insurance and reinsurance holding company, was formed in April 1983 by the captive insurance company pioneer, The Reiss Organization. Capital was contributed by 26 U.S. and European corporations, including National Distillers.

Reiss, well known for successfully managing captives

*Continued on page 76*

## Outlook for federal tort reform crumbles

By JERRY GEISEL

WASHINGTON—The chances that Congress will enact federal product liability reform legislation appear to be crumbling, though observers say it's too soon to completely write off the proposal.

Employers and insurers that support the legislation, which would pre-empt varying state product liability statutes with a uniform federal tort law, suffered a major setback earlier this month when the Senate Commerce Committee—on an 8-8 vote—failed to approve the bill, sponsored by Sen. Robert Kasten, R-Wis. (BI, May 20).

Instead of sending the bill to the full Senate for consideration, the Commerce Committee decided to hold new hearings on whether the bill should be amended to include a victim compensation mechanism.

Such a system would make it easier for

product-accident victims to collect damages in cases in which it is difficult to determine whether a product manufacturer or the victim was at fault.

The addition of such a victim compensation amendment to the tort reform bill is overwhelmingly opposed by insurers, while the issue could split business support for the bill at a crucial time.

The failure of the proposal to win Commerce Committee approval—a hurdle it has cleared in the two previous congressional sessions—is a very serious development, said Roger Levy, vp-government affairs for the Independent Insurance Agents of America in

Washington. "The bill has been knocked off the track."

However, Washington observers are not interpreting the Commerce Committee vote as a signal that Congress has tossed the Kasten bill, S. 100, into a legislative trash can.

"The issue is not dead in the Commerce Committee," insists James A. Anderson, director of government relations for the Washington-based National Assn. of Wholesaler-Distributors, a major backer of the Kasten bill.

Manufacturers have been lobbying for four years for a uniform federal product liability bill, like the Kasten bill, because it would

offer them more protection from product liability suits.

For example, the Kasten bill would bar product liability suits in cases where a capital goods product was more than 25 years old. It would also bar the use of the strict liability theory in cases where the design of the product was alleged to have caused the accident.

Under strict liability, it is only necessary for a plaintiff to prove that the product was defective; it is not necessary to prove the manufacturer was negligent in designing or manufacturing the product.

The Kasten bill also would specify that judges—not juries—would award punitive damages in product liability lawsuits. And to win punitive damages, a plaintiff would have to prove the manufacturer acted with "reckless disregard" for the safety of product users.

*Continued on page 77*



Court ruling limits defense coverage for defendant in asbestos litigation

Page 2

Ohio workers file \$1.1 billion suit against employer, chemical firms

Page 2

## update

## North-West rescue blocked

Continued from previous page  
in liquidation Dec. 4 (BI, Dec. 10, 1984).

The judge's opinion was in response to a "rescue plan" filed with the court March 15 by the Louisiana group, known as the Committee of Insureds and Agents (CIA). That plan called for creating a new insurer in Louisiana by spinning off North-West's business written by Mid-Continent Underwriters Inc., its New Orleans-based managing general agent. Most of that business—state and federal workers compensation, marine and general liability—was written on a surplus-lines basis in Louisiana and several other states.

The CIA was assessing the court opinion last week to determine whether to appeal, said CIA attorney Cliffe Laborde.

Meanwhile, Oregon Insurance Commissioner Josephine M. Driscoll, who is the liquidator, said she will now close North-West's Louisiana office. She noted guaranty funds in states where North-West wrote on an admitted basis have been paying claims.

In a separate order filed May 21, the judge approved distribution of funds placed in a joint account by several employers that had self-insured retentions on policies with Mid-Continent. North-West required larger employers to accept a self-insured retention of \$25,000-\$100,000 per occurrence (BI, Oct. 29, 1984).

No claims have yet been paid through the liquidation.

## Revised tax plan to be unveiled

WASHINGTON—The Treasury Department's revised tax simplification package will take a much softer line on employee benefits than the department's original proposal, sources say.

The latest proposal, to be unveiled this week, is expected to call for the retention of 401(k) salary reduction plans, but with lower contribution limits and more restrictions on withdrawals. The Treasury's original proposal eliminated 401(k) plans (BI, Dec. 3).

The revised plan also may propose taxing employees on a small part—perhaps between \$10 and \$25 a month—of the health insurance premiums paid by employers. This so-called tax floor would replace the original plan to tax employees on premiums exceeding \$70 a month for individual and \$175 a month for family coverage.

Also, sources say the Treasury may scrap a proposed tax on all employer-paid group term life premiums. Currently, employees are not taxed on premiums paid for up to \$50,000 of coverage.

Sources say the Treasury may propose that tax-free educational and group legal benefits be continued through 1987.

## New Hampshire captive bill dies

CONCORD, N.H.—The New Hampshire Senate this month rejected legislation to permit the formation of captive insurers in the state. The bill, H.B. 696, had cleared the House (BI, May 13). The legislation was modeled after Vermont's liberal 1981 captive law.

## Insurer's officers, auditor sued

NEWARK, N.J.—The Vermont insurance commissioner is suing three former Ambassador Insurance Co. officers, its parent company and its former outside auditor to recover funds to pay outstanding claims in Ambassador's contested liquidation.

The suit, filed last week in U.S. District Court in Newark, seeks \$50 million in compensatory damages and \$3.475 million in allegedly illegal dividend payments. A Vermont judge found Ambassador insolvent by about \$45 million last year and ordered its liquidation, which the insurer is now appealing (BI, Sept. 17, 1984).

The suit names the insurer's parent, Ambassador Group Inc.; Arnold Chait, the insurer's former president, who also heads the parent company; Doris Chait, his wife, who served as the insurer's treasurer; Richard A. Tafro, the insurer's former vp of finance; and Coopers & Lybrand, Ambassador's auditor in 1981-82.

The suit alleges the Chait's and Mr. Tafro breached their fiduciary duty and "fraudulently" and "negligently" misrepresented the insurer's financial condition.

The lawsuit seeks repayment of \$3.475 million in allegedly illegal dividend payments taken by the Chait's and the insurer's parent in 1982-83.

H.J. Henry, senior vp for Ambassador's parent, said the lawsuit was "possibly retaliatory," since it came one week after some "favorable" rulings by Vermont Superior Judge John J. Meaker.

Judge Meaker last week granted Constitution State Service Co. authority to review the insurer's claims files in Vermont so it could estimate the cost of claims-handling services. Ambassador is seeking the review in connection with its plan to sell its liabilities to a reinsurer to stave off liquidation (BI, May 6).

Mr. Henry had not seen the lawsuit and declined to comment further on it or to discuss Ambassador's insurance coverage.

Continued on page 77

## index

A.R.M. exercises	49	Spotlight report	3
Books & ideas	48	Ticker	81
Classifieds	78	Vol. 19, No. 21—Business Insurance (ISSN 0007-6864) is published weekly at 740 Rush St., Chicago, Ill. 60611. Second-class postage is paid at Chicago, Ill., and at additional mailing offices. Postmaster: Send address changes to Business Insurance, circulation department, 740 Rush St., Chicago, Ill., 60611; 312-649-5221. Copyright 1985 by Crain Communications Inc.	
Comings & goings: buyers	50		
Comings & goings: industry	73		
Datebook	56		
Info	34		
Insurance services guide	80		
Legal briefs	49		
Letters	8		
London line	74		
Markets	54		
Opinions	8		
Perspectives	45		

## Court limits defense cover for asbestos defendant

By STEPHEN TARNOFF

PHILADELPHIA—A recent federal court decision limits the amount of defense coverage available to an asbestos defendant from its primary insurer.

U.S. District Court Judge James Giles ruled May 16 that Pittsburgh Corning Corp. is not entitled to unlimited defense coverage under pre-1966 policies written by its former primary insurer, Travelers Indemnity Co.

However, Judge Giles also said in *Commercial Union Insurance Co. vs. Pittsburgh Corning Corp.* that Travelers must continue to defend Pittsburgh Corning in all cases that were pending at the time the policy limits were exhausted.

Thus, Travelers will have to pay defense costs for about 7,600 cases pending at the time it stopped defending Pittsburgh Corning in 1981 when the limits were exhausted, the court said.

The decision also means that Commercial Union Insurance Co., a Pittsburgh Corning excess insurer that has been defending Pittsburgh Corning since 1981, stands to recoup between \$30 million and \$55 million from Travelers, a CU attorney says.

Travelers was Pittsburgh Corning's primary liability insurer from 1961-1970. Commercial Union wrote first-

layer umbrella liability coverage for Pittsburgh Corning over the same period. Travelers also provided Pittsburgh Corning with umbrella layers above CU's layer from 1961 to 1970.

In addition, more than 35 other insurers provided excess coverage to Pittsburgh Corning from 1961 through 1981.

The issue before Judge Giles was the extent of Travelers' continuing duty to defend under the primary policies it wrote for Pittsburgh Corning from 1962-1966.

In an earlier memorandum opinion handed down in December 1981, Judge Giles interpreted Pennsylvania law to hold that Travelers had a continuing duty to defend Pittsburgh Corning, even after the limits of the primary policies were exhausted.

Despite the ruling, Travelers declined to continue paying Pittsburgh Corning's defense costs and subsequently filed a summary judgment motion requesting Judge Giles to clarify how defense costs were to be apportioned between Travelers and Commercial Union. After Travelers stopped defending Pittsburgh Corning, Commercial Union assumes defense responsibilities in 7,600 pending cases under a reservation of rights.

Continued on page 80

## Insurers won't pay full tab for next satellite rescue

By STACY SHAPIRO

LONDON—Underwriters may contribute to another satellite rescue mission—an attempt to "jump start" the Hughes Aircraft Co. satellite lost in April on a space shuttle flight—but they won't pick up the entire tab, an underwriter says.

The attempt to boost the wayward probe into a proper orbit, which will be made on an August shuttle mission, will be "substantially financed" by Hughes, according to one of Hughes' Lloyd's of London underwriters, Stephen Merrett, chairman of Merrett Syndicates Ltd.

But, the probe's underwriters may chip in if the mission is successful, Mr. Merrett adds.

Last year, underwriters led by Mr. Merrett spent \$10.5 million to rescue two other satellites that were lost on a shuttle flight in February 1984 (BI, Nov. 19). They are now trying to resell the probes.

How much Hughes will pay for the mission to rescue the Syncom satellite—and how much the underwriters will pay if the rescue succeeds—was still being worked out last week by Hughes and the underwriters, sources said.

Until an agreement is reached, none of the other principals—Hughes; its broker, Marsh & McLennan Inc. in Los Angeles; and International Technology Underwriters Inc. in Washington, the lead U.S. underwriter on the Syncom risk—would comment on the mission.

However, Frank B. Pipkin, customer services manager at the National Aeronautics & Space Administration in Washington, said, "NASA is very confident we can do the repair. We see it as much simpler than the retrieval of two satellites last year."

The Hughes Syncom satellite failed to reach a geostationary orbit after it was deployed on the April shuttle launch. Astronauts aboard the shuttle then tried to use a makeshift "fly swatter" to flip a switch that would activate the motor on the huge probe, but the attempt failed.

Continued on page 75

## Ranger wants MGA's authority to be restricted

By STEVE TARAVELLA

SANTA ANA, Calif.—Houston-based Ranger Insurance Co. is battling in court to prevent its managing general agent from binding coverages on its behalf, arguing that reinsurance in place may not be valid.

But the MGA, Orient-Pacific Insurance Agency Inc., is trying to dissolve a temporary restraining order prohibiting it from writing business for Ranger until the companies' disputes can be arbitrated.

Ranger says it tried unsuccessfully for several months to restrict Orient's authority to bind insurance in its name, according to papers filed May 10 in Orange County Superior Court in Santa Ana, which granted the restraining order against Orient May 10.

On March 4, Ranger restricted the limits of policies Orient could write, and on April 4 ordered it to stop writing any new business. Both orders were ignored, Ranger says. On May 9, Ranger terminated the MGA agreement, effective November 1985 per the 180-day cancellation notice.

Also on May 10, Ranger served

Continued on page 80

## Ohio workers file \$1.1 billion suit against employer, chemical firms

By CAROL CAIN

COLUMBUS, Ohio—Celanese Corp. and several other major U.S. chemical manufacturers are facing a \$1.1 billion lawsuit filed by 160 former employees of Celanese's defunct Hilliard, Ohio, plant who claim they suffer from occupational injuries.

The lawsuit is the largest such claim filed in the state since the 1982 Ohio Supreme Court decision in *Blankenship vs. Cincinnati Milacron*.

In that precedent-setting workers compensation ruling, the court said employers are no longer protected from employee lawsuits under the exclusive remedy provision of the state's workers compensation act when an employee's injury stems from an "intentional act" by an employer (BI, April 26, 1982).

The U.S. Supreme Court later refused to review the case; since then, hundreds of lawsuits have been filed against Ohio employers based on that decision (BI, Nov. 8, 1982).

In this most recent case—*Sally Neff vs. Celanese Piping System Division*—former employees are charging the corporation, its subsidiaries, a former plant manager and numerous named and unnamed chemical manufacturers with an intentional tort, negligence and

loss of consortium after the workers allegedly were exposed to polyvinyl chloride—PVC—and vinyl chloride monomers—VCMs.

The plant's former employees are suffering from a variety of physical and mental illnesses, including lung and throat cancers, throat polyps, skin rashes and several nerve disorders, according to a clerk for attorney Michael Moore, who filed the lawsuit April 25 in Franklin County Common Pleas Court in Columbus.

The suit asks for a jury trial and is seeking jointly and severally \$500 million in compensatory damages, \$500 million in punitive damages and \$100 million for the employees' spouses and children for loss of consortium.

Three other lawsuits against the same defendants, each with only one employee named as the plaintiff, make the same charges. In those cases, the employees each are seeking \$20 million in compensatory damages, \$20 million in punitive damages and \$500,000 for loss of consortium which brings the total amount of damages sought from all four cases to \$1.22 billion.

Celanese officials would not respond to inquiries about the litigation.

The employees filed their complaint in court rather

Continued on page 75

# Financial guarantees

## Will the light go out if losses start rolling in?

By JUDY GREENWALD

NEW YORK—Financial guarantee insurance is a bright beacon in the insurance industry, attracting new entrants who are earning high premiums and not yet paying big losses.

And there appears to be no dimming its brilliance—the number of new products offered is limited only by the imaginations of the financial guarantee underwriters.

At the same time, demand for the innovative insurance products, which generally enhance the credit-worthiness of business ventures, continues to grow as investors become more security-conscious and demand the backing of insurance before they will commit their money to investments.

In response, a relatively small group of insurers and brokers is investing greater financial and personnel resources in financial guarantee products.

At the same time, however, they acknowledge that certain forces threaten to diminish the glow of the financial guarantee market.

The tightening property/casualty market is reducing capacity available for financial guarantee products.

And, while losses on financial guarantees have been low so far, the nature of these products makes it conceivable that a single risk could produce a catastrophic loss.

Worry about insurers' growing liability for financial guarantees is prompting state insurance regulators to develop new regulations governing financial guarantees (see related story).

Independent of state regulators, the two major credit-rating organizations, Standard & Poor's Corp. and Moody's Investors Services Inc., also are rating financial guarantee insurers, based on their ability to pay claims (see story, page 23).

Nonetheless, the times appear right for financial guarantee insurance. And, the biggest players say there is no stopping them now.

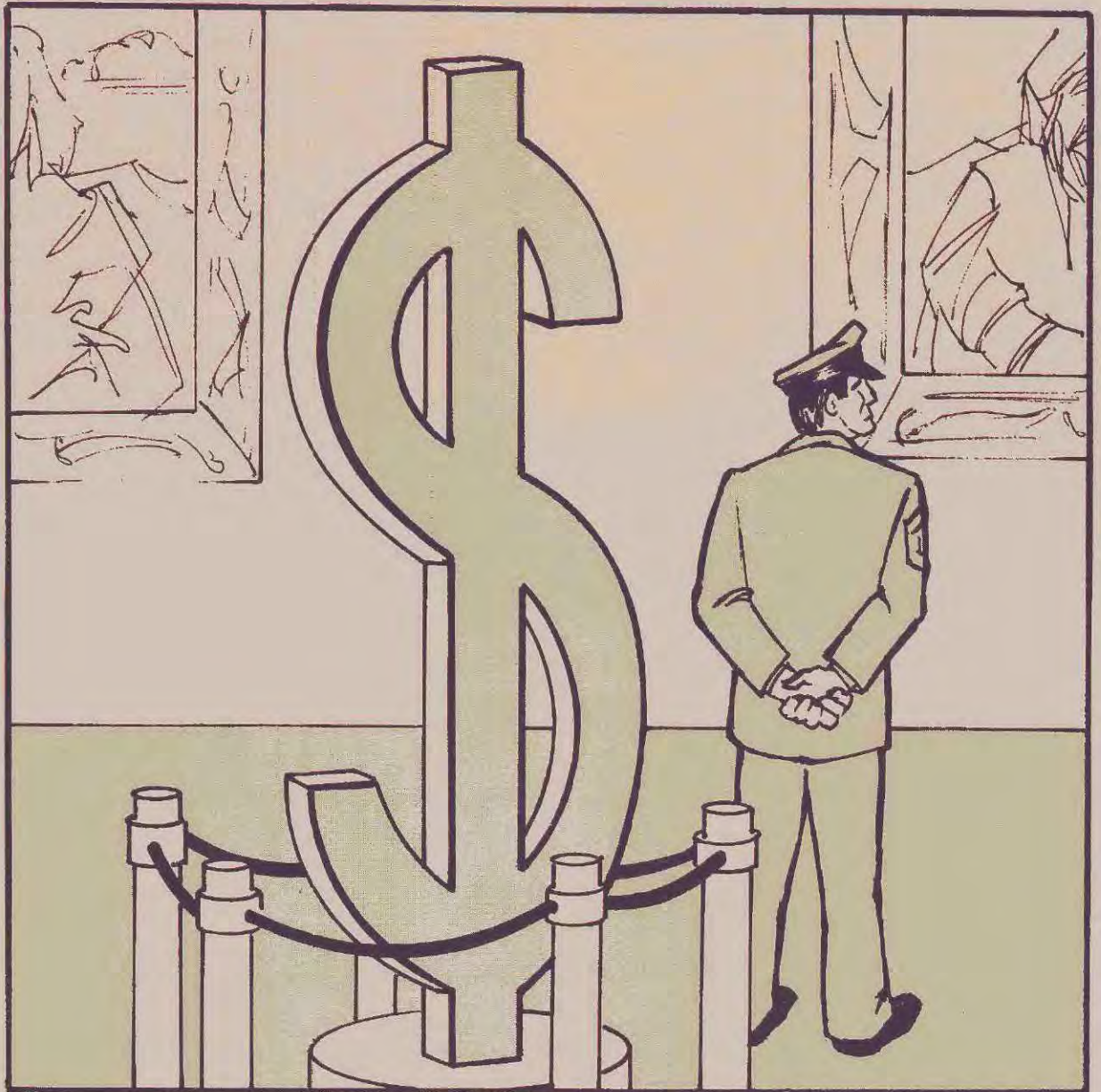
"The market seems to be growing very, very quickly," says Richard H. Napier, second vp of General Reinsurance Corp. in Stamford, Conn.

"The demand is phenomenal," says Lee Carter, vp at Alexander & Alexander Inc.'s Dallas office and a member of its corporate credit enhancement services group.

Consumers are bewildered by the "almost endless" number of investment opportunities before them, explains Michael Djordjevich, president of USF&G Financial Security Co. in San Francisco.

At the same time, Chrysler's near-financial collapse in the late 1970s, the recent runs on savings and loans in Ohio, and the default on \$2.25 billion in municipal bonds by the Washington Public Power Supply System last year have whetted investors' appetite for financial guarantee insurance, he says.

*Continued on next page*



Graphic: Thomas Gianni

## Insurer insolvencies worry regulators

By STEVE TARAVELLA

Afraid huge losses on complex, high-risk financial guarantee insurance could drive underwriters into insolvency, insurance regulators are preparing to exert more control over the market.

- A National Assn. of Insurance Commissioners committee last week began work on a model regulation governing all financial guarantee insurance.
- Legislation has been introduced in California and is being drafted in Illinois to regulate the underwriting of municipal bond guarantees.
- New York expects to have legislation in place by year-end to regulate the entire financial guarantee insurance market in the state.
- The governor of Texas is expected to sign legislation this week absolving the state property/casualty

guaranty fund of any responsibility for financial guarantee claims left unpaid by insolvent insurers.

Currently, no state has comprehensive regulations governing financial guarantee products.

But, the emergence of many innovative insurance products to protect investments in what are more and more frequently very creative and complex business transactions is pushing regulators to action.

The issues they are considering: reserve requirements for financial guarantee losses, capital and surplus requirements for financial guarantee insurers and if all insurers should be allowed to underwrite financial guarantees.

The market now includes insurers that write only financial guarantee products and multiline insurers that write financial guarantees against the same cap-

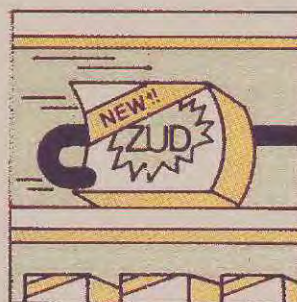
*Continued on page 14*



### Capacity crunch hitting political risk insurers

A lack of reinsurance support is creating a capacity crunch for political risk insurers in both the United States and London. At the same time, however, there is a growing demand among multinational corporations for the coverage, which protects a company against loss of goods or assets due to political strife. So, a

number of new insurers are jumping into the fray and easing the capacity problems, at least somewhat. See Associate Editor Michael Bradford's report, beginning on page 32.



### Interest is on the decline for product recall cover

Interest in product integrity impairment and product recall insurance, which peaked after the Tylenol tragedy in 1982, is declining. The question is, whose interest is missing? Some market observers say lack of interest on the part of buyers caused some insurers to drop or restrict the coverage. However, others say

buyers are still interested in purchasing the policies but insurers, reacting to recent market hardening, are not interested in selling them. See Staff Reporter Diane Lynn Kastiel's report, beginning on page 26.

## Financial guarantees

*Continued from previous page*

"Investors want to sleep well," he says. People figure if they have insurance on their house, why not have it for other assets, he adds.

The volatility of the economy in recent years has increased investors' desire for greater security, says Beverly Wadsworth, a vp at the Continental Insurance Co.

"It's like a second line of defense."

Ms. Wadsworth points out that in some cases the purchase of financial guarantee insurance permits lending institutions and others to remove contingent liabilities from their balance sheets.

The hottest of the financial guarantee products are municipal bond guarantees and limited partnership bonds.

Despite changes in the tax law that could diminish the advantages of investing in municipal bonds or

limited partnerships, the related insurance is expected to continue to flourish (see story, page 19).

Residual value insurance and accounts receivable coverages are also very stable products (see story, page 7).

And, insurers predict strong future demand for commercial paper guarantees, municipal and commercial lease guarantees, multifamily housing bond guarantees and guarantees of student loans for college tuition.

One of the newer and most promising areas for insurers involves the pooling of receivables on auto loans for public offering (see story, page 18).

Buyers don't have to twist insurers' arms to write these coverages.

The high premiums financial guarantees generate is seductive to many underwriters.

For instance, premiums on a residual value policy insuring the future value of six container vessels

for a period of 10 years was \$1.5 million, said Steve Barone, a manager of credit enhancement services at Alexander & Alexander's Winston-Salem office.

To keep up with the demand and take advantage of these lucrative premiums, some insurers and brokers are investing greater personnel and financial resources in financial guarantee products.

Continental, for instance, has increased the number of people it has working on financial guarantee products by about one-third, to 100 from about 75 a year ago, Ms. Wadsworth says.

USF&G, a longtime surety bond underwriter, established a financial guarantee division—USF&G Financial Security Co. in San Francisco—just three months ago. It is managed by Mr. Djordjevich, who previously managed the financial guarantee department at Fireman's Fund Insurance Cos.

And, although Fireman's Fund

last year appeared to be withdrawing somewhat from the financial guarantee market, it is now gearing up to become more heavily involved, says Richard Thiel, vp in charge of Fireman's Fund's corporate financial insurance.

Fireman's Fund recently hired Lew Glucksman, former chairman of securities broker and investment banker Lehman Bros., to run its financial insurance department. And Michael Couto, formerly an investment banker with the American Express International Bank, has joined the Fireman's Fund as a senior vp.

"All of this indicates a strong commitment to financial guarantee insurance," says Mr. Thiel.

"We are re-evaluating and establishing parameters for the business," Mr. Thiel says, including conducting a "thorough review" of how collateral is managed.

The 20-person Fireman's Fund financial guarantee department is

particularly interested in insuring commercial paper, he said.

Brokers also are taking a greater interest in financial guarantee insurance.

Alexander & Alexander Inc. has established, on the national level, a credit services enhancement group of about 10 specialists around the country, says Sandy Clark, a senior vp based in San Francisco and a member of the group.

"It's a very significant move for a broker like ourselves," points out Mr. Clark.

At Johnson & Higgins, about 25 people are working at least part time on financial guarantee insurance. While there has not been a net increase in J&H's staff as a result of its involvement in financial guarantee insurance, more people from other parts of the company have been brought into the area as the business has grown, says Don Matthews, senior vp at J&H.

Marsh & McLennan Inc. has developed a network of 50-60 people who deal in financial guarantee insurance on either a part-time or a full-time basis, says William Duggan Jr., managing director in M&M's New York office and coordinator of its financial guarantee area.

Corroon & Black Corp. has assigned 25 staffers to its financial guarantee division in New York. Its subsidiary, Municipal Lease Insurance Managers Inc., has an exclusive underwriting agreement with Fireman's Fund for municipal lease guarantees.

It also operates IDBI Insurance Managers Inc., which produces industrial development bond insurance for Continental Insurance Co.

Corroon & Black's third financial guarantee subsidiary, D.G. Morris Inc., is a reinsurance intermediary specializing in financial guarantees.

And more brokers are considering moving into financial guarantee insurance.

"We're looking at it very closely here in New York, and also on a national level, to decide how to use our resources and what those resources need to be," says Brian Smith, senior vp at Fred S. James & Co. of New York.

However, growth in this area could be dampened by the overall tightening of the commercial insurance and reinsurance markets, some observers warn.

"The market has quieted down" and capacity has dwindled as insurers concentrate more on underwriting conventional property/casualty insurance, says John Gross, a managing director at M&M.

While there is a lot of talk about financial guarantee insurance being an "up and coming business," actually capacity for it has tightened, says David H. Elliott, vp in charge of financial guarantees at Aetna Life & Casualty Co.

Insurers and reinsurers are both reluctant now to write residual value insurance, says A&A's Mr. Barone. System performance insurance, which guarantees a project will meet performance standards, also apparently has been restricted by the market.

Insurers are turning away from the exotic financial guarantee products saying, "We know how to do property and casualty business," adds Mr. Barone.

They also are currently worried about maintaining the proper premium-to-surplus ratio, and financial guarantee insurance can eat up surplus fast because of the size of the policies, says Peter Brown, vp in Johnson & Higgins' energy group in Chicago, who handles system performance guarantees.

Reinsurance capacity also is tightening for financial guarantee insurance, but is still available for the right deals, says Douglas Morris, president of reinsurance intermediary D.G. Morris. Capacity of

*Continued on page 6*

# IN BUSINESS, THERE'S MORE THAN ONE RISK.

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PreCare is administered nationwide by NWNL Group and MedTrac, whose parent organization has been working with physicians to review hospital care for over 10 years. That gives PreCare the experience that many other utilization review programs lack.

To find out more about how PreCare can reduce your health benefit costs, call your broker/consultant or your NWNL Group Manager. Or send us the coupon below.



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BI 5

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## NWNL GROUP

A division of Northwestern National Life Insurance Company  
Home Office: Minneapolis, Minnesota

## Financial guarantees

Continued from page 4

\$200 million is attainable for quality deals, he says.

Insurers' interest in financial guarantee insurance also could be dampened if they are stung by huge losses. And, the potential for large losses is real.

Fireman's Fund, for example, recently settled a suit for \$55 million involving two financial guarantee policies with aggregate limits of \$6 million. The insurer, however, contends that it will cover most of the settlement cost with the recoveries it will make on the investments it receives in the settlement (see story, page 12).

Everyone expects a significant loss sooner or later, says Karen G. Bellus, an assistant vp in Alexander & Alexander's New York office and a member of its credit enhancement services group.

Insurers' reaction to a loss, she says, will be that of a person learning to ride a horse.

"Until you fall off, you don't know whether or not you're going to get back on," she says.

The risk may not be as great as some fear, Ms. Bellus adds. Often financial guarantee policies are so collateralized that it should mitigate any major loss to the insurers. But, "nobody can be sure," she admits.

The few losses so far are deceptive because the business is so young, says James' Mr. Smith.

Insurers only began writing limited partnership bonds about five years ago. "The first ones are only coming off the books now," he says. "It's still probably too early to tell whether that low loss experience that is currently being reflected is realistic," he says.

The potential for losses on financial guarantee products is almost an "all or nothing" situation, says Richard Erlanger, a vp in A&A's New York office and a member of its credit enhancement services group.

If a house is damaged in a fire, an insurance policy may have to pay on only 15% of the insured value, but if a bond issue defaults, the insurer has to pay off the entire issue, he says.

As a result, insurers are particularly selective about the deals they do underwrite, observers say.

Insurers must be "extra sure" that the quality of underwriting is extremely high, says Mr. Elliott of Aetna. "You just can't afford to take a very serious loss."

"The underlying deal, the underlying people and the underlying risk must make sense," says Mike Tilton, who last week left National Union Fire Insurance Co. of Pittsburgh, Pa., an American International Group Inc. unit where he had been an executive vp.

"Too many people think financial guarantee insurance is the answer to a lot of business-risk type problems," he says. "For every deal that makes sense, 99 probably are some insurance broker's perception of an answer to a business risk." But, the 99 should not be insured, he says.

To take advantage of the good opportunities and stay far away from the bad deals requires special expertise. For example, to underwrite limited partnership bonds, an insurer needs expertise in law, accounting, real estate and taxes, says Val Goldstein, a vp at National Union.

"It requires a new type of talent for underwriting, as well as one that recognizes the changing environment," he says.

Partially in response to the special expertise required to write financial guarantee insurance, a two-tiered marketplace has emerged.

On one level are many conventional multiline property/casualty companies, including AIG, CIGNA, Aetna, Crum & Forster (through its

subsidiary Industrial Indemnity Insurance Co.), CNA Insurance Cos., Fireman's Fund, Continental, Travelers Indemnity Co., USF&G and General Re.

On the second tier are monoline companies devoted to one exclusive type of financial guarantee insurance. They are generally owned, however, by the multiline companies and other financial services corporations that want a share of the financial guarantee market.

This is especially apparent among the insurers specializing in municipal bond guarantees, which insure payments on bonds in the event a municipality defaults.

Municipal Bond Insurance Assn., one of the largest markets for guarantees of tax-exempt bonds, is owned by a consortium of five insurance companies that underwrite a particular share of each MBIA guarantee: Aetna Casualty & Surety Co., which has 33%; Fireman's Fund, 30%; Travelers, 15%;

CIGNA, 12%; and Continental, 10%.

Founding shareholders of the Bond Investors Group Inc. are AIG, Government Employees Insurance Co., Bankers Trust New York Corp., Phibro-Salomon Inc. and Xerox Credit Corp.

Investors behind the Financial Guaranty Insurance Corp. are Kemper Group, General Re, General Electric Credit Corp., J.P. Morgan & Co. Inc., Merrill Lynch & Co. Inc. and Shearson/Lehman Bros. Inc.

Finally, AMBAC Indemnity Corp. in New York, the other large market for municipal bonds, is now being sold by Baldwin United to Citicorp, Xerox, investment banker Stevens Inc., and AMBAC's own officers and directors.

Citicorp's purchase of AMBAC is a natural development for the company, says a Citicorp spokesman. Financial guarantees are "very much a part of the business of banking. It always has been."

However, two insurance industry trade associations are asking a U.S. District Court in New York to block Citicorp's attempt to enter the bond guarantee market.

The American Insurance Assn. and the Alliance of American Insurers filed suit earlier this month to overturn a Wisconsin state comptroller's decision to allow Citicorp to acquire a controlling interest in Verex Indemnity Corp. of Madison.

The Citicorp proposal calls for Verex, in a separate transaction, to become a municipal bond guaranty underwriter by acquiring the business of AMBAC. According to the Citicorp proposal, Verex would assume the name AMBAC Indemnity Corp.

Citicorp's plans must still be approved by the Wisconsin Insurance Department.

If that happens, an AIA spokesman said, the two trade groups would file a similar suit against the

Insurance Department in an attempt to block Citicorp's plans.

The lawsuit filed by the trade groups against the Wisconsin comptroller of the currency says approval of Citicorp's request to acquire Verex will permit "the unlawful entry of Citicorp's and other national banks into the municipal bond insurance and guaranty business" in violation of laws that restrict such practices.

But, it appears to be too late for insurers to lock banks out of the financial guarantee insurance business.

As USF&G's Mr. Djordjevich explains, the three industries of insurance, traditional banking and investment banking are converging in the financial guarantee business.

"Here we're dealing with probably the most dynamic area of the economy," he says. "I see a very good future for a careful group of players." ■

# AMERICAN IN REINS

## Natural catastrophe management: delayed claims can blow you away.

There's no gas, no electricity, no water, no phone. Sometimes, as with the couple in this news photo, there's no house. Just an empty place where their home used to be.

Six hours after the hurricane, you're making your way through the debris, looking for your policyholders. You're wearing your Catastrophe Team hat with your company's name on it. Your policyholders will remember that name with gratitude as long as they live.

They're lucky, because you have a Catastrophe Plan. Your Cat Team moved in right after the storm, bringing loss notices, proof-of-loss forms, drafts, pads, pencils, flashlights, food, clothes — even special Cat Team hats to facilitate passage through military and police blockades.

Your Cat Team is among the first on the scene. You've got to inspect losses at several hundred households and businesses. By pre-arrangement with reliable local contractors

you are able to provide immediate repair work.

If you can't get to the scene right away, competition for contractors and suppliers becomes intense. Prices escalate. Cases stretch out. Additional living expense increases. Policyholders, in deep trouble, become irate. That's when people in desperation turn to legal help, the State Insurance Commissioner and the news media. As a result, your claim costs will escalate and your company's reputation will suffer.

With a Catastrophe Plan, your company completes the job and gets out while others are still getting organized.

Consider a business interruption loss. If you can get a company back in business — even partially or under temporary shelter — you help them keep their customers. Your prompt action will reduce the cost of your business interruption claims substantially.

You've helped your policyholders. You've saved money. But even more important, you've enhanced your company's reputation. In fact, you could gain many new policyholders because of your fast and efficient claim handling.



## AMERICAN REDEFINITION

# Financial guarantee products' popularity varies

By JUDY GREENWALD  
and ROBERT A. FINLAYSON

Despite lots of talk about the growing marketplace for financial guarantee insurance, only a few of these new products are flourishing.

Some financial guarantee products are only holding their own. Others have not taken off yet, but hold great promise. And still others are withering on the vine, victims of the tightening insurance market or general lack of interest.

Among the flourishing products: guarantees of municipal bonds and limited partnerships, which are expected to continue to be very strong products despite expected changes in tax laws affecting the attractiveness of these investments (see story, page 19).

Coverages that are still solid products even though the premium volume they generate may be slipping or increasing only modestly include contract surety bonds, residual value insurance and accounts receivable insurance.

• **Contract bonds.** The growth of contract surety bonds last year was hampered again by the continuing slowdown in public works projects, which is taking its toll on the construction industry.

Basically, a surety bond guarantees monetary payment or completion of a project should a party fail to perform specified acts within a stated period.

Most surety bonds are contract bonds that guarantee that contractors will complete their jobs and

comply with all the requirements of a project. However, surety insurers also write miscellaneous risks, including non-contract obligations and financial guarantees.

While contract bonds formerly accounted for two-thirds of all surety bonds underwritten, they represented just 45% of the \$1.9 billion in premium volume generated by all surety bonds in 1984.

In contrast, other surety products—including financial guarantee products—accounted for 55%, according to Lloyd Provost, president of the Surety Assn. of America in Ise- lin, N.J.

Although premium volume generated by contract bonds increased only 2% in 1984 compared with 1983, the pure loss ratio for contract bonds increased by 28%, he says.

The combined loss ratio for contract bonds in 1984 was 125%, while the combined loss ratio for all surety business was 110%, he says.

The future of contract bonds, however, is rosier, surety experts say, because of an anticipated turnaround in public works construction projects within the next two years.

The federal government is expected soon to release money generated by the 5-cent-a-gallon gasoline tax for federal highway construction, which will pump millions of dollars into the beleaguered highway construction industry.

Mr. Provost says he also sees an increase in concern over the condition of the nation's infrastructure, which includes roads, public buildings, sewer and water systems, air-

ports and a host of other facilities. However, he does not expect public construction to reach the level of the 1960s and 1970s.

Meanwhile, underwriters expect losses to continue through 1985 as a result of the weak financial condition of many public works construction firms.

Many contracts are attempting to "hang on" in anticipation of an upturn in the public works sector, explains W.R. Holley, assistant vp in charge of surety bonds at USF&G Corp. in Baltimore.

However, he says, "Pretty soon the cash flow gets you, and that's when you end up in our claims department."

To pick up the slack in the public construction area, Mr. Holley says that USF&G, like most surety underwriters, is working to convince those involved in private construction projects to make use of surety bonds, too. Such projects currently are not usually bonded.

Mr. Holley says that in the private as well as the public construction area the risk always exists that a contractor will fail to meet project requirements or will go broke and leave the project uncompleted.

"There's definitely a risk and an exposure," he says. "It's just a question of marketing."

• **Residual value insurance.** Residual value coverage is "still viable," but it is "really a product reaching its maturity," says Richard Napier, second vp at General Reinsurance Corp. in Stamford, Conn., which reinsures residual value risks.

"It does seem to have tapered off," he concedes.

Residual value insurance guarantees the value of equipment or other assets in the future, with insurers indemnifying the policyholder if the asset's value falls below a specified level during the policy period. Existence of the coverage permits financial institutions in particular to price leases more competitively and allows all companies in general to strengthen their balance sheets by carrying equipment at the insured residual value rather than at the book value, which is normally lower.

The assets most commonly insured are commercial and corporate aircraft and railroad rolling stock, but machine tools, automobiles, telephone systems and computer equipment have been insured as well.

Morris Roberts, vice chairman of Clarendon Group Services in New York, estimates that the residual value insurance market is generating about \$30 million in premium annually, about the same amount it was generating a year ago.

Clarendon Group Services is a subsidiary company of Clarendon Insurance Co. (Bermuda) Ltd., which is a residual value insurance company.

"It grows in spurts" and is highly sensitive to the economy and changes in the tax law, Mr. Roberts says.

Capacity for the coverage also has been affected by the overall tightening of the commercial insurance market, says Steve Barone, a member of Alexander & Alexander Inc.'s credit enhancement services group in Winston-Salem, N.C.

Insurers and reinsurers alike are saying "we know how to do property and casualty business," says Mr. Barone, and are preferring to stick with that.

• **Accounts receivable insurance.** Accounts receivable, or bad debt, insurance, which protects companies if their debtors fail to

Continued on page 10

# FRONTIERS INSURANCE

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# BUSINESS REINSURANCE

## opinions

# Financial guarantee uncertainties

IS FINANCIAL GUARANTEE insurance a wave of new products that insurers can ride to new profits? Or, is financial guarantee insurance a whirlpool of risky business that threatens to pull underwriters down into insolvency?

Those are the crucial questions now facing insurers and insurance regulators, and definitive answers unfortunately are not obvious. Respected insurance experts who have pondered these issues have come to different conclusions.

It's easy to be caught up in the enthusiasm for writing financial guarantee insurance products. All the talk about insurers reaching new heights of sophistication, satisfying new insurance needs, rejuvenating a tired industry and making new profits by writing financial guarantees is intoxicating stuff.

But quite sobering is the prospect of massive underwriting losses on financial guarantee insurance when one begins to consider the aggregate liabilities that could be assumed by insurers. No one has yet calculated insurers' aggregate exposure already assumed under financial guarantee insurance policies, and insurers and brokers continue to develop new ways to insure billions of dollars of business risks.

Also sobering is the potential for litigation over the meaning of these new policies and the prospect that the policies could be interpreted to provide more coverage than was intended by the insurer.

Already, Fireman's Fund Insurance Cos. has agreed to settle for about \$55 million a suit over the terms of two of its financial guarantee insurance policies that were written to aggregate limits of \$6 million. Granted, the insurer said it expects to cover the settlement cost with recoveries on investments it receives in the settlement. But, future litigation over the coverage provided by financial guarantee insurance policies may not be so advantageous to the insurer.

We share the concern that some insurers may not have the financial strength or financial expertise to write the kind of financial guarantees they are underwriting today and hope to write tomorrow.

But, before we advocate prohibitions against insurers writing financial guarantees, we remind ourselves that some conventional property/casualty insurers have shown they don't have the financial strength or financial expertise to underwrite their conventional lines of insurance.

The solution, then, is to regulate financial guarantee insurers to prevent them from taking on more risk than they can bear, as is the intent in regulating conventional insurers.

There is no time for insurance industry professionals and regulators to waste in developing sound procedures and regulations governing the underwriting of finan-



cial guarantee insurance. The amount of new liabilities assumed under these policies is mounting daily, as evidenced by the flurry of financial guarantee underwriting described in our special report this week.

One regulation that we would endorse would require multiline insurers to segregate the capital and surplus they want to use to write financial guarantee insurance. Then their financial guarantee liabilities alone could be measured against this capital and surplus, giving everyone, including the buyer of the financial guarantee insurance, the information needed to determine if the financial guarantee insurer will be able to meet its obligations.

But while insurers and regulators are debating how to regulate financial guarantee insurance, we have one more question:

Why, at the same time insurers are trying to limit their exposures under conventional liability insurance policies by switching to a claims-made form and including defense costs within policy limits, are insurers anxious to jump with both feet into business with which they have so little experience?

## letters

### Mandated well-child coverage not a sound idea

To the editor: Whose interest is served by mandating coverage for multiple visits to a pediatrician for a well child (*BI*, April 1)?

Will sending a well child to see the pediatrician seven times in its first year of life make the well child more well? Who really pays? Who really benefits? Who has proven this to be a cost-saver? What was their evidence? What cost was saved? Where did those savings go?

With due respect to those who see some social good in this, I perceive nothing more than a blatant attempt by some group of pediatricians to grab a bigger piece of the group insurance pie for themselves.

Economists might well argue over whether the ultimate payer is the employer, the customers who buy its products, the federal government through tax deductibility or the employees whose

wages might have been higher had their group insurance costs been less.

To the extent that it affects wages, however, it affects the lowest-earning employee the most—exactly that employee whose child is of most concern to those who see a social good in this bill.

**Jerome D. Abbott**  
Senior Vp  
Stirling & Weiss Inc.  
New Canaan, Conn.

### Occurrence? Claims-made? That's the question

To the editor: Thank you for the letter from Marsh & McLennan's John P. McLaughlin regarding the proposed commercial general liability forms (*BI*, May 6).

For some time, I have believed that much of medical malpractice "crisis" was contrived by the insurance industry to force the insurance-buying public into be-

coming the industry's errors and omissions carrier. What I can't figure out is whether we have them on an occurrence or claims-made basis.

**James A. White**  
Director—Risk Management  
and Insurance  
Carle Foundation  
Urbana, Ill.

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## Receivables

Continued from page 7

pay their bills, generated about \$60 million in premiums in 1984, up from \$52 million in 1983.

American Credit Indemnity Co. of New York, a division of Baltimore-based Control Data Co. and the lead insurer of accounts receivable insurance, wrote \$42 million in premiums on accounts receivable insurance in 1984.

The next-largest market, Continental Insurance Co., wrote \$15 million in premium volume in 1984 through its affiliate, London Guarantee & Accident Co.

Fidelity & Deposit Co. of Maryland, a subsidiary of Swiss Reinsurance Co. and Zurich Insurance Co., recently entered the accounts receivable market.

Steve Taylor, assistant vp at Continental, estimates that premium volume for the total market will continue to grow about 10% annually.

Policyholders tend to be medium-sized companies that need the protection against an unexpected credit loss that might severely impact their cash flow, he said.

Rates vary, but 0.2% of a firm's annual sales volume would be a "ballpark figure," he says.

American Credit Indemnity expects its premium volume to increase to \$46 million this year, but believes it could write even more bad-debt coverage.

"Probably one of the biggest difficulties we face is a lot of companies don't even know the product is available," says Richard Nelson, senior vp of marketing.

And, a new potential area of growth, Mr. Nelson says, is insuring U.S. companies' accounts receivables due from Western Europe.

Other financial guarantee products that continue to perform strongly include change-in-law coverage and movie completion bonds.

• **Change-in-law coverage.** Despite the tightening insurance market, broad coverage continues to be available to protect investors against changes in government regulations that would adversely affect an industrial development project.

Known as change-in-law insurance, this coverage is designed to repay debt service and provide for operation and maintenance costs for development projects that are held up or made uneconomical by changes in government regulations that occur after the coverage is bound.

This type of coverage is also referred to as force majeure coverage and often is written in conjunction with a builders risk policy, explains Roy Oddy, chairman of MacLean, Oddy & Associates Inc. in Dallas, a subsidiary of Sedgwick Group P.L.C. MacLean Oddy is one of the leading wholesale brokers for force majeure coverage.

Mr. Oddy says that the majority of inquiries his firm gets regarding change-in-law coverage come from banks and financial institutions seeking to protect their investment in a project that could be adversely affected by changes in local, state or federal regulations.

As the financial community becomes more aware of the protection offered by this insurance, it may become difficult for a highly-leveraged industrial development project to obtain financing without first obtaining change-in-law coverage, Mr. Oddy predicts.

Although there has been a contraction of capacity in recent months, Mr. Oddy says his firm has been successful in obtaining "substantial" limits for the coverage.

"We have access to both the London and U.S. markets that write this coverage," Mr. Oddy says, declining to be more specific.

MacLean Oddy has written about \$5 million in premium volume for force majeure coverage during 1985, and Mr. Oddy expects to write a substantial amount more this year.

In addition to change-in-law protection, force majeure insurance provides coverage for other events beyond the control of the insured that would delay completion of a project.

• **Movie completion bonds.** The market for guaranteeing completion of film productions is attracting its share of fans.

"I don't know where all the investors are coming from," says Lindsley Parsons Sr., executive vp at Film Finances Inc., one of the largest film guarantors in the U.S. "We're getting far more requests this year than ever before."

Film Finances in Hollywood, Calif., now guarantees completion of 32 films that are in various stages

of production. That is up from about 22 at this time last year.

The company is seeing profits, he says, despite one unusually large loss recently. Film Finances paid out more than \$1 million to the backers of a rock musical production, which he declined to identify.

Film Finances' main competitor, The Completion Bond Co. Inc. of Beverly Hills, Calif., is currently guaranteeing about 20 to 25 films in various stages of production, about the same volume it insured last year, says Alan Wilson, executive production administrator.

Mr. Wilson has observed an increase in the number of underwriters competing to write completion bonds.

"Everyone seems to think it is easy to underwrite," he says.

As insurers look ahead, they expect commercial paper guarantees, multifamily bond guarantees, student loan guarantee programs

and municipal and commercial lease guarantees to offer them new premium volume.

• **Commercial paper guarantees.** Observers believe commercial paper guarantees will be a hot product in about two years.

This is one area that is "set to grow," says Gen Re's Mr. Napier.

The insurance guarantees that the insured corporation will meet payments on its debts.

Only about 1% of the "billions and billions" of dollars of commercial debt is now insured, says David H. Elliott, vp of Aetna Life & Casualty's financial guarantee department.

But Aetna, which completes 15 to 20 commercial paper guarantees a year, is not planning big growth in its business, Mr. Elliott says. The insurer must be "very cautious, very selective" in deciding which deals to accept, he stresses.

Richard A. Erlanger, vp in Alex-

ander & Alexander's New York office, says the product is ready to take off as soon as capacity is available. And, he predicts that monoline insurers will be formed to write the coverage.

One monoline company expected to specialize in insuring corporate debt, American Financial Assurance Corp., is now organizing.

In the meantime, Mr. Erlanger says, potential clients are "knocking on the front door."

Bob Rose, vp and manager of the financial services group for Johnson & Higgins in New York, agrees that commercial debt insurance will grow in the next two years, led by monoline companies now active in the tax-exempt bond area.

Traditional multiline property/casualty companies will not be the leaders because they are in the midst of "tremendous convulsions" as the insurance market hardens, he observes.

Continued on facing page

# What Group Administration is improved



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Continued from previous page

However, Leon J. Karvelis Jr., executive vp and director of underwriting and research for Municipal Issuance Service Corp., managing agency for the monoline Municipal Bond Insurance Assn., notes that MBIA's constitution currently prohibits it from moving into the corporate debt market.

But Phyllis Smyczek Finn, vp of AMBAC Indemnity Corp., which is also a monoline company active in the tax-exempt market, says taxable corporate as well as municipal debt "is definitely a potential area for growth."

Terrence J. Mech, senior executive assistant in the financial guarantee area at Industrial Indemnity Insurance Co., believes the corporate debt market will grow as the market for tax-exempt bonds declines due to changes in tax laws (see story, page 19).

Industrial Indemnity wrote less than \$1 million in gross premiums

in the commercial paper area last year, compared with about \$90 million in gross premiums in the tax-exempt area, he says.

• **Housing bonds.** Guaranteeing industrial bonds of more than \$10 million, including multi-family housing bonds, will attract insurers, says Tom Purtell, a vp at Alexander & Alexander Inc. and a member of its credit enhancement services group.

Of the \$21 billion of insured tax-exempt bonds issued in 1984, about \$3 billion was for multifamily housing, says Daniel Mushegian, president of FGC Services Inc. in Rye, N.Y., which helps set up the insurance for these programs.

Last year, Industrial Indemnity wrote coverage for about one-third of the market.

Fireman's Fund Insurance Cos., which has been less active in the market this year, also wrote about one-third of the market last year,

says Mr. Mushegian. The remaining share was divided among CNA, Financial Guaranty Insurance Co., USF&G and AMBAC Indemnity Corp.

• **Student loan coverage.** Continental Insurance Co. has recently sold two student loan guarantee policies to the Student Loan Marketing Assn., which makes student loans and markets investments in other student loans.

The Continental policies guarantee that the loans made directly by Sallie Mae will be repaid, either by the parents of undergraduates or by graduate students.

The two-month-old program is insuring less than \$100 million in loans, but it is potentially a very large market, according to Mark Knapp, an assistant vp at Continental. An estimated \$10 billion is loaned to students.

• **Lease insurance.** The mar-

kets for both municipal and commercial lease insurance are potentially "tremendous areas for growth," says Douglas Morris, president of D.G. Morris Inc., a New York subsidiary of broker Corroon & Black Corp.

Lease insurance pays when a lessee defaults.

Municipalities last year leased about \$4 billion worth of personal property, such as equipment and real property, such as buildings, estimates Mr. Morris.

The two major insurers in the municipal lease field, he says, are Continental Insurance Co. and Fireman's Fund, through its managing general agency, New York-based Municipal Lease Insurance Managers Inc., a Corroon & Black subsidiary.

The two insurers combined wrote about \$3 million in premiums last year, Mr. Morris said.

A potentially even bigger market is for commercial lease insurance.

"Upwards of \$60 billion" of property was leased last year, says Mr. Morris. So far, he says, Continental has been the only insurer to introduce a program, although others are considering it.

**The future of some financial guarantee products** currently offered apparently hinges more on commercial property/casualty market conditions than others.

• **Systems performance insurance.** There are two trends in the systems efficacy insurance market, says Henry Maddocks, a vp at Alexander & Alexander Inc. and a member of its credit enhancement services group in Minneapolis:

Demand for the product is growing and the market writing it is shrinking.

System performance insurance, also called efficacy insurance, covers the failure of a mechanical system to meet technical performance standards. It has been written mainly for energy-related projects, such as waste energy plants.

However, primary limits of only \$10 million to \$15 million are available today, down from previous limits of \$50 million, Mr. Maddocks says, because of the overall tightening of the commercial market and partly because many insurers lost money when they went to considerable effort to prepare insurance policies on projects that never materialized.

The biggest market for the coverage, he says, is American International Group Inc.; Lloyd's of London, Hartford Steam & Boiler Co., the Chubb Group and CIGNA are active, brokers say.

Of the 23 system performance policies A&A has placed, 21 were third-party policies, covering the designer or builder of a project rather than the project owner, Mr. Maddocks explained.

Premiums are usually 1.5% to 2% of the project cost, and there is generally a deductible.

Mr. Maddocks estimates that \$10 million in premium volume for efficacy insurance will be written this year.

**Other financial guarantee products** apparently are dead or at least not growing because of lack of interest among buyers. These include weather-related coverages and money market fund guarantees.

• **Weather insurance.** National Union Fire Insurance Co. of Pittsburgh, an American International Group Inc. affiliate, recently discontinued its snow removal insurance program after not issuing a single policy since it was announced in March 1984.

Irene Bruno, municipalities manager at National Union, said there was no interest in the program which was designed to provide coverage for towns or municipalities that were hit with abnormal snowfall. The policy would have paid the cost per inch of removing above-average snowfall, up to a limit of \$1 million.

But the tightening insurance market has significantly driven up the cost of property and casualty insurance for towns and municipalities, leaving them with no money for additional insurance, Ms. Bruno explains.

However, at least one underwriting manager and administrator of the coverage is looking for a great year.

Good Weather Inc. of Jericho, N.Y., perhaps the largest marketer of weather-related insurance, has broken off its underwriting management agreement with AIG to underwrite for Chubb Corp.

Harold Mollin, director of programs and marketing at Good Weather, says Chubb "will promote us more."

Continued on page 12

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## Weather cover

Continued from page 11

Good Weather wrote about \$4 million to \$5 million in premium in 1984 and expects to write \$10 million in premiums in 1986, says Good Weather President Henry L. Fox.

Despite the tightening reinsurance market, Good Weather easily renewed its reinsurance treaties, he says. "We can offer \$20 million to \$25 million in coverage, based on sales," he says.

Despite Mr. Mollin's enthusiasm, brokers are not forecasting sunny days for weather insurance.

"I would have thought that by now industrial usage would have been greater," according to Monte J. Gollub, a Marsh & McLennan Group Associates Inc. vp in New York.

Mr. Gollub says he expected an increase in demand for weather coverage from wine makers, com-

modity traders, snow tire manufacturers and retailers and other manufacturers whose sales are affected by weather conditions.

But the increased demand never materialized.

Frank Sinott, a vp with Johnson & Higgins in New York, says that the federal crop insurance has preempted the private insurance market for crop and agricultural risks.

● **Money market mutual guarantee insurance.** For all practical purposes, the financial guarantee market for money market mutual funds is dead, having never really lived despite optimistic expectations two years ago.

A lack of buyer demand and the tightening insurance market killed this product, which was intended to help money markets compete with the insured money-market accounts offered by banks and thrifts beginning in late 1982.

# Fireman's Fund to pay \$55 million to settle financial guarantee suit

By ROBERT A. FINLAYSON

SAN FRANCISCO—Fireman's Fund Insurance Cos. will pay about \$55 million to settle litigation over two financial guarantee insurance policies it wrote with aggregate limits of only \$12 million.

But, the insurer says it will recover most of the settlement cost from the interests it will obtain in mortgage trust deeds as part of the settlement.

Fireman's Fund agreed to the \$55 million payment to settle a class-action lawsuit filed late last year in U.S. District Court in San Francisco on behalf of 2,000 individuals who had invested \$55 million in a

trust deed investment program sold by Woodson Co. in San Rafael, Calif.

The investors faced losing millions of dollars in interest payments after Woodson filed for bankruptcy in August, even though the mortgages they invested in were backed by real property.

Under the Woodson trust deed investment program, the firm sold investors fractionalized participation interests in second and third mortgages.

Fireman's Fund issued Woodson two \$6 million contractual guarantee insurance policies from 1982 to 1984.

The Fireman's Fund policies en-

abled Woodson to obtain Real Properties Securities permits from the state of California and to promote the investment program as uniquely guaranteed and insured, according to the suit filed against Fireman's Fund by the investors.

Woodson guaranteed timely monthly interest payments to its investors, regardless of the status of its underlying loans, said Elizabeth Cabraser, a partner with the San Francisco-based firm of Loeff & Cabraser and lead attorney for the plaintiffs.

The Fireman's Fund coverage was intended to pay if Woodson failed to make these contractual payments, the court papers allege.

Early in 1984, according to the complaint, Fireman's Fund told Woodson that it would not renew the insurance when it expired in August 1984.

Unable to convince Fireman's Fund to reconsider, unable to obtain replacement coverage and suffering from a high rate of borrower defaults, Woodson filed for reorganization under Chapter 11 of the Federal Bankruptcy Act.

Although Fireman's Fund had written only two \$6 million policies for the Woodson program, plaintiffs' attorneys argued the insurer was liable for the entire amount of the insured investments at the time of the bankruptcy.

Plaintiffs' attorneys contended that the trust deed investments issued by Woodson were securities for purposes of the registration and anti-fraud provisions of the federal securities laws. And, they argued that certificates of insurance issued by Woodson based on the Fireman's Fund policies were an integral component of these securities.

Therefore, the plaintiffs argued that "Fireman's Fund's liability was not limited to the aggregate \$12 million limits of its 'contractual guarantee' policies."

Rather, the suit alleged, the insurer's liability extended to the aggregate face value of all certificates of insurance issued to Woodson investors.

Ms. Cabraser says that if Fireman's Fund had not intended to afford coverage to each investor, it should have stated that in the policy language and the certificates of insurance.

Without this information, Ms. Cabraser says, the investors could not make an informed decision about whether to put money into the Woodson program. Under federal securities laws, she explains, all information material to an investment must be disclosed.

Under the terms of the settlement agreement, Fireman's Fund will pay the full amount of the investors' principal investment, plus any unpaid interest that has accrued on the loans from the date of the original investment to the settlement date.

Fireman's Fund also agreed to pay plaintiffs' attorney's fees and court costs, which have yet to be determined.

In return, the plaintiffs agreed to assign to Fireman's Fund their interest in the mortgages.

"Because it was a class-action suit and the meter was running, we felt this was the best way to respond to the situation," a spokesman for Fireman's Fund explained without elaboration.

The suit originally asked for \$150 million, including an unspecified amount for punitive damages.

The District Court granted preliminary approval of the settlement agreement May 16. The court will review the settlement for final approval June 20.



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## Regulators act

*Continued from page 3*

ital and surplus that supports conventional property/casualty insurance policies.

Insurers, which are eager to have a say in the shaping of any new financial guarantee regulations, already object to some of the proposed regulations.

And, there is debate over whether such regulation should be implemented state-by-state or if a more uniform approach is needed.

The NAIC financial guarantee insurance study committee met for the first time May 17 in New York, headed by New York Insurance Superintendent James P. Corcoran. Its goal is to devise comprehensive financial guarantee regulations that could be adopted by all state regulators.

"We don't want to leave any pebbles unturned," says Michael J. Dugan, director of the Nebraska Insurance Department.

"People are thinking up things to write faster than we can think up what to do about it," exclaims Texas Insurance Commissioner Tom Bond.



"Is all this truly insurance?" he asks. "It is in the sense that a third party is taking a risk, but it certainly falls out of the traditional regulatory framework."

Nebraska and Texas are two of the states with representatives on the committee.

Among the issues the study group will address are financial guarantee insurers' capital and surplus levels, reserving and accounting practices, financial reporting and disclosure methods.

The recent financial problems of several insurers that wrote financial guarantees in California have brought all financial guarantee insurance business under renewed scrutiny.

In late March, the California Insurance Department placed Cal-Farm Insurance Co. into conservation after the Sacramento insurer could not cover payments on \$60 million in bonds that it had insured that were in default.

The insurer, which wrote \$79 million in premiums last year on mainly automobile and homeowners coverage, had written coverage on an additional \$100 million in bonds, according to the department.

The Cal-Farm action followed a March 4 order under which the California Insurance Department took control of Glacier General Assurance Co., a Missoula, Mont., insurer that the department claimed was statutorily insolvent.

Glacier had written surety bonds on mortgages that were part of the mortgage-backed securities that subsequently cost BankAmerica Corp. a \$95 million loss. BankAmerica is now suing Glacier and other involved parties (BI, March 11, Feb. 18).

Mr. Corcoran stresses, however, that the NAIC committee on financial guarantee insurance was not formed in response to these insurers' problems, but rather as a step to prevent insurer insolvencies.

"We don't want regulation by reaction," he said. "It's obvious we have to exercise foresight here, not wait until the place burns down."

The committee may decide to develop one model law for the regulation of municipal bond insurance alone and another for all other financial guarantee products.

California and Illinois also are currently focusing only on the regulation of municipal bond guarantees. New Jersey has regulated such insurance since 1975, and New York has since the early 1970s.

Municipal bond insurance, which has become increasingly popular in the last five years, guarantees bond holders continuing payments if a state or local government defaults on a bond. An estimated 21% of the \$101 million in new long-term municipal bonds issued last year were insured, compared with only 3% in 1979. It is estimated that ultimately as many as 30% of all municipal bonds will be insured.

The largest underwriters of municipal bond guarantees are two monoline, specialty companies: the Municipal Bond Insurance Assn. and AMBAC Indemnity Corp.

Regulators are concerned that insurers could not withstand the huge loss that could accompany a default on a municipal bond.

For example, the value of the municipal bonds on which the Washington Public Power Supply

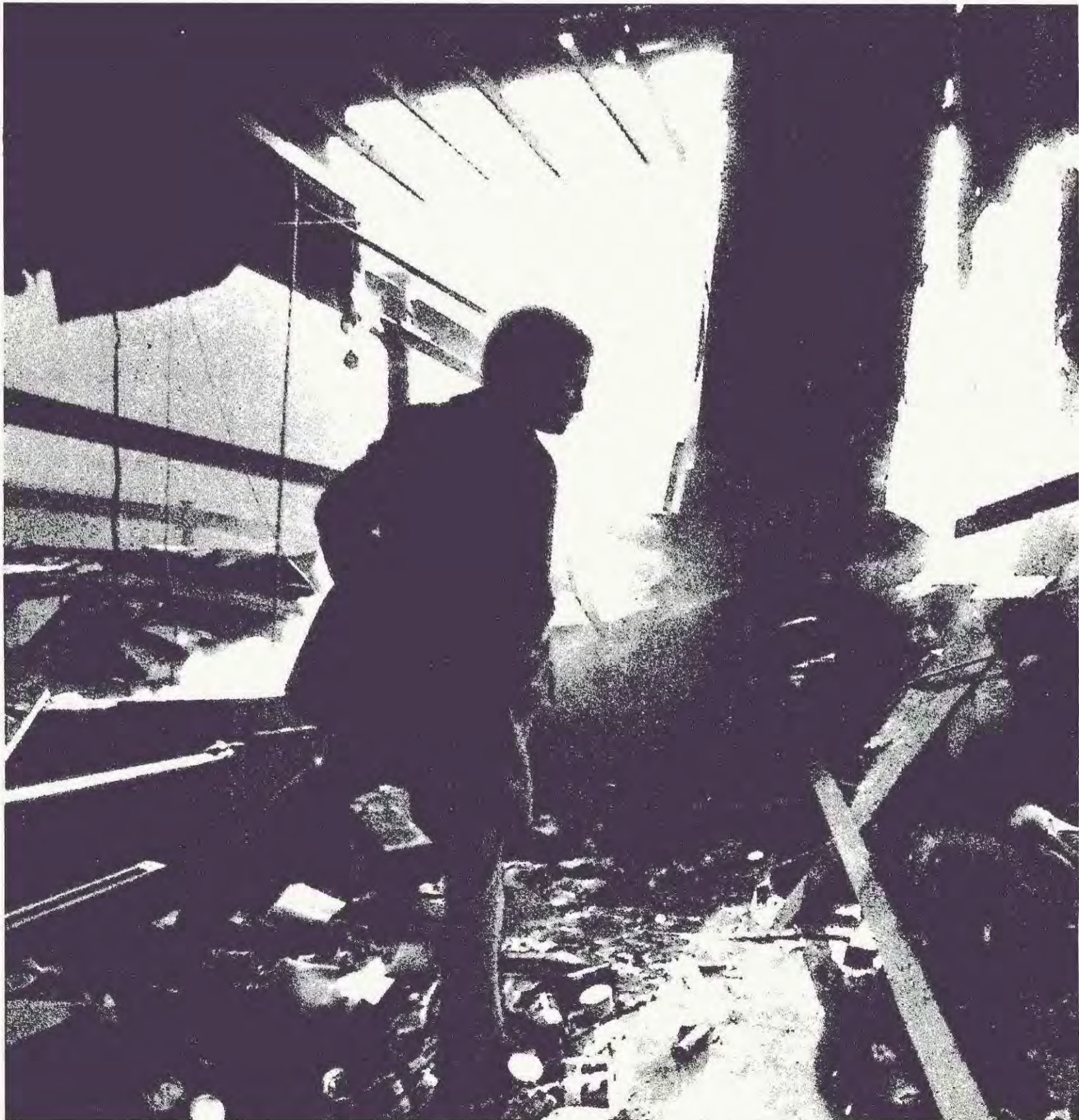
System defaulted last year was \$2.25 billion. In that case, AMBAC insured only a small portion, and its loss is estimated below \$30 million.

"If Lloyd's isn't smart enough to write it, I don't know if anyone is," says Kenneth Smith, an Illinois deputy insurance commissioner, referring to the fact that Lloyd's prohibits the issuance of financial guarantee insurance policies.

Illinois Insurance Department officials have been meeting in Chicago and Springfield over the past month with representatives of insurers' trade associations and financial rating organizations, like Standard & Poor's Corp., to receive their input on regulations to monitor municipal bond guarantees. Mr. Smith said.

The regulation, which is ex-  
*Continued on next page*

# WITH A UAC ADJUSTER THERE'S A LOT GOING FOR



Continued from previous page  
 expected to be drafted by mid-June, would not affect the underwriting of other types of financial guarantees.

Reserving methods among the issues concerning the Illinois department.

To better reflect the exposures, reserves should not be based on a percentage of the premium written in the previous 12 months, as is the

case with conventional insurance, Mr. Smith says.

"You just can't go by (loss) history or these things," he notes.

For example, writing guarantees on bank's loans would have been profitable in 1926, but disastrous just three years later, when the Depression began.

Another provision—which is drawing insurers' ire—would prohibit an insurer from guaranteeing

a bond whose value is greater than 75% of the underwriter's net worth, including contingency reserves.

Illinois also is considering limiting the premiums a multiline insurer can generate from municipal bond insurance to perhaps 20% of its annual premiums, Mr. Smith reports.

It has not been determined whether the percentage would be based on premiums written, premi-

ums in force, new premiums or direct premiums before policyholder refunds, he added.

To avoid such a restriction, some multiline companies might set up monoline subsidiaries to write municipal bond guarantees, he notes.

California Insurance Commissioner Bruce Bunner expects legislation—A.B. 945, which would regulate the insurance of municipal bonds—to pass by July and take ef-

fect Jan. 1, 1986.

The bill has been reworked to incorporate insurer suggestions and may be revised again.

Some critics say the bill now is only a watered-down shell of the original proposal, but underwriters complain that it is so restrictive it will limit insurers' ability to write municipal bond guarantees.

"The California bill is so restrictive that in its current mode, a triple-A insurance company may not even be able to operate there. It's so strict as to be harmful," says one underwriter, who is working with the department on the legislation but asked not to be identified.

Of particular concern to municipal bond insurers in California is the bill's provision establishing a ratio between the insurer's gross aggregate liability for municipal bond guarantees and its capital, surplus and contingency reserves.

The bill requires the insurers to set up a contingency reserve fund equal to half of its earned premiums on municipal bond guarantees.

The California bill now calls for a ratio of 200-to-1, not including unearned premium reserves.

So for every \$1 of capital and surplus and contingency reserves, the insurer can have at any one time an aggregate exposure of no more than \$200, including principal and interest on the bond.

New York allows a 300-to-1 ratio, including half the unearned premium reserves. Illinois had considered a 300-to-1 ratio, not including unearned premium reserves, but dropped the proposal.

Michael Djordjevich, president and chief executive officer of USF&G Financial Security Co. in San Francisco, says he would even support a more conservative 100-to-1 ratio if the insurer's liability were considered not on a gross basis, but were considered net of reinsurance or tangible collateral.

Some insurers also contend that a licensing provision in the California bill is too strict. A company that writes municipal bonds outside the state but is licensed in California for writing other insurance would have to comply within two years with the California municipal bond requirement or lose its license to write any insurance in California.

"The proposal would evict from all insurance business in California those companies whose municipal bond insurance programs do not meet the California regulation. This is the wrong way to approach the goal of a uniform national standard to protect investors wherever they live," Mr. Djordjevich wrote Mr. Bunner April 23 in a letter about the bill.

Another provision, since removed from the bill, would have permitted only monoline companies to write municipal bonds, just as many states allow only monoline companies to write mortgage guarantees.

"That would have put us out of business," says Tom Conneely, v-p-government relations at Industrial Indemnity Co., a subsidiary of Crum & Forster. Industrial Indemnity writes a variety of financial guarantee products, but its thrust is municipal bonds, he explains.

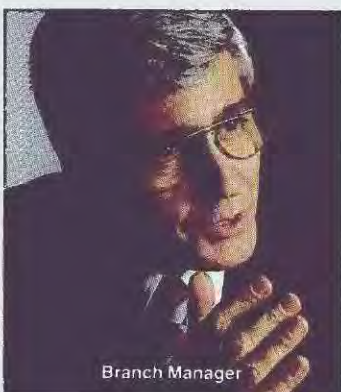
California's bill also requires non-admitted alien reinsurers that are ceded business by municipal bond insurers to have at least \$25 million in combined capital and surplus.

"Whatever you do to the primary company, you have to do to the reinsurer," Mr. Bunner says. But, he admits state regulators can do little to monitor alien reinsurers.

While municipal bonds are generally believed to be the least risky of all guarantee products written today, observers say regulators aren't overlooking riskier coverages, but are taking a "we-have-to-start-somewhere" approach.

In fact, Mr. Bunner calls California  
*Continued on next page*

# ON THE SCENE, YOU BEHIND THE SCENE.



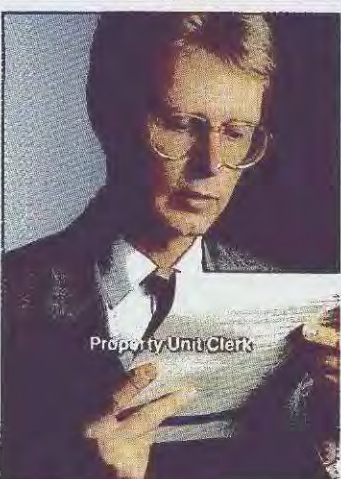
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## Regulators act

*Continued from previous page*  
nia's action "step one" and notes that regulation of guarantees of corporate taxable bonds—which is next on the state's list—will be patterned after its regulation of municipal bond guarantees.

But others, like Mr. Djordjevich, say regulators are acting too quickly, in piece-meal fashion, and without proper information.

Mr. Djordjevich says the financial guarantee market is evolving so quickly that regulators cannot keep up with it. Many insurance commissioners do not truly understand what it is they are attempting to regulate, he maintains.

"A.B. 945 has been presented as a panacea, which it is not. It assumes a panic situation, which does not exist. There is no crisis in municipal bond insurance," he said in his letter to Mr. Bunner.

Financial guarantees have be-

come "the new whipping boy," Mr. Djordjevich says, even though riskier coverages exist, like contract surety bonds, which guarantee that contractors will complete their jobs and comply with all the requirements of the project.

Meanwhile, New York, which has regulated municipal bond guarantees since the early 1970s, is preparing to regulate the entire financial guarantee market.

New York will act by the end of this year, Mr. Corcoran says.

"We don't think the regulatory environment now is responding to what's going on out there," he says. "We don't want to see the already-shrinking capacity in the market flee to this type of 'no-risk' coverage. This is a very serious problem, and the exposures are substantial."

Richard Hsia, a deputy insurance superintendent in New York, agrees: "No state, including New York, has yet adopted an overall strategy to deal with financial guarantee insurance as it's now coming into place. That's exactly what we're trying to do now. We want to come in pre-crisis to prevent it from occurring and to manage it if it ever does."

One type of guarantee New York will look at is the now well-known Citicorp-CIGNA Corp. policy, in which CIGNA assumed some of Citicorp's foreign loan exposures. That policy, bound in May 1984, was scrapped three months ago after disagreement between CIGNA and its political risk treaty reinsurers (*BI*, Feb. 1).

"The question is first, 'Should it be permitted?' and then, 'How?'" says Mr. Hsia.

Mr. Corcoran wants financial guarantee writers to follow sound underwriting practices "and not expose themselves to these catastrophic losses on the rather adolescent theory that there's no risk."

The New York department has not yet determined how to do this.

In addition to regulating the underwriting of financial guarantees, states are taking a second look at whether financial guarantee policyholders should be protected by state guaranty funds.

Texas Gov. Mark White is expected to sign legislation next week relieving the Texas Property & Casualty Insurance Guaranty Assn. from responding to insurance losses from municipal bonds, fidelity bonds, and other surety business.

Texas already excludes mortgage guarantee losses from the fund.

While Illinois' current proposal to regulate municipal bonds does not address the guaranty fund issue, the Insurance Department hopes to amend other legislation to do so, Mr. Smith notes.

The Illinois Insurance Guaranty Fund currently responds if a mortgage guarantee insurer becomes insolvent. The department would like to exclude from the fund mortgage insurance and other financial guarantee claims owed by insolvent companies.

But, Illinois' Mr. Smith points out, even if the guaranty fund were relieved of responsibility for these losses, it would still have to respond to unpaid claims in other lines if a multiline insurer could not pay conventional property/casualty claims because a financial guarantee loss made it insolvent.

The NAIC study committee also is considering the relationship between financial guarantee underwriters and guaranty funds.

Mr. Djordjevich supports removing these coverages from state guaranty funds and suggests that some states might consider establishing a separate guaranty fund that would respond only to financial guaranty claims filed against insolvent underwriters.

California treats municipal bonds as surety products. Thus, they already are not under the California Insurance Guaranty Assn., Mr. Bunner says. ■



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# New financial guarantees springing up

By JUDY GREENWALD

NEW YORK—One of the newer and more promising arenas attracting financial guarantee insurers involves the pooling of receivables on consumer auto loans for public offering.

Salomon Brothers Inc. recently developed a Certificates of Automobile Receivables program for Marine Midland Bank in New York that is insured by National Union Fire Insurance Co. of Pittsburgh, an American International Group Inc. unit.

Marine Midland Bank pooled 12,000 receivables totaling \$60 million on new and used automobiles and light trucks and sold them to a separate trust.

The trust, earlier this month, then made a public offering of certificates on the \$60 million in receivables, available in \$250,000 increments. The certificates, which have a weighted average life of 18.5 months, have an effective annual yield of about 9.7%.

Pat Jehle, vp in Salomon Bros. mortgage finance department, said the limits of the insurance coverage provided by National Union is initially equal to about 10% of the outstanding loan balances and will decline to about 2% as the principal declines.

The 10% represents a "conservative" estimate of the number of auto loans likely to default, although the actual number of defaults probably will be considerably less than 10% of the balance.

A spokesman for National Union was not available for comment.

Ms. Jehle said obtaining the insurance secured a Triple-A rating for the offering, making it more attractive in the market.

The program, she says, is an adaptation of a mortgage-backed securities program Salomon Bros. has offered since 1978. Salomon Bros. may develop this type of pro-

gram for other receivables, too.

Financial Risk Underwriting Agency Inc. in New York, which now specializes in underwriting limited partnership bonds on behalf of the Royal Group and United States Fidelity & Guaranty Co., also is considering insuring public offerings of pooled consumer receivables.

"The potential for this type of product is enormous," says Financial Risk President Robert Ungerleider. In the first eight months of 1984, banks and other financial institutions made \$164 billion in auto

loans, he pointed out.

Receivables on other consumer items—such as boats, trucks, mobile homes and even credit card receivables—could be similarly pooled for public offering, Mr. Ungerleider says.

S&B Insurance Services Co. in White Plains, N.Y., the brokerage arm of the Municipal Bond Insurance Assn., is developing two insurance programs for certificates of receivables, says Joseph Swain, senior vp of S&B.

He agrees the programs, which are still in the development stage, could "cut across a lot of lines," including auto and boat loans, yacht financing, credit cards, consumer loans and mortgages.

As needs arise, other types of financial guarantee products con-

tinue to be developed.

For example, the credit enhancement division of Alexander & Alexander Services Inc. has recently developed a new product to protect cities that are sued when they exercise their right of eminent domain in appropriating property, said Steve Barone, manager of credit enhancement services in A&A's Winston-Salem, N.C., office.

Under terms of the policy, which is underwritten by two insurers that Mr. Barone would not identify, the policy responds if the court rules that a city must pay more for a property than it had offered.

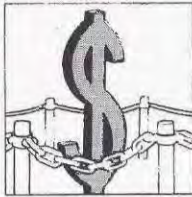
A city in North Carolina has purchased such coverage with limits of \$1 million and a \$150,000 deductible, Mr. Barone said.

Aetna Life & Casualty Co. and

Travelers Corp. recently insured a preferred stock issue by U.S. Steel Co. in Pittsburgh, marking the first time such an offering has been insured, says David H. Elliot, vp in charge of financial guarantees at Aetna.

The stock issue featured a rather rare variable dividend based on a floating rate, and the existence of the insurance made it easier to sell the complex issue, Mr. Elliot says.

Aetna also recently has guaranteed four Euronote issues: a \$100 million, five-year issue for the Rockefeller Group; a \$100 million, seven-year issue for Montagu Placements Ltd.; a \$60 million, five-year issue for Bear Stearns; and a \$50 million, five-year issue for Thyssen Bornsiza, a private Monaco-based company. ■



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# New tax laws won't hurt guarantee market

By JUDY GREENWALD

NEW YORK—Brokers and insurers expect the market for municipal bond and limited partnership guarantees to continue to flourish, even if Congress decides to limit the tax benefits the bonds and partnerships offer to investors.

Underwriters of guarantees for municipal and other tax-exempt bonds note that state and local governments still must issue bonds to raise funds, even if the bonds become less attractive because they are no longer tax-exempt.

And, underwriters of limited partnership bonds expect partnerships to continue to attract investors, even if their value as tax shelters is diminished.

Municipal bond insurance guar-

antees bond holders full payment should a state or local government default on a bond.

Insured bonds generally receive the same rating that either of the two major rating services—Standard & Poor's Corp. and Moody's Investor Services Corp.—assign to the insurer's ability to pay claims (see story, page 23).

Thus, if an insurer's ability to pay claims has been rated AAA by one of the rating services, the municipal bonds insured generally will be rated AAA as well.

The advantage of insured bonds is that the higher rating lowers the interest cost the issuers must pay. And, the insurance can make the bonds more marketable to security-conscious investors.

Depending on the issue, premi-

ums charged for the guarantee generally range from 0.7% to 1.25% of the total principal and interest payable on the bond.

The popularity of the guarantees is growing, observers note.

An estimated 21% of the \$101 billion in new, long-term municipal bonds issued last year were insured, according to industry estimates, and in the first quarter of this year, about 25% of the municipals introduced were guaranteed.

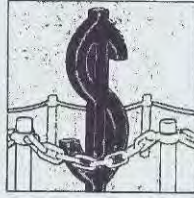
Observers predict the total percentage of municipal bonds that are insured could reach 30%. As re-

cently as 1979, only about 3% of municipal bond issues were insured.

The popularity of the product may not be diminished if Congress approves tax-reform proposals that could significantly cut the number and types of tax-exempt bonds that can be issued.

While the proposals, if enacted, will have some impact on the market, they are not expected to affect the "bread and butter" of the Municipal Bond Insurance Assn., says Lauren M. Miralia, executive vp at Municipal Insurers Service Corp. of White Plains, N.Y., MBIA's managing general agency. MBIA generated \$164 million in premiums on municipal bond guarantees in the year ending November 30, 1984.

Most of MBIA's business, he says,



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is guarantees for general obligation and utility revenue bonds, whose tax status is not expected to be impacted by tax-reform legislation. The legislation is more likely to affect, he said, other elements of the tax-exempt bond market, including bonds issued to finance student loans, bridges and tunnels.

Initially, the proposals would have an impact on the municipal bond insurance market, says Phyllis Smyczek Finn, vp of New York-based AMBAC Indemnity Corp., which, founded in 1971, is the oldest guarantor of municipal bonds. It would not release premium volume information.

"But the bond issues would still have to come to market in one form or another," she said, since municipalities would still have to issue bonds to raise funds.

If what are currently tax-free bonds do become taxable, guarantees would increase their marketability, Ms. Finn points out, noting that AMBAC eventually plans to expand into writing guarantees for taxable bonds.

Schools and bridges still have to be built even if bonds issued for such purposes are taxable, agrees Gerald L. Friedman, chairman and president of New York-based Financial Guaranty Insurance Co.

Mr. Friedman notes that his company is also prepared to write guarantees for taxable bonds.

"If they're going to be financed by municipalities, we'll help them," says Mr. Friedman, who founded his company in 1983. Its 1984 premium volume for municipal bonds was \$61.6 million.

Mr. Friedman estimates the tax proposals could affect about 20% to 25% of the tax-exempt bond market. But the demand for coverage is "so dramatic," it can't materially reduce the growth of the municipal bond insurance industry.

"To the extent (the proposals) reduce tax-exempt bonds coming to market it will affect our market," says a spokeswoman for Bond Investors Guaranty Insurance Co.

She agrees with Mr. Friedman that since an increasing proportion of bonds are being insured, even if fewer bonds come to market, the total number of insured bonds will not necessarily decline.

"I don't think (the proposals) will affect us significantly."

Besides affecting municipalities, the tax proposals may alter the tax status of bonds issued by hospitals, many of which are currently tax-exempt. But insurers that guarantee hospital bonds also downplay the effect of the proposals on their business.

"Hospitals will still have capital needs," says Cliff Cramer, president of New York-based American Health Capital HIBI Management Inc., which underwrites bond insurance for hospitals on behalf of Industrial Indemntiy Co.

About 90% of the more than \$2 billion in bonds HIBI has underwritten since its establishment in September 1983 are tax-exempt, with the remainder taxable, says Mr. Cramer.

Although most of the tax changes that would affect tax-exempt bonds are merely proposals now, one type of tax-exempt bond—industrial development bond issues of less than \$10 million—are already slated to lose their tax-favored status.

Industrial development bonds are tax-free securities issued by municipalities to finance private development intended to strengthen a community's economy.

According to the U.S. Treasury Department, \$14.4 billion in industrial development bonds were issued in 1983, the latest year figures

Continued on next page

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## Tax changes

Continued from previous page  
are available.

Tcm Purtell, vp of Alexander & Alexander Services Inc.'s credit enhancement services division, who is based in Cincinnati, estimates that about 5% to 7% of this market is insured, up from only 2% to 3% a year ago.

"Sunset" legislation, approved by Congress under 1982's Tax Equity & Fiscal Responsibility Act, bars the introduction of most industrial development bonds valued at less than \$10 million after 1986, with the exception of bonds to finance manufacturing facilities, which has been given another two years of life, says a spokeswoman for IDBI Insurance Managers Inc. of New York, a Corroon & Black Corp. subsidiary.

IDBI's sole market is Firemen's Insurance Co. of Newark, N.J., a Continental Insurance Co. subsidi-

ary.

IDBI, she noted, has begun writing guarantees for industrial development bonds for multiple housing projects, which will not be phased out under TEFRA's sunset legislation, she notes.

The firm insured its first housing bond, valued at \$840,000, earlier this month. "We are thinking ahead," she says.

IDBI had insured \$170 million to \$175 million in principal in industrial bonds between 1982 and the end of 1984.

Other insurers that guarantee industrial development bonds include Chicago-based CNA Financial Corp. A spokesman for CNA would not comment.

Just as municipal bond insurers say tax-reform proposals should not have a profound effect on their business, so do insurers that write guarantee bonds for limited partnerships.

Limited partners are individuals who purchase shares or "units" of a larger investment vehicle, which is most likely real estate, but can include cable television operations and racehorses.

The partners make a modest cash down payment for their unit and issue a promissory note payable in annual installments to finance the balance of their investment.

Investors then can take their pro-rata share of the partnership's tax deductions for property depreciation, interest due on development loans and mortgages and other fees incurred by the partnership.

Limited partnership bonds guarantee the investors will make timely payments on the promissory notes they have issued.

Mary Laughlin, a Dallas-based vp with A&A's credit enhancement services division, estimates that \$250 million in gross premiums were written in limited partnership bonds in 1984, up from just \$3 million in 1981.

"So far, the losses have been small," she says.

One of the main reasons for the low level of losses, she explains, is that if an investor defaults, he or she must declare as income all the tax deferrals previously taken.

"That's a pretty severe penalty," she notes.

Also, because the bond backs the "unit" in the limited partnership rather than the individual partner, if an individual investor defaults, the unit can be resold, says Randall Kastner, president of the Milwaukee-based Financial Guaranty Assn., a managing general agency for Industrial Indemnity Co. in San Francisco.

Mr. Kastner noted that the premiums, which are paid up front, usually range from 1% to 1.5% of the value of the bond.

Financial Guaranty Assn. generated \$24.5 million in premium volume from limited partnership bonds in 1984. Mr. Kastner, a former vp at MGIC Indemnity Corp., had an agreement with MGIC under which he serviced all of the limited partnership bonds in MGIC's portfolio in exchange for some additional business. MGIC subsequently stopped underwriting the bonds and sold its business to CNA. Now Financial Guaranty services this business on behalf of CNA, in addition to underwriting on behalf of Industrial Indemnity. CNA would not comment.

Among proposed changes that would affect limited partnerships' tax advantages is lengthening the period of time during which property owned by the partnership can be depreciated from 18 years to as much as 40 years. That could more than cut in half the amount of tax deductions the investor can make in any one year.

In addition, investors are now permitted to deduct interest owed

Continued on page 22

## Paced to go the distance

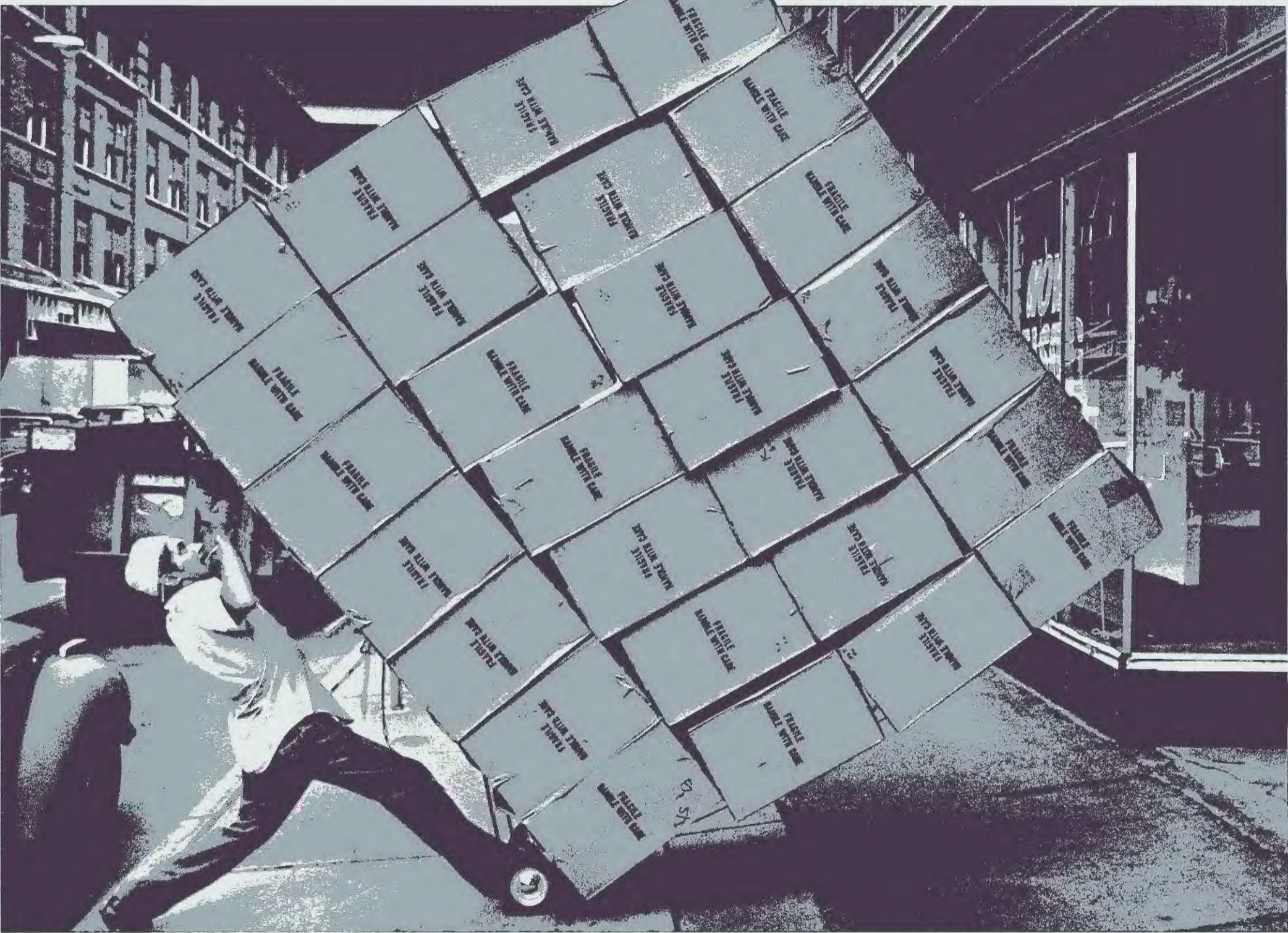
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## Tax changes

Continued from page 20

—but not actually paid—during the tax year, says Mr. Kastner. Congress is considering changing the law so that investors can only deduct interest that has already been paid.

Insurers and brokers active in limited partnership bonds say that while interest in limited partnership bonds was slow during the first quarter, as syndicators cautiously awaited congressional action on tax proposals, the overall growth of the bonds will not be significantly hurt by whatever legislation Congress passes.

They note that, in the future, limited partnerships will be designed to provide economic benefits to investors, rather than principally being tax shelters.

"It's our feeling that the bonds will survive—that the bonds will actually be bigger and better," according to Margaret Connor, an assistant vp in Johnson & Higgins' financial services group in New York.

Tax-reform legislation, she says, "will purge the market of pure tax-shelter deals that really don't make any economic sense."

Ms. Connor estimates that until now, 25% of all limited partnership deals could be classified as "pure" tax-shelter deals, while others were tax shelters to varying degrees. "I think the slack will be taken up by the bonds (for partnerships) that make more economic sense, and investors' appetite will increase as the year comes to an end."

A strong indication of the future of limited partnership bonds, she says, is the announcement by Baltimore-based Fidelity & Deposit Co. of Maryland earlier this month that it intends to underwrite limited partnership bonds for real estate deals.

"We're seeing better deals now because of the proposed changes," says Lee Carter, a Dallas-based vp with A&A's credit enhancement services division.

Financial Guaranty Assn.'s Mr. Kastner predicts that limited partnership bond volume will continue to grow at a 10% to 15% annual rate, even if the tax proposals are enacted.

In one recent transaction, Financial Guaranty underwrote a \$32 million bond on behalf of 330 partners who were purchasing an interest in the Biltmore Hotel in Phoenix.

The partnership had a five-year pay-in period, and Financial Guaranty earned \$850,000 in premium, according to Mr. Kastner.

Whatever Congress does, there will still be advantages to investing in real estate, says Robert Ungerleider, president of the Financial Risk Underwriting Agency Inc., which writes limited partnership bonds on behalf of the Royal Insurance Group and USF&G Corp., generating about \$25 million in premiums annually.

Mr. Ungerleider complained, however, about being "in limbo" as he awaits Congress' next move. One limited partnership real estate bond recently underwritten by his firm was valued at \$2.675 million and written on behalf of 35 partners who were purchasing a garden apartment complex in Austin, Texas. The total premium earned was \$167,000.

A change that might be anticipated as a result of congressional action is a switch in the type of investors who become involved in limited partnership agreements, according to Clifton Brown, an assistant vp with Continental Insurance Co., whose limited partnership bond business generated about \$12 million in premium last year.

Until now, he said, many partners have been wealthy investors interested in tax write-offs. But, if the purpose of the partnership is

switched from a tax shelter to economic investment, those entering the partnerships are likely to be less wealthy and more interested in making money.

Val Goldstein, a vp at National Union Fire Insurance Co. of Pittsburgh, an American International Group Inc. unit, said "very responsible" syndicators are working under the assumption that Congress will alter the tax benefits of the partnerships.

Therefore, they are making sure the deals they propose make good economic sense.

"These are the deals we have always been doing," Mr. Goldstein says.

National Union, which has about 25 people working in its limited partnership bond program, does not release the premiums generated by the bonds, says Mr. Goldstein. One market observer, however, estimated that it totals "at least" \$25 million.

## Insured industrial bond helps firm expand

WINCHESTER, Mass.—An industrial development bond—backed by insurance—can save a growing company money, but be prepared for hard work if you choose this financing route, warns Michael Burnell, vp and treasurer of the Scandia Trading Co. Inc.

The Winchester, Mass.-based apparel company, with about \$30 million in annual sales, used an industrial development bond three years ago to raise \$2.25 million when it decided to consolidate its headquarters into one building.

It decided to buy a former General Motors Corp. office-distribution center facility.

Next came the task of raising the funds to renovate the building.

"Everyone kept coming up with an industrial development bond," says Mr. Burnell.

Industrial development bonds are tax-free securities issued by municipalities to finance private developments.

Scandia decided it had three options:

- The Bank of New England would be willing to

purchase the industrial revenue bond for its portfolio. But the bank wanted to attach a floating interest rate to the bond, which Scandia did not want.

- The company could arrange for a public sale of the bond, using a letter of credit as security.

- The company could purchase insurance to back the bond offering.

Scandia decided to take the last course because not only would it be "slightly more economical" than getting a letter of credit from a bank, but it would not affect the company's borrowing capacity.

Scandia and its investment banker—Tucker Anthony—arranged for IDBI Insurance Managers Inc. of New York to back the offering. The 20-year note raised in the offering carried a 9.5% interest rate.

IDBI earned a \$160,000 premium.

The one drawback of going the financial guarantee route was the complicated legal proceedings involved, says Mr. Burnell. "That is a very involved, time-consuming and usually frustrating process," he says, describing the period as "two months of pure agony."

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# Rating services screen underwriters' strength

By JUDY GREENWALD

NEW YORK—The financial strength of reinsurers is important to credit-rating services evaluating financial guarantee insurance on debt issues.

Both Standard & Poor's Corp. and Moody's Investors Service Inc. rate financial guarantee insurers' ability to pay claims. And, they will increase the rating on insured municipal or corporate bonds or commercial paper only as high as the rating they give the underwriter of the financial guarantee for its claims-paying ability.

Only insurers whose claims-paying ability is rated triple-A, for example, can improve an insured issue's rating to triple-A, the highest rating.

A financial guarantee written for an issue guarantees that the insurer will meet the issuer's obligations if the issuer cannot. Because the insurance can increase a debt's rating, it can reduce the interest rate the issuer must pay investors.

In addition to rating the insurers, New York-based Standard & Poor's is preparing to rate a "large list" of reinsurance companies that participate in treaties for monoline financial guarantee insurers, said managing director Robert Mebus.

The reinsurers' rating will determine how much credit in the S&P rating process the monoline financial guarantee insurer is given for the purchase of reinsurance.

If a reinsurer providing \$100 million of reinsurance has a triple-A rating, he says, then the insurer

gets 100% credit for the reinsurance. But, if the reinsurer has only a double-A rating, then the insurer gets only 50% credit, or credit for only \$50 million worth of reinsurance. If the reinsurer's rating is less than a double-A, the reinsurance will not be recognized.

S & P has given triple-A ratings to about 20 multiline and monoline insurers and reinsurers of financial guarantee insurance, Mr. Mebus said.

Moody's, the other leading rating firm, which has given its triple-A rating to a handful of insurers writing financial guarantees, is

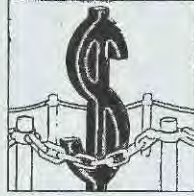
now re-evaluating two of those ratings, said Susan Abbott, associate director at Moody's. One re-evaluation involves reinsurance.

American International Group is more heavily reinsured "than any other company in the world" and, as a result, Moody's is analyzing the stability of its reinsurers, she said.

If AIG were downgraded to a double-A, National Union Fire Insurance Co. of Pittsburgh Pa., an AIG unit active in financial guarantees, also would be re-evaluated, she said.

An AIG spokesman had no comment by press time.

Moody's also is re-evaluating Aetna Casualty & Surety Co.'s triple-A rating, analyzing whether the insurers' liabilities to equity ratio is "out of balance."



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Ms. Abbott noted that because Aetna shares only 33% of the risks of the Municipal Bond Insurance Association, the MBIA's triple-A rating from Moody's will not be affected if Aetna is downgraded.

An Aetna spokesman said discussing the implications of a downgrading "would just be speculation at this point."

Final decisions on the claims-payment ratings of AIG and Aetna will be made within the next few weeks, Ms. Abbott said.

S&P and Moody's differ somewhat in their approach to rating insurers and determining an insured issue's rating.

Mr. Mebus said S&P considers whether the financial guarantee insurer is multiline or monoline.

Monoline companies are those that write only financial guarantees, such as AMBAC Indemnity Corp., and multiline companies include insurers such as Aetna, Fireman's Fund Insurance Cos. and CIGNA, which underwrite conventional property/casualty insurance and financial guarantees.

Part of a multiline insurer's surplus must be available to support its property/casualty lines, but a monoline company's smaller surplus base is exposed only in the financial guarantee area.

A monoline company, Mr. Mebus says, must have a primary capital base of at least \$100 million, and reinsurance of at least \$100 million.

If an issue submitted to S&P for rating is insured by a monoline financial guarantee company whose claims-paying ability has been rated triple-A, it's assumed the insured issue will get a triple-A rating from S&P. This is not necessarily the case when an issue is insured by a multiline company.

S&P also considers whether the financial guarantee insurer can meet the "worst-case scenario," says Mr. Mebus. "Our stress case is the Great Depression," he says.

S&P looks for assurance that the insurer would have sufficient capital to survive a simulated four-year depression. For the monoline company, S&P determines whether there is enough capital in place. For the multiline company, S&P determines whether there is enough capital to support financial guarantee business as well as the basic property/casualty business.

S&P, he says, has just introduced a new methodology in this model. Previously, he said, the determination of needed capital was based on a study of municipal obligations during the Great Depression. The new model, he says, includes 20-25 categories of municipal bonds, divided by type of issuing government or government agency. S&P determines the capital allocation needed to meet each type of risk.

For instance, a state would probably be less likely to default on a general obligation bond in the event of another depression. And, if the state did default, the duration would be shorter than it would be for other bonds, and the financial guarantor would recover almost all his losses, so there would be relatively little "ultimate" loss.

The amount of capital needed, then, for a financial guarantee insurer to support this business would be relatively small, says Mr. Mebus.

On the other hand, more municipal hospitals than states would likely become insolvent, and the insolvencies would probably last longer, so a lot less would be recovered. Therefore, relatively more capital would have to be available to insure municipal hospital bonds.

Using this model, S&P then determines, based on the insurers' mix of business, how much capital is needed, says Mr. Mebus.

Continued on next page

## Credit-rating services

Continued from previous page

Other factors also are considered. For instance, Mr. Mebus says, an insurer with a "well-diversified" book and high standards would need less capital than one with a poor record and a lower quality book.

Among factors S&P looks for in financial guarantee transactions is that the financial guarantor is not assuming a liquidity risk. For instance, if a school district with a 30-year, \$10 million bond defaults, says Mr. Mebus, the insurance contract should not allow for any acceleration of debt that would make the insurer immediately responsible for the entire debt service of the 30-year period. The insurer should only be responsible for the annual debt service as if it were the district.

This is important, says Mr. Mebus, because otherwise, the insurer would "need a lot more capital."

He says insurers and reinsurers writing financial guarantees rated triple-A by S&P are: Aetna Casualty & Surety, AIG, AMBAC Indemnity Corp., CIGNA, CNA Financial Corp., Continental Corp. and Crum & Forster Inc., the parent of Industrial Indemnity Co.

Also, Financial Guaranty Insurance Co., Fireman's Fund, Hanover Re, the Mercantile & General Reinsurance Co., Bond Investors Guaranty, Royal Group, Skandia America Reinsurance Corp., Travelers Indem-

nity Co., Government Employees Insurance Co., Kemper Reinsurance Co., Allstate Insurance, USF&G and the Zurich Insurance Co.

Also, he notes, American Financial Assurance Co., a financial guarantee insurer now being organized, has stated that it will seek a triple-A rating.

Officials of American Financial Assurance declined to comment, saying it was premature.

"We don't think alike in the insurance area," said Ms. Abbott of Moody's, referring to S&P. While S&P works more closely with numbers in evaluating an insurer, "We're a little more subjective about it," she said.

Among factors Moody's considers, she said, is the insurer's equity, the lines of business it writes, its reserves and its financial statements. And, she said, Moody's tries to judge whether the company's financial condition is "appropriately reflected in the numbers."

Moody's does not always upgrade an issue's rating because it is insured. It depends upon the insurance agreement, said senior analyst Michael Molesky.

Moody's only recently began to rate insurers on their claims-payment ability, but it plans to expand its staff to rate more insurers, he added.

In addition to AIG and its National Union unit, Aetna and MBIA, other insurers rated triple-A by Moody's for claims-paying ability are The Travelers Corp. and the Financial Guaranty Insurance Co. ■

## Risk managers can help with financial guarantees

NEW YORK—Risk managers generally are on the sidelines when their companies purchase financial guarantee insurance rather than being involved in the complex transactions, insurers and brokers say.

But, they add, risk managers could play a useful role in the process if they would make the effort to do so.

However, before they attempt to step in, they must do their homework.

Brokers that place financial guarantee insurance say they would like to see risk managers more closely involved because of their expertise.

"Our goal and desire is to have

the risk manager at the table with us," says Steve Barone, who specializes in residual value insurance in Alexander & Alexander Services Inc.'s Winston-Salem, N.C., office.

"We at M&M try to involve the risk manager as much as possible" in the placement of financial guarantee coverages, says William Duggan Jr., managing director in the New York office of Marsh & McLennan Inc.

But, Michael Djordjevich, president and chief executive officer of the San Francisco-based Financial Security Co., a USF&G Corp. subsidiary that specializes in financial guarantee coverages, says the risk manager "has yet to catch up with what has happened" in the financial guarantee area.

Instead, he says, the risk manager has "stayed behind," focusing his attention on traditional insurance.

In most cases, the comptroller or financial vp of a corporation are the ones who navigate the purchase of financial guarantee insurance, says Lee Carter, a vp in Alexander Inc.'s credit enhancement services group.

But, the risk manager has the power to change this situation, observers say.

The risk manager could coordinate the purchase of insurance with his corporation's financial people, trading on his understanding of the strengths and weaknesses of the insurance market, recommends Mr. Djordjevich.

He can also provide his management with good advice on the companies they are about to "get in bed" with, he added.

"Why rely on an insurance broker if you have a person in your shop who knows the insurance company?" he asks.

But, the risk manager has to make an effort to be useful.

"We all have to reach for it," he says. "Very few things are on the platter."

Beverly Wadsworth, a vp at Continental Insurance Co. in New York, believes risk managers are headed in the right direction now.

Risk managers' functions, she says, are becoming increasingly financial in nature, and many are now reporting to their financial vps.

In contrast, 10 years ago the corporate insurance department was isolated from the company's financial operations, she said.

There is a "natural synergy," she says, between risk managers and financial vps because both are concerned with protecting the firm's cash flow.

"The risk manager is becoming much more financial today, appreciating more what financial guarantee insurance can do for the company, and is definitely getting more involved," she says.

However, brokers and insurers warn that a risk manager who decides to take the plunge into financial guarantee insurance had better do his or her homework before approaching the market because financial guarantee insurers are very selective in what they will underwrite.

If the risk manager does not appear to fully understand the financial guarantee he is trying to purchase for his company, he will lose credibility with the insurers and possibly cost his company the protection it is trying to secure, they warn. ■



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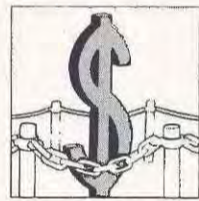
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BI - 5/85

## GMD. BENEFITING THE WORLD WITH COST CONTROL IDEAS.

# Interest waning in product integrity cover

By DIANE LYNN KASTIEL

Product integrity impairment and product recall coverage is becoming an insurance dinosaur, experts say.

However, trying to ascertain the reason for its near-extinction is like trying to figure out the age-old "chicken-or-the-egg" dilemma.

Some suggest that demand for product integrity impairment and product recall coverage waned after the initial surge of interest following the Tylenol disaster in October 1982. They say lack of demand has prompted insurers to stop offering the products.

"During the year that followed (the Tylenol incident), there was a flurry of interest on the part of insureds, brokers and insurance companies to get into (product integrity and recall coverage), but that subsided," explains Ralph Palmieri, executive vp at First State Insurance Co. in Boston, which began offering product integrity coverage in the autumn of 1982 but dropped it a year later.

"Fortunately, there were not many incidences like Tylenol, and so the insurance-buying public didn't seem to see the need for that kind of coverage."

Seven people in the Chicago area died in October 1982 after taking Extra-Strength Tylenol capsules that were laced with cyanide.

John Gross, managing director of casualty products at Marsh & McLennan Inc. in New York, agrees that product integrity impairment and recall insurance "was never a big player. It's an esoteric coverage that got some play during some incidences, but never took hold."

However, other experts insist that buyers are still interested in the coverage but insurers, in response to the hardening market, have stopped writing the coverage or limited capacity severely. The insurers that continue to offer the coverage have increased both rates and deductibles, these experts add.

"(Insurers) are arbitrarily turning up their noses at high hazards," said Bill Richardson, executive vp at Frank B. Hall & Co. Inc. in New York. "Not just because of Tylenol but because they don't need to take those risks to make their premium goals."

Charles L. Ruoff, senior vp at Fred S. James in New York, agrees. "We're having a heck of a time getting our clients' coverage placed on reasonable terms for any kind of coverage."

"A lot of players have left the field, not because the product integrity and product recall coverages have produced underwriting losses, but because they're focusing on using their surplus to underwrite their basic business. They just don't have enough resources to go around."

"I think (risk managers) are looking for (product integrity and recall coverage), but they're not willing to pay the premiums on it," said Warren Brockmeier, a vp at The Wyatt Co. in Chicago and head of its risk management consulting division. "There are some firms buying it, but demand is very limited because of the poor market for it."

Regardless of the reason, the fact remains that the market for product integrity impairment and recall insurance is drying up. Observers' estimates of market capacity range as low as \$5 million to as high as \$75 million. Most are between \$35 million and \$50 million. Most agreed that capacity was as high as \$100 million a year ago.

In addition, rates and deductibles are on the rise.

Tom Rodell, vp and marketing

manager at Alexander & Alexander Inc. in Chicago, says rate increases "are in excess of 100%" while deductibles have doubled.

In addition, the scope of the coverage has narrowed, he said.

"Over the last couple of years we have been able to negotiate some pretty broad contracts," Mr. Rodell said. "And now most underwriters are going back to standard form-type coverage."

"The 'throw-ins' are being thrown out because underwriters don't want to write that coverage," said Mr. Ruoff. "Either they don't have reinsurance for it or they think it should be priced separately and don't have the resources to do that anymore."

Although they are often lumped together, there are distinct differ-

ences between product recall coverage and product integrity impairment insurance:

- Product recall coverage, the more limited of the two coverages, usually pays for the withdrawal of the product from the market, including transportation costs and the cost of destroying or disposing of the product.

- Product integrity impairment coverage, in its broadest form, will pay for all expenses associated with the recall of a product. In addition, it also covers a variety of expenses resulting from the recall, including

loss: profits, public relations or advertising expenses, costs of rehabilitating the product and even the cost of introducing a new product if the reputation of the original product was damaged severely enough to make it unmarketable.

However specific policies vary, both in the exposures covered and the circumstances that trigger the policy.

For example, some policies are triggered only if a product is tainted with after it leaves the manufacturer's plant. Others are triggered by any contamination of the product—even if it was inadvertently caused by the manufacturer. Still others can be triggered by the mere perception—caused by rumors or extortion threats—that the product might be contamin-

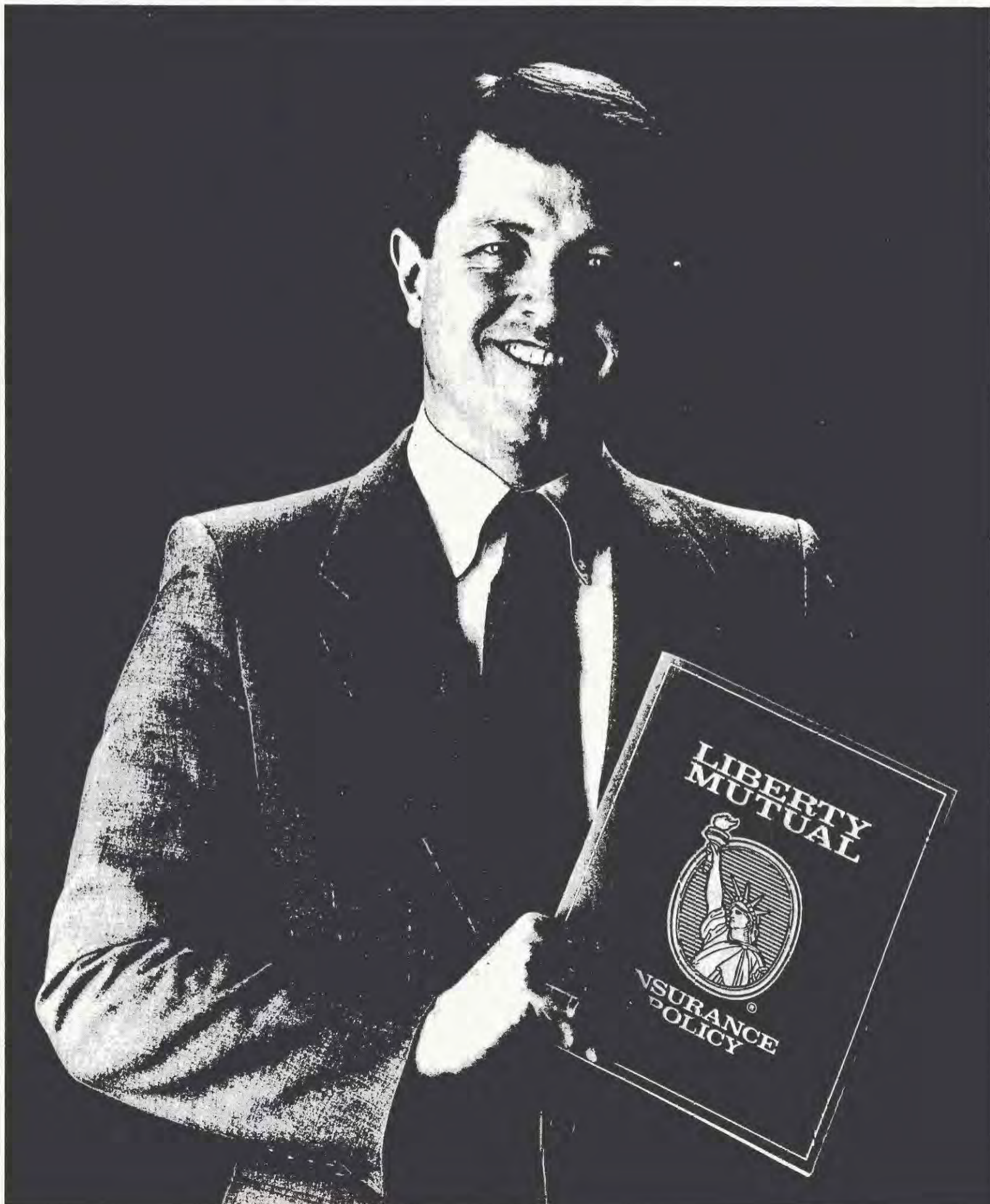
ated.

Product integrity impairment coverage was first written in December 1981 by Lexington Insurance Co. in Easton, an American International Group Inc. unit. Lexington is one of the few remaining markets for the coverage, along with Federal Insurance Co., a subsidiary of Chubb Corp., in Warren, N.J.

The Lexington coverage remains as broad as when it was offered and, perhaps because of this, the company has seen "a dramatic increase" in demand for the coverage, says Assistant Vp Jerry Casper.

"This is not a dead market at all," Mr. Casper said. "Demand tends to move in cycles and tends to follow

*Continued on next page*



Continued from previous page closely with product incidences. Certainly in the last year there has been an increase in activity."

Mr. Casper would not disclose the number of policies Lexington has written, the premium volume written or the number of companies that have expressed interest in the coverage.

Lexington writes four different product integrity policies, according to Mr. Casper:

- The most limited policy covers lost profits and recall expenses, but only if the incidence was triggered by actual tampering that causes or threatens to cause bodily injury.

- The second policy also covers lost profits and recall expenses caused by tampering, but it is also triggered if the U.S. Food and Drug Administration orders a product recall, even if there is no actual tampering.

- The third policy covers only recall expenses, not lost profits, and

is triggered by any "error or inadvertent omission" of the manufacturer. Tampering would not trigger the policy.

- The fourth, and broadest, policy Lexington offers covers lost profits and recall expenses and is triggered either by actual bodily injury, the threat of bodily injury or the perception that the product may cause bodily injury. Product tampering does not have to be evident to trigger the policy, but the manufacturer must not have intended or expected the defect in the product.

Mr. Casper said the policies' limits vary, depending on the policyholder and the insured product, but would not be specific. However, he did say that, on the average, limits are lower than they have been in the past.

And, although he declined to quantify deductibles required by Lexington, he said that the coverage is never written on a first-dol-

lar basis.

In addition, the company requires the policyholder to coinsure between 5% and 25% of the primary coverage in excess of the deductible. The exact percentage of coinsurance that is required is inversely related to the size of the premium—as the premium rises, the amount of coinsurance required is reduced.

Mr. Casper said that Lexington has recently increased rates for the coverages, but would not be specific. "The market is contracting for all lines of business, and obviously this line is affected by it. This line of business is not immune to the forces in the marketplace."

Another major market for the coverage, Federal, introduced its "product protection" policy in October 1982.

According to Anthony L. Gagliardi Jr., assistant vp of Chubb Corp., Federal's parent company, the policy has two clauses: a product recall clause and a product inci-

dent clause.

The product recall clause only covers the costs of withdrawing, transporting, inspecting and destroying an insured product and is triggered by either a voluntary or government-imposed recall.

The product incident clause covers lost profits, business interruption and recall expenses associated with a product impairment. It also covers the expense of rehabilitating a product whose reputation has been damaged after an incident, including advertising and public relations expenses, he says.

However, Mr. Gagliardi said the product incident clause is triggered only by "malicious, intentional incidences," and not occurrences caused by natural forces or the manufacturer (see story, page 30).

Since the product protection policy was first introduced, Federal has severely restricted the number of policies that include recall coverage. "We don't think (recall cover-

age) makes sense from an underwriting standpoint," Mr. Gagliardi said. "There are not a lot of policies written, so there's really no spread of risk."

In addition, Federal has increased rates for the product incident coverage, while lowering the coverage limits and raising the deductible.

Mr. Gagliardi said the deductible charged is dependent on the insured company and the exposure, and could range from \$10,000 to \$25 million.

Although he would not specify the limits offered by Federal, he noted that "capacity is restricted, and I think it's difficult for any policyholder to purchase from insurers limits higher than \$5 million to \$10 million." He noted that Federal has had a hard time reinsuring the coverage, though he would not elaborate further.

Two years ago, Federal offered limits of up to \$100 million (*BI*, April 11, 1983).

Mr. Gagliardi could not pinpoint a premium range for the coverage. "That's even harder to come up with," Mr. Gagliardi said. "There are just not enough insureds purchasing the policies."

Although observers say Lexington and Federal are the major markets for both types of coverage, a few other insurers—including American Home Assurance Co. in New York, another AIG unit, and Liberty Mutual Insurance Co. in Boston—offer limited coverage.

American Home began offering a product integrity impairment policy, which includes product recall coverage, 18 months ago.

"While we will still write the coverage, the capacity is not what it used to be," said Robert Pulka, vp with American Home. "It's probably less than \$5 million." When the coverage was first introduced, limits ranged between \$25 million and \$100 million, he said.

Mr. Pulka said deductibles have stayed constant at about \$50,000 since the coverage was introduced, and rates usually start at 1 cent for every \$100 of the policyholder's sales, plus 10 cents for every \$100 dollars of the policyholder's profits.

In addition, policyholders are given "credits" for good experience and a good recall plan.

Although he couldn't give exact figures, Mr. Pulka said rates are rising and credits are being reduced.

"I wouldn't apply the credits this year that I applied last year," Mr. Pulka said. "I would give credits for the same thing, but I wouldn't give as much credit. For example, if I would give 25% credit for something last year, I would still give them credit this year, but maybe only 20%."

Mr. Pulka said the coverage has generated \$3 million in premiums. American Home has not paid any losses, he said, although it recently received a claim.

"Up to this point, we've done outstanding," he said. "But I see a dwindling demand for it right now. The reasons for that is because people are more concerned with getting their basic coverage together."

Product integrity impairment and recall coverage "is a coverage that's been self-insured for zillions of years, and people are willing to self-insure it in order to concentrate on buying insurance for their basic property/liability coverage," he added.

Liberty Mutual has offered a product recall endorsement to its product liability coverage since the early 1970s. However, the endorsement only applies to finished products, not products used as ingredients or components of other products, according to a spokesman.

The endorsement will cover the cost of shipping, handling, ware-

Continued on next page

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## Product integrity

*Continued from previous page*  
housing or destruction of a damaged product; advertising or public relations efforts necessary to mitigate the incident; and any extra payroll costs associated with the recall, such as overtime pay for permanent employees and salaries of temporary employees.

The spokesman said the endorsement's limit is \$100,000, and it usually requires a \$25,000 deductible. He would not comment on rates.

According to the spokesman, there has been little interest in the endorsement and few claims filed against it.

Other insurers that had written product integrity impairment and recall policies, like First State, have pulled out of the market.

According to Mr. Palmieri, First State offered a product integrity impairment policy with a \$5 mil-

lion annual aggregate limit and required policyholders to coinsure 10% of the risk after meeting deductibles ranging from \$100,000 to \$500,000.

Mr. Palmieri explained that First State only wrote five or six of the policies and never received any claims. Still, the insurer dropped the coverage a year after its introduction. "We did not feel that the laws of large numbers would be at work for us here because not enough people were buying it," he added.

Like First State, The Home Insurance Co. in New York pulled out of the market in January 1985, after a two-year trial run.

"Quite frankly, it never sold very well. And, with the hardening of the market, we just decided to stop offering it," said Charles Abruzzo, assistant vp at The Home. "If we wrote over \$2 million in any one single year, it would be a lot."

The Home's coverage was an en-

dorsement to its product liability policy. Mr. Abruzzo said the endorsement covered recall expenses and "product damage" expenses, but would not elaborate on the definition of product damage.

Insurers' decisions to drop the coverage or to insist on higher rates are taking a toll on buyers.

The director of risk management for a large Midwestern consumer products company, who asked that he not be identified, said two of the insurers that have written the company's product integrity impairment coverage have canceled their portions of the coverage in the past month.

"The one in the excess layers doesn't bother us that much, but the one in the primary layers does because we understand there's not replacement coverage out there."

The consumer products manufacturer has a broad product integrity impairment policy which covers a variety of expenses in-

cluding recall costs; business interruption expenses for 24 months after the incident; expenses associated with the rehabilitation of the impaired product or the introduction of a replacement product; and loss of profits.

The coverage had a \$10 million per-occurrence retention and provided limits of \$100 million per occurrence and aggregate.

The risk manager would not disclose the premium except to say it was between \$200,000 and \$300,000 the first year of the policy and was raised by 33% upon renewal.

"If we can't replace (the canceled layers) we'll continue the program with those layers unfilled," the risk manager said. "We'll just add that to our self-insured retention. The question is, 'What's going to happen at renewal time?' Will there be so little capacity that it won't be worth it to put coverage together to begin with? This is catastrophic coverage; you need higher limits. A

\$10 million limit doesn't do you any good."

Other risk managers have concluded that product integrity impairment coverage isn't worth the cost.

"We studied the coverage available about six months ago," said the manager of the insurance department for another consumer products manufacturer, who also asked that his company not be named.

"We had been self-insured for that exposure and our policy is to look at self-insured risks every once in a while and make a recommendation to management. And, we came to the conclusion that the coverage wasn't worth the cost. We recommended to management that we continue to self-insure both the product tampering and product recall exposures, and that's what they agreed to do."

This risk manager said he got a premium quote of \$250,000 on a policy with a \$25 million limit and a \$10 million per-occurrence deductible. The premium would be \$350,000 if the deductible was lowered to \$5 million.

The policy would have covered a variety of expenses, including recall costs, lost profits and advertising or public relations expenses related to the recall. The coverage would have been triggered by a defect or deficiency in the product that could result in bodily injury or a general public perception that the product could cause bodily injury.

The company's risk manager said, "The low limit wasn't a big factor in our decision—it was the big premium they were quoting relative to rather limited coverage."

Although risk managers are reluctant to discuss how they're handling the product integrity and recall exposures, consultants and brokers agreed that most of their clients are either self-insuring or, more commonly, recognizing it as an uninsured exposure.

This is not to say they're not practicing risk management, however.

"I think, generally, (risk managers) have picked up on quality control and are getting more sophisticated," said M&M's Mr. Gross. "And, that's an important reason why they have decided not to buy the coverage. They feel they can minimize the risk and they can retain the exposure that is there," he added.

Risk management consultants agree. "Companies today have to think of other risk management tools besides insurance," according to Bernard Salwen, senior partner at S.B. Ackerman Associates in New York.

"Insurance is only one risk management tool, and I don't really consider it that. It's not really managing risk as much as it is setting up a payment system. Management of the risk, in this case, involves things like secure packages and increased quality control."

Still, some risk managers think companies that ignore this exposure are making a big mistake.

"They're whistling 'Dixie,'" said the risk manager who had layers of his coverage canceled. "The exposure is great—the exposure is very great, I think."

"It's not a frequency problem, it's a severity problem. If you have a product that's producing millions of dollars in revenue and the image of that product is destroyed, you have one hell of a loss on your hands."

And, he said, although precautions like careful product testing and secure packaging are necessary, they don't eliminate the need for insurance.

"I don't think corporations are buying this product because their quality control is inadequate," he said. "As a matter of fact, if your quality control is not first-rate, you probably can't get this coverage to begin with."



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## Poultry firm may keep insurer despite flap over its coverage

HARRISONBURG, Va.—Rocco Enterprises Inc. says it may continue to buy product integrity impairment insurance from Federal Insurance Co., even though the two companies are mired in litigation over the coverage.

"We will actively be looking for insurance," said John Williams, treasurer of the Harrisonburg-based company. "Whether we stay with the same company or not is undecided, but it is certainly feasible that we will."

Rocco's policy expires Aug. 8. A Federal official would not say if it will renew the coverage.

Federal, a subsidiary of Chubb Corp. in Warren, N.J., sued Rocco in August 1984, seeking a declaratory judgment that the food and

grain processor should not be reimbursed for lost profits that resulted when 605,000 turkeys and 50,000 chickens were infected with the Avian flu and had to be destroyed (BI, Aug. 27, 1984).

In October, Rocco named its broker, Johnson & Higgins of Virginia, as a third-party defendant in the litigation, charging the broker with breach of fiduciary responsibility, misrepresentation and negligence, says Rocco's attorney Gary Spahn of Mays, Valentine, Davenport & Moore in Richmond, Va.

Rocco, with annual sales of about \$200 million, says it lost \$8 million in the incident.

The case is scheduled to go trial in January 1986.

The companies are arguing over whether the Federal policy's "product recall" coverage or "product incident" coverage applies to the situation (see story, page 26).

The recall coverage only pays for the reasonable cost of withdrawing, transporting, inspecting and destroying a damaged product. The much-broader product incident coverage, however, will pay a variety of other expenses, including the cost of re-establishing or replacing a product and advertising or public relations expenses.

The policy, which has a \$10 million aggregate limit, states the recall coverage responds to voluntary or government-imposed recalls triggered by a defect or deficiency that could or does result in bodily injury or property damage. But, the product incident coverage only responds to "intentional and malicious alteration or contamination."

Federal argues in court papers that the recall coverage applies because the situation was not the result of "intentional and malicious alteration or contamination."

A Federal official would not comment specifically on the case. J&H officials declined to comment.

Rocco, however, claims that it understood when it bought the policy that the product incident coverage would apply in such a situation.

Although the language of the product incident coverage does not specifically name lost profits as a covered expense, Rocco argues lost profits should be covered.

Rocco's policy was renewed by Federal last August, shortly after the insurer filed suit.

"We think this is an honest disagreement and does not necessarily have to affect our business relationship," Mr. Williams said.

Mr. Williams said he would not consider forgoing product integrity and recall coverage.

"If we were to lose our Thanksgiving and Christmas sales due to an intentional or unintentional impairment that made our product or created the perception of our product as being unfit to the public, the losses would probably be more than the company could sustain."

Thomas Verghese, credit manager for Victor F. Weaver Inc. in New Holland, Pa., agrees. Weaver, a poultry firm with \$160 million in annual sales, was also hit by Avian flu. Then, it had no product integrity or recall coverage. Mr. Verghese declined to say how much money the company lost.

In October, Weaver bought a \$10 million product integrity policy from Federal for \$38,000. The policy has a \$500,000 deductible and is triggered by "anything that would compromise the wholesomeness of the product," he said. But, it specifies it will not cover Avian flu. ■



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Consequently, risk managers are facing dramatic tightening of coverage as well as heavy premium increases.

Ironically, multiple broker competitive bidding—viewed by some as the best way to get favorable rates—may aggravate the situation. The Request For Proposal procedure, mandated for many public sector insurance buyers and favored by some corporate risk managers as well, is a particular culprit. When multiple brokers go into the market competing for the lowest premium for the coverage, the best price rarely surfaces. In fact, underwriters today often will decline to quote under these circumstances.

Underwriters also have become sensitized to the turnover that routinely follows when the buyer is a "shopper." Stability is still important to insurers.

Today's hardened insurance market calls for a professionalism that replaces the obsolescent multiple-broker bidding system with a two phase concept.

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## Political risk insurers see capacity squeeze in U.S. and London

By MICHAEL BRADFORD

Lack of reinsurance support is significantly reducing political risk insurers' capacity in both the United States and London.

Reinsurance capacity is down 30% to 40% while insurers are paying as much as 40% to 50% more for the reinsurance they are able to secure, sources say. This in turn is reducing the limits of coverage available to corporations with political risk exposures.

At the same time, however, the

demand for the coverage among multinational corporations is continuing to grow, which is prompting new insurers to enter the market and shore up capacity somewhat.

Political risk is a generic term used for several specific types of coverage that protect a company from loss of assets or goods due to political strife.

The most-often requested political risk coverage is contract frustration insurance, which covers losses due to the cancellation or repudiation of contracts that result from political acts of the host country.

Other widely written forms of political risk insurance include coverage against confiscation, expropriation and nationalization of assets by a foreign government and currency inconvertibility covers.

Unfair calling of letters of credit and supply interruption are also covered as political risks. Supply-interruption coverage guarantees



goods by a foreign government that has a purchase agreement with a U.S. company.

Export credit insurance also is available, although it is not commonly regarded as a "pure" form of political risk insurance. The coverage protects against losses from non-payment of goods after they have been received by a foreign buyer. Such losses often stem from political unrest.

Observers in both the United States and London say political risk insurance will be much more widely available within the next few years due to increased interest among underwriters.

But for right now, the overall hardening of the insurance market is making it difficult and costly for insurers to put together reinsurance treaties for political risk coverage.

For example, when Allstate Insurance Co. withdrew from the political risk reinsurance market late last year, it took with it a sizable amount of capacity, observers say.

Although its move did not surprise the market, the fallout from that announcement may have had a ripple effect on the market, says Ed Santos, political risk broker with John F. Sullivan Co. of New York.

"As a big player, Allstate probably took along some of the smaller ones," he said.

As of last week CIGNA Worldwide Inc. still had not completed its Jan. 1 renewal of its political risk treaty and the political risk coverage it is underwriting is being reinsured on a facultative basis, said Joe Tavares, U.S. political risk manager for CIGNA Worldwide in New York.

"Reinsurance is the key stumbling block this year," Mr. Tavares stressed, adding that treaty renewal costs are up as much as 40% this year.

Earlier this year, CIGNA's proposal to write a \$900 million policy to cover foreign loan exposures for Citicorp collapsed from lack of reinsurance support (BI, Feb. 11).

The program fell through because of disagreements between CIGNA and its political risk treaty reinsurers over how the treaty

Continued on page 35



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## Political risk

Continued from page 32  
could be used.

Although Mr. Tavares would not say if that contributed to the insurer's current reinsurance woes, U.S. and London brokers say it did have an impact on CIGNA's renewal and the entire market.

"Now reinsurers are more aware that they shouldn't be getting involved in any banking-type programs. Whenever (reinsurers) see anything coming with a bank's name connected to it, it's a 'no-no,'" said Sullivan's Mr. Santos.

But, the CIGNA/Citicorp problem only added to the overall problem of securing reinsurance in today's market.

The tightening reinsurance market for other classes of business has "spilled over and affected political risk," says Doug Paul, head of American International Group Inc.'s political risk division in New York.

He adds, however, that "it has only slightly affected our ability to serve our clients." AIG was one of the first U.S. insurers to offer political risk insurance, introducing it about seven years ago.

Capacity offered by political risk reinsurers is 30% to 40% less than it was last year, Mr. Santos says, but he too believes most buyers can get coverage.

He says he has found some new reinsurance capacity among syndicates on the New York Insurance Exchange, although he declined to name them.

However, Carol Godfrey, political risk specialist at Swett & Crawford in Dallas, the wholesale brokerage division of Swett & Crawford Group Inc., believes insurers may not be able to meet buyer's demands because of the reinsurance shortage.

"Political risk is facing the same situation as the property/casualty market," she says. "There is probably not enough capacity to go around. I think there are potential insureds who won't be able to get the coverage."

Julian Radcliffe, a political risk specialist and director of Lloyd's of London broker Hogg Robinson Group P.L.C., said capacity for political risk coverage in the London market has dropped significantly since Jan. 1.

He, too, attributes the reduction to large losses in the London reinsurance market—unrelated to political risks—that have affected all treaty renewals. But, he adds that reinsurers are also reacting to political risk losses they have had swallow, citing an estimated \$50 million currency exchange inconvertibility loss in the Sudan and other losses expected from Mexico.

While the loss ratio on political risk coverage in 1984 was only 50% to 60% in 1984, according to underwriters and brokers, those figures can change rapidly, they warn.

Swett & Crawford's Ms. Godfrey pointed out that "we're not talking about small losses. When they hit, they're big."

C. Richard Peterson, senior vp and political risk specialist with Fred S. James & Co. in Philadelphia, agreed that political risk losses "are a catastrophe when they occur. They are very large, but they don't track with loss ratios that you see in property/casualty. One year, they can be very large,

the next, very small."

As a result, reinsurers "are being more careful about the risks being written," said Mr. Radcliffe. They are demanding to know more about the type of business insured, and they are charging more.

"It would not be exaggerating to say the underwriter may have to pay twice as much for reinsurance," Mr. Radcliffe remarked.

David Neckar, political risk underwriter with Merrett Syndicates Ltd. in London, says Merrett has not been as affected by restricted reinsurance capacity as some of the newer underwriters.

Reinsurance capacity for political risk coverage has been reduced 40% to 50% in the last year, he explains. "A number of the lower-ranking syndicates have pulled out" because they could not find reinsurance, he said.

(Merrett was a pioneer in writing political risk coverage in the early

Continued on next page

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### Political risks

*Continued from previous page*  
1970s and is one of the few remaining markets in London.)

"It's difficult to say exactly how much capacity has dropped" because of the tight reinsurance market," said Mr. Radcliffe. "A large piece of business might be hard to place."

For example, he said, a company might have trouble purchasing a political risk policy with limits of \$100 million in a country considered "risky."

"You might be able to get it, but at a high premium rate," he said.

"Capacity depends on the actual risk," said Sullivan's Mr. Santos.

Andrew Palmer, director of London political risk broker Berry Palmer & Lyle Ltd., believes the capacity crisis might be somewhat overblown.

Mr. Palmer said the London market wrote around \$150 million

in political risk premiums last year, and it is expected the figure for 1985 will be similar.

"There is a reduction of capacity for policyholders," said Mr. Palmer. "But if instead of \$100 million in capacity for a risk, there is only \$50 million, for the vast majority of cases, that is enough."

"The impact has not been as great as one might think," he said.

Also, insurers are not demanding significant across-the-board rate increases for political risk coverage, despite the tightening reinsurance market.

"The market doesn't operate that way," explains Mr. Palmer. "You have to look at the country. If there is a great demand for coverage there, then it is reflected in the prices. But there are countries where coverage is placed now at rates lower than two or three years ago."

Mr. Parker's optimism about the availability of coverage appears to be supported by the emergence of political risk insurance markets that will provide additional pockets of capacity.

Trade Credit Underwriters Agency Inc. in New York plans to begin underwriting export credit insurance on behalf of Aetna Life & Casualty Co. in Hartford, Conn.

*Continued on page 38*

### Chubb covers land war risks

Chubb Group is now underwriting land-based civil war risk coverage.

Robert S. Frank Sr., underwriting officer for the group's international division, said Chubb's reinsurance treaties allow it to write land war risk coverage with limits of about \$7 million "per insured, per country."

He said Chubb will also provide some additional capacity to provide slightly higher limits.

He said Chubb has underwritten land-war risks in El Salvador, which it does not reinsure.

The vast majority of the world's insurers follow the Waterbourne Agreement of 1937, which says marine underwriters will not insure war risks on land. The agreement was signed after insurers suffered substantial losses from bombing raids on stationary land-based targets during the Spanish Civil War.

Chubb's move earlier this year into this area makes it the only U.S. insurer to insure land-based war risks.

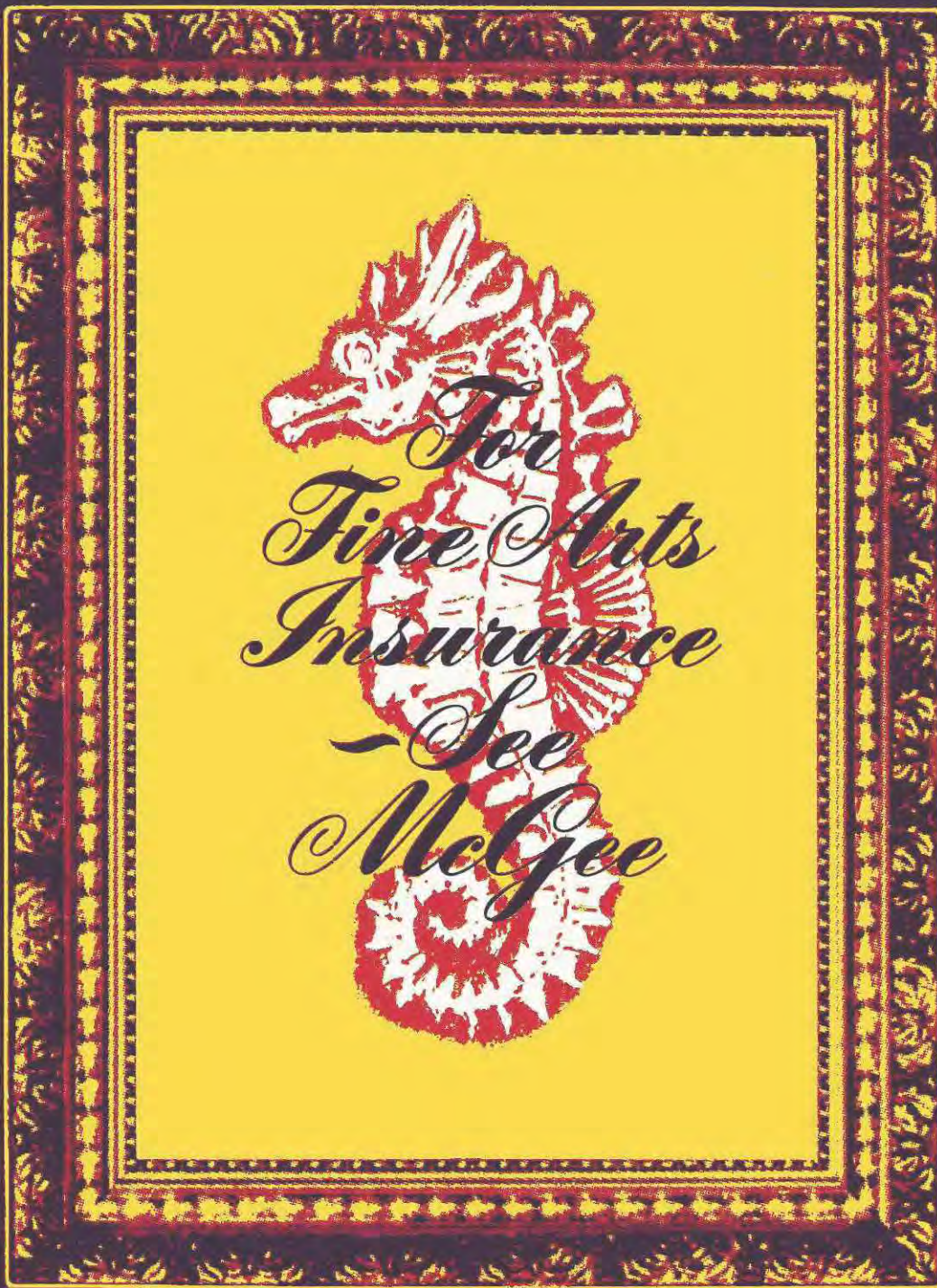
The Chubb insurance covers losses attributed to civil war, insurrection, revolution or rebellion. It also includes losses due to project relocation costs incurred as extra expense as the result of war.

The coverage can be written "just about anywhere," said Mr. Frank.

The new Chubb offering is written as part of a single 19-page policy that combines political risk coverage with other coverages companies purchase overseas.

Mutual Marine Office Ltd., a marine insurance underwriting manager in New York, announced last year that it was willing to commit \$5 million in capacity for land-based war risk coverage (BI, Oct. 15, 1984).

But John Blackman, chairman of the firm, said recently that the coverage "is still one of our projects, but it's on the back burner."



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# Nicaraguan embargo not yet worrying insurers

By MICHAEL BRADFORD

President Reagan's embargo on trade with Nicaragua is not yet causing concern among insurers who write political risk coverages.

Insurers say it is too early to tell if the embargo declared on May 1 will result in claims filed by U.S. companies with operations in the war-torn Central American country.

President Reagan ordered the embargo as a protest against the actions of Nicaragua's Sandinista government. The measure bans all trade with Nicaragua and forbids the country's aircraft and ships from entering the United States.

The Overseas Private Investment Corp. in Washington is the major insurer of political risks of U.S. companies that do business in Nicaragua. A spokesman for the agency said it has a total exposure of \$8.2 million for three separate types of risks covered.

OPIC has written \$3.2 million in coverage for expropriation risks, \$2.9 million for currency inconvertibility risks and \$2.1 million for war risks in Nicaragua. The coverage was purchased by four U.S.-based firms: American Standard Inc. in New York, Citicorp in New York, General Mills in Minneapolis and Pennwalt Corp. in Philadelphia.

An investor named Adolph Weil also is listed by OPIC as a warehouse

contractor with coverage in Nicaragua.

The OPIC spokesman said there has been no notification of claims from any of the U.S. firms or Mr. Weil. "It's much too recent to see if there is going to be any effect on business."

The Export-Import Bank, another federal agency that writes export credit insurance for U.S. companies through the Federal Credit Insurance Assn., has not provided coverage involving Nicaragua since 1983, a spokesman noted.

In the private market, CIGNA Worldwide Inc. reported that it has no exposure in Nicaragua. Joe Tavares, manager of the U.S. area for CIGNA Worldwide, said the insurer has "stayed away from Nicaragua." That decision was based on the insurer's strategy of conservative underwriting, he said.

Nicaragua is considered a "high risk" country. Although coverages written by OPIC are generally in the form of 20-year contracts, insurers in the private market don't offer such lengthy terms.

Private market insurers keep a "watch list" of countries that are considered unsafe for political risk exposures. The list is updated continuously as conditions change across the world.

Besides Nicaragua, areas that are on current watch lists include the Philippines, Argentina, Brazil, Nigeria, Iran, Iraq and Libya.



## Political risk

Continued from page 36  
as soon as reinsurance treaties are in place.

Bob Svensk, TCU president and former president of AIG's political risk division, said he expects to be able to provide coverage of up to \$50 million per risk.

Clients, he said, will be "the major exporters of the world, both U.S. and foreign."

UIC Ltd., a New York-based wholesale brokerage and underwriting manager, is also helping shore up the political risk market.

President David D. Avasthi said UIC will begin writing political risk coverages at the end of this month for North River Insurance Co. in Morristown, N.J., a unit of Crum & Forster Inc., also based in Morristown.

Mr. Avasthi did not reveal how much capacity North River would provide, but did say the main coverage written will be for contract frustration.

Mr. Avasthi says that other U.S. insurers would like to enter the political risk arena but they "can't gather reinsurance because of certain gaffes by some underwriters in the past."

He also said it could be awhile before any new political risk coverages are introduced into the marketplace because of the current cautious attitude of reinsurers.

New capacity in the London market is coming from two new political risk underwriters: PanFinancial Insurance Co. Ltd. and Trade Indemnity P.L.C.

PanFinancial is a joint venture of Continental Corp. of New York, Skandia International Insurance Corp. in Sweden and Yasuda Fire & Marine Insurance Co. Ltd. of Japan.

PanFinancial, capitalized at \$9 million pounds (\$11.25 million) in January, will begin writing export credit and contract frustration coverages in mid-June.

Alastair Malcolm and Martin Roberts, both formerly with the credit insurance division of the British National Group, will direct the new insurer.

While Mr. Malcolm said "it is difficult to be precise" concerning PanFinancial's capacity for political risks, another London source said he expects the new underwriter to provide limits of up to around 3 million pounds (\$3.8 million) per policyholder.

Mr. Malcolm also expects other underwriters to enter the political risk market. "There will undoubtedly be more," he said "In putting together (PanFinancial), we saw a lot of interest from others."

Trade Indemnity, an established domestic credit insurer, has recently begun offering political risk insurance to clients that have most of their exposures in Europe or North America, but also need some coverage for foreign operations.

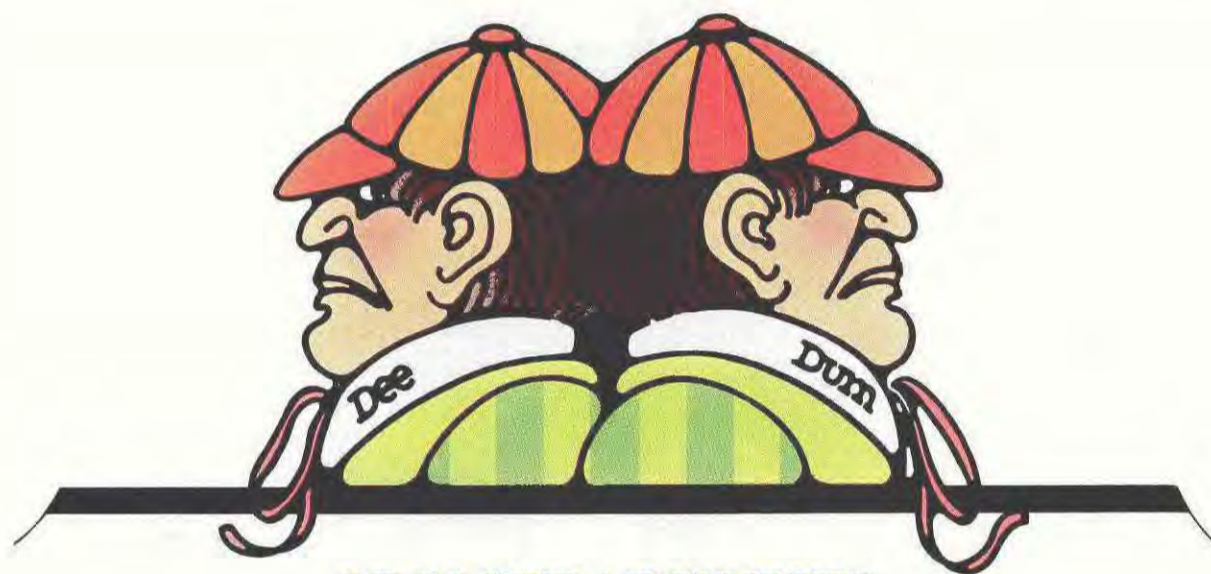
Dennis L. Howson, general manager and underwriter for Trade Indemnity, explained that the underwriter provides export credit and other political risk coverages as a "bolt-on" or addition to their clients' domestic credit policies.

Mr. Howson said the insured decides which political risk coverages it wants added to the policy. Trade Indemnity currently has no plans to offer political risk insurance as a separate cover, he said.

Although he would not release any specific capacity figures, Mr. Howson said, "I believe we have quite enough capacity to cover any request made to us. Our reinsurance was well-sorted out before we went live with this on the first of May."

Meanwhile, banks may be using the current shortage of capacity in the political risk market to back into insurance underwriting, says Victor Hertz, manager of political

Continued on page 40



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## Political risk

Continued from page 38  
risk services at Frost & Sullivan Inc., a New York consulting firm.  
"A number of major banks have used that as an excuse to begin talking about forming underwriting facilities that would help bridge the market," said Mr. Hertz.

"A lot of brokers feel that it is a ploy for (banks) to come into underwriting under a brokerage cover."

BankAmerica Corp. and Citicorp are already establishing political risk brokerage operations (BI, April 1).

BankAmerica has formed units in London and the United States to

provide political risk brokerage services to its bank clients.

BankAmerica Insurance Services Ltd. in London, although it isn't actually placing coverage yet, is fielding requests from bank clients and expects to begin providing coverage by midsummer.

BISL has also opened a New York division that will place coverages for U.S. bank clients as well as third-party clients.

Susan Mashkes has been hired as managing director of the political risk division of BankAmerica's New York unit. She was formerly assistant vp of the political risk division at Johnson & Higgins in New York.

Ms. Mashkes said banks are entering the brokerage business to compete with financial supermarkets like Sears Roebuck & Co., Merrill Lynch Pierce Fenner & Smith Inc. and American Express Co.

Insurance is a natural expansion area for banks, she noted, and "political risk insurance is a good place to start because it is easy for the banks to understand."

The BankAmerica units will offer "the whole gamut of political risk and export credit coverages," she said.

However, the bank has no plans to begin underwriting political risk

coverages, Ms. Mashkes noted, even though it is empowered to do so for third-party clients by the 1982 Export Trading Company Act.

Citicorp also plans to open a U.S. brokerage unit to provide political risk coverages. The New York-based bank holding company announced earlier this year that it had hired Peter Clark, a political risk underwriter with the Overseas Private Investment Corp., to head the new unit.

Citicorp already owns Lloyd's of London broker Grindlay Brandts Insurance Brokers Ltd.

Although more insurers apparently will be entering the political risk market, public markets insure the bulk of political risks in both the United States and London.

A spokesman for the Export Credit & Guarantee Department in London said it covers about 90% of all insured exports there. The coverages issued by the government agency are the same as those underwritten in the private market.

The department insures policyholders' commercial and political risks under one policy, the spokesman explained. He said business valued at 17.8 billion pounds (\$22.6 billion) was insured by the agency during the fiscal year ending in March 1984 and 2.1 billion pounds (\$2.7 billion) in claims have been

paid over the last three years.

Of those claims, 1.5 billion pounds (\$1.9 billion) was for political risk losses, said the spokesman.

The U.S. counterpart to the ECGD is the Overseas Private Investment Corp., a federal agency in Washington. The agency provides coverage for currency inconvertibility, expropriation and war risks. It is authorized to write a total of \$7.5 billion in coverage for each risk.

In fiscal 1984, OPIC reported a net income of \$97.2 million, up from \$82.7 million during fiscal 1983.

The agency paid out \$25 million on 21 currency inconvertibility claims in 1984, including one for \$11.3 million in the Dominican Republic to Gulf & Western Industries Inc. of New York.

Another U.S. government agency, the Export-Import Bank, provides export credit insurance through the Federal Credit Insurance Assn., its underwriting agent in New York.

The agency covers credit risks for a variety of clients, a spokesman noted, including large U.S. multinationals and smaller businesses.

Over the past three years, the agency has paid more than \$600 million in claims, he said.

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The instructors are Larry D. Gaunt and William R. Feldhaus,

both professors at Georgia State University.

The registration fee for the course is \$445 for RIMS members and \$545 for others.

For more information or to register, contact Fran Jordan, Administrator-Continuing Education Program, RIMS, 205 E. 42nd St., New York, N.Y. 10017.



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# FINANCIAL GUARANTEES

Recent rash of insolvencies shows tighter regulation of insurers needed

By Bruce Bunner

LAST YEAR I WAS asked by an insurance magazine to write an article about current insurance issues of interest in California. In that article, I predicted that financial guarantee insurance would become a scandal in about two years.

My prediction proved right, but my timing proved wrong. Shortly after publication of the article, Glacier General Assurance Co., Pacific American Insurance Co. and Cal-Farm Insurance Co. became financially distressed as a direct result of their mismanagement of this insurance product (BI, March 11).

(Glacier General and Pacific American were involved in mortgage losses at Bank of America; Cal-Farm was taken over by the California Insurance Department March 29 after it was determined that about \$60 million in financial guarantee bonds sold by Cal-Farm were in default.)

These insolvencies clearly demonstrate that financial guarantee insurance is a very specialized coverage that requires a financial expertise and knowledge not

usually possessed by the traditional underwriter and risk manager.

Regulators will have a difficult time regulating the various forms of financial guarantee insurance. The variety of forms appears endless, from municipal bond insurance to corporate and limited partnership bonds. Since these coverages are currently in the marketplace, it would be difficult to reform that which already has developed.

Further, you cannot legislate such attributes as conservatism of management, prudence of management and financial expertise of management, which this product demands to avoid insurer insolvency.

The product does not lend itself to typical actuarial concepts and rating methodology. For example, the private guaranty mechanisms for the state-insured thrifts of California, Ohio and Maryland were working wonderfully until this year. They are now either bankrupted or severely strained to meet their obligations. Even the current adequacy of the resources of

*Continued on page 48*

Cooperation, caution are the keys to regulating innovative coverage

By Michael Djordjevic

ONE OF THE MOST dynamic and creative segments of the free enterprise system can be found in our financial institutions.

Within the broad markets these institutions serve, a new and specialized type of business has emerged recently to meet the needs for rapidly evolving innovations: financial insurance or guarantees.

These guarantees protect against the loss of investment or credit due to failure to pay or to perform according to contractual obligations. The demand for this form of insurance has shown remarkable growth in recent years and is a particularly notable development.

When free-market forces bring forth a profitable business, that business often attracts the attention of market participants who are more interested in "the quick buck" than in serving legitimate business needs.

In an environment where freedom of action exists and where some people only follow their self-interests, unrestrained

and misguided abuses of the system are not really surprising.

Paradoxically, it is this very condition that engenders both the strength and the weakness of capitalism!

It has always been the perennial question in the Western world—and the United States in particular—how to allow for maximum freedom that fosters creativity and wealth without ruinous competition, exploitation of the masses and abuse of the very freedom that underpins our society.

These somewhat philosophical but fundamental issues need restating before a meaningful and well-balanced discussion about regulation of financial insurance can begin.

Whenever a regulation is promulgated, a constraint on creativity and on freedom is imposed. This is a general proposition.

But, it is also universally true and demonstrated that controls and discipline must be imposed from the outside upon unrestrained or mindless freedom if internal self-control fails and forces from within threaten, for selfish reasons, to

*Continued on next page*

# Cooperation key to financial guarantee regulation

Continued from previous page  
diminish that very freedom.

Evidence is ample and indisputable in human affairs that growth and creativity need room and space to expand and mature.

A child smothered by overly strict parents most likely will not grow to be a self-reliant, balanced and creative individual. Even a young growing tree that is tied too tightly to the supporting stick may die.

Thus, as a general proposition, we may paraphrase Thomas Jefferson: "The regulation that regulates the least is the best."

But, as Jefferson himself—and many other enlightened thinkers before and after him—knew, a framework of rules and guidelines is needed to secure the maximum freedom for all in a society of conflicting self-interests and immature or unenlightened men and women.

Financial insurance is a relatively new endeavor in its current shape and direction.

It is now a market-driven business that has slowly responded to:

- The breakdown of regulations of financial institutions.
- The public bewilderment with almost endless forms of intangible wealth.
- Consumers' own growing concern for preservation of intangible assets from various forms of risks inherent in a multilayered and complex investment and financial environment.

Indeed, in the early 1970s, when the first municipal bond policies were written, the business was driven primarily by the need of bond issuers to reduce their cost of borrowing. Buying insurance from a AAA-rated insurance company was an easy means of attaining this objective.

It was not too long before creative players within financial markets began to recognize the unique and complementary nature of financial guarantees to the emerging and vast number of new financial/investment instruments.

In addition, business failures and near collapses—like Penn Central, Lockheed, Chrysler and Washington Power Supply System—produced concerns on the part of the investors.

The American consumer is the most insurance-conscious in the world. Therefore, it is only natural for him or her to seek security and comfort through insurance on financial instruments in an increasingly complex and uncertain investment climate.

The barriers of regulation were broken down by natural forces of competition in the financial arena in the 1970s. Three major industries have begun to converge: banking, insurance and investment banking.

This dynamic process, which involves some of the most talented, aggressive and imaginative people, has revitalized competition and has benefited the consumer.

Unfortunately, it also has produced

some questionable activities and undesirable outcomes, like the Bank of America/Glacier General Assurance Co. fiasco (BI, March 11). There probably will be more negative news of this kind.

Whenever a new frontier is opened or a "gold rush" begins, it is inevitable that "bad goes alongside the good." This is indeed the price of freedom, but also the source and strength of progress and the vitality of democracy and capitalism.

In the current set-up, it is obvious that:

- The market for financial insurance is expanding.
- New and, at times, far-reaching practices of doing business are expanding.
- Competition and self-serving interests may threaten the healthy and promising growth of this newly emerging business.

Currently, banking, insurance and investment banking are competing more directly and more openly than ever

**'There are many issues and many complex... questions besetting both the business and the regulators. Among those, one certainly stands out: the need for a coherent and holistic view and understanding of the changes that already have taken place in the financial services industry.'**

before in modern history.

At the same time, these three great workhorses of capitalism are *converging*, supplementing each other and providing new forms of products and services.

Immediately, and ultimately, the consumer and society benefit from these trends.

Financial insurance is a natural outgrowth of insurance and risk management. Many risks pervade an advanced free-market economy. And, by tradition, subjective evaluations of these risks and their redistribution through the economy have been prime functions of the banking and investment services industries.

Through financial insurance, the insurance industry also can become a key participant in this economically most-significant process.

Financial insurance has become the bridge that has firmly connected the insurance industry to its sister industries, banking and investment banking. Its future in an industry that has been plagued by adverse cycles and results is promising.

The key issue is one of controlled growth, disciplined underwriting and adequate and realistic pricing.

Logic would suggest that participants in financial insurance should, for the good of all, police themselves first and foremost. In addition, they should support sound and intelligent rules and regulations, and vigorously oppose those that are not.

In the next year or two, we will witness continuing and increasing competition as well as convergence in the financial arena. We shall also hear and see many attempts to regulate these forces that are yet to be properly analyzed, comprehended and dealt with. What we have today is a hodgepodge of rules and regulations of a bygone era and many regulators who, like some generals, fight past wars.

The financial services market in

general, and financial insurance in particular, will continue to expand and move into still-uncharted areas. This process will produce some undesirable—but visible—practices.

There will be casualties, among both consumers and business.

Regulatory bodies will respond, belatedly and in a fragmented fashion, as they usually do.

The end result may be an "over-kill" and counterproductive. This unproductive direction can be avoided through sincere cooperation and determination on the part of the industries involved and their respective regulatory agencies. This can be done; it should be done!

There are many issues and many complex philosophical and practical questions besetting both the business and the regulators.

Among those, one certainly stands out foremost: the need for a coherent and

holistic view and understanding of the changes that already have taken place in the financial services industry, in particular banking, insurance and investment banking.

What alarms me most is the real possibility of piecemeal, fragmented regulations dealing only with one aspect or one industry. Imagine four different composers writing separately a single piece of music for a quartet! What music that would be!

Yet, we may be witnessing the same process emerging in the arena of regulation of financial services and financial guarantees.

It would be a mistake to conclude that only legal and statutory rules govern and will govern financial markets and financial insurance. The market itself always produces its own internal rules.

A case in point is the role and "regulations" that are already in existence: the rating industries, in particular Standard & Poor's.

Already, for years, Standard & Poor's has "regulated" financial insurance in a manner more effective and pervasive than any single state regulator would or can do.

In financial guarantees, the guarantor must have a high (AAA or AA) standing and perception in the marketplace.

Without such a rating, business is difficult to conduct.

Rating agencies have set up standards, which are constantly being reviewed and improved, to measure and establish strength and future vitality of the guarantor, be it a bank or an insurance company.

Recently, Standard & Poor's has made a great effort and great strides to quantify capital requirements for various types of municipal insurance risks.

Moody's has just rated several issuers of municipal bond guarantees and seems to be waking up to its own responsibility.

And, the Fitch rating agency also is poised to make its contribution to the

process.

Moreover, the users of financial insurance, particularly investment bankers, are becoming more selective and careful. Events like the recent Bank of America/Glacier General fiasco are bad, but they also contribute to market discipline.

And, major insurers are becoming increasingly aware of and sensitive to the complex requirements of financial insurance. So, all together, we can observe meaningful attempts and actions for self-policing in the industry.

The newly emerging and expanding financial services business needs new rules. But, those rules must not be created and promulgated in a vacuum.

Trying to regulate financial insurance without understanding its ties to banking and investments makes little or no sense.

There should be no rush to regulate because of immediate concerns or political pressures. What we have is a good, sound business that already has benefited society and the economy and established an enviable risk-free and profitable record. We should not "throw the baby out with the bath water."

The proper way to approach the problem of balanced and productive regulations is to:

- Recognize the nature of and forces unleashed in the arena of financial services.
- Approach the issue from a panoramic viewpoint, not a keyhole one.
- Secure cooperation among the regulators and the three industries; get together, enlist the best talent, create a conceptual model.

- Be patient and flexible in working out regulations step-by-step within the broad conceptual framework.

In more specific terms, forthcoming regulations should address and deal with at least these essential issues and questions:

- Capital. There should be stiff entry requirements and high thresholds in terms of capital needed to get involved in financial insurance. Also, all along, the capital capacity to stay in the business has to be demonstrated and provided for by financial guarantors.

- Reserving. There should be realistic and appropriate reserving standards that correctly reflect and recognize unique characteristics of the business, like collateral, reinsurance and other protections.

- Contingency reserve. There should be a requirement for additional protection to policyholders against economic distress.

- Pricing. There should be regulatory recognition of flexible and profit-driven pricing mechanisms.

The future holds both promise and a challenge for financial insurance. It can—and should—be a profitable business for the industry and should provide good service and a desired product for the risk-adverse consumer.

The challenge is the same one that has haunted man throughout history: how to deal with freedom.

If it is abused, outside forces always interfere and try to bring order, which often degenerates into tyranny. But, if it is responsibly promoted, nurtured and handled, all involved benefit and grow.

As a perceptive cartoonist pointed out, "We have seen the enemy, and it is us."



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# YOU'RE LOOKING AT WHAT MAY BE AMERICA'S GREATEST RESOURCE.

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It gets dumped, burned, or even goes uncollected. And it's marred our water, land, and air.

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# Insolvencies show need for tighter regulation

Continued from page 45

the Federal Savings & Loan Insurance Corp. are questionable.

In other words, this coverage cannot be underwritten on a year-to-year basis. But, adequate asset funds must be accumulated to respond to the effects of unforeseen adverse economic conditions or events when they occur.

The current statutory financial accounting model is inherently weak, in that it does not provide for catastrophe reserving concepts. Even the statutory contingency reserves currently applicable to mortgage guarantee insurance business do not bear any reasonable relationship to an insurer's actual annual aggregate exposure for this risk or the actuarially determined permissible loss.

Some would suggest that insurers should not be permitted to guarantee financial arrangements. For the legislator and regulator, this would be the risk-free solution.

But, in spite of the abuses, which never can be eliminated, financial guarantee insurance is appropriate for the insurance industry.

Although the property and casualty industry engages in an abnormal amount of self-flagellation as to its financial difficulties, the industry is nevertheless fiscally strong and financially stable. Aggregate property and casualty surplus is approximately 25% to admitted assets, whereas for the thrift institutions, the surplus ratio is approximately 5%. Moreover, the property and casualty industry does not have the liquidity, asset/liability mismatch, and demand deposit problems of the thrifts.

The regulatory issues to consider that will require the assistance of the industry will include such matters as line of coverage, required capitalization, limitations on exposure, reserve calculations and reinsurance considerations.

Someone once said that financial guarantee insurance is like pornography: You cannot define it, but you know it when you see it. The California Insurance Department considers financial guarantee insurance as surety insurance, regardless of its contractual structure. This interpretation presents

certain technical problems, because certain limitations are imposed on surety coverages in the California Insurance Code.

For example, any single insured surety risk cannot exceed 10% of the insurer's capital and surplus, and guarantees under surety insurance cannot be secured by liens of mortgages. Further, the Insurance Code is silent as to the offset of any collateral values in the calculation of the single-risk definition.

The department currently is attempting, through proposed legislation, to redefine and modify these surety limitations. These code sections, when originally developed, never contemplated the various kinds of guarantee insurance arrangements we now have in the marketplace.

For example, the many mortgage-backed municipal bonds insured in recent years are in technical violation of the California Insurance Code under a narrow and literal interpretation of the current surety code provisions.

Some within the industry would prefer to impose minimum statutory capital and surplus to write financial guarantee insurance. Some would further argue that this coverage should be monoline, similar to mortgage guarantee insurance.

I do not agree with either of these arguments. Imposition of minimum capital and surplus requirements is generally self-serving and anti-competitive. Monoline legal separation of classes of business is archaic and a step backward to a 1930s mentality.

In this day of financial sophistication, we should be trending toward a statutory accounting model that facilitates the identification of assets, liabilities and surplus by rational exposure classifications.

The regulatory emphasis should focus on the allowable amount of aggregate exposure and the allowable amount of risk as to any one issuer of a financial instrument. These allowable amounts should be a function (or multiple) of the insurer's total capital and surplus.

Most regulators will advocate low aggregate exposure levels, due to the uncertainties inherent in the various forms of financial guarantee insurance.

Regulators will be particularly sensitive to this coverage when written by multiple-line companies.

Two of the recent insolvencies mentioned heretofore had a reasonably stable book of insurance in force that was destroyed in a matter of months by their unpropitious venture into the financial guarantee insurance market.

I strongly believe that financial guarantee insurance should not be accorded equal priority with indemnification insurance contracts in the event of an insolvency. It is noteworthy that letters of credit and similar credit enhancement instruments of the thrifts do not share equal priority with the depositors.

The insurance industry is opposed to according a lesser priority for this coverage. Members of the insurance industry perceive that their products will have limited marketing appeal to prospective purchasers.

This is nonsense, as most purchasers of financial guarantee insurance are financially sophisticated, and they look to the insurer's viability, financial strength and creditworthiness rather than placing their reliance on the adequacy of insolvency, or guaranty, funds.

Currently, California does not allow any deduction from loss reserves for the time value of money or anticipated salvage.

We currently are introducing legislation to facilitate such deductions from loss reserves, subject to certain limitations.

The time value of money can be considered for unpaid losses on defaulted issues as to insured principal and interest only to the extent that invested assets have been identified in the insurer's accounts and where the insurer can demonstrate clearly that the invested assets will mature in reasonable relationship to the maturity of the defaulted loss obligation.

As for salvage, such deductions will be allowed only to the extent that the collateral held by the insurer under the defaulted issue would otherwise qualify as an admitted invested asset.

For financial guarantee insurance, reinsurance presents its usual problem to the regulator when the non-admitted and

the alien reinsurance markets are used by the primary insurer.

For regulatory reasons, I would prefer to limit the amount of aggregate exposure that could be placed in these non-admitted markets.

But it appears the capacity of the alien market is required to adequately obtain spread of risk and serve the marketplace for the larger underwritings of tax-exempt and taxable bond and note obligations.

In relation to the exposure, reinsurance credits on financial statements will not be significant, due to the relatively small amount of the premium applicable to financial guarantee coverages. Thus, letters of credit, funds held and other security measures do not provide the regulator with the security, comfort and reliance usually present in other reinsurance transactions.

Standby letters of credit for higher values would be desirable, but the cost would be too prohibitive to accomplish the basic insurance transactions.

To avoid the typical abuses of the offshore reinsurance market, it appears that in the interest of solvency safeguards, the most practical approach to using the non-admitted reinsurance market is to establish high threshold amounts as to the capital and surplus required of non-admitted reinsurers to serve this class of business.

In conclusion, the property and casualty industry can and should serve the needs of this developing market of financial guarantee insurance.

Regulators need to move quickly to gain a better understanding of this class of insurance. Industry should cooperate with and assist regulators to improve the accountability and disclosure standards for this class of business and to develop the prudent financial standards to be used to effectively monitor industry solvency.

Bruce Bunner is the commissioner of the California Insurance Department.



## Book on computers is too technical for most laymen

### Understanding Computer Science

By Roger S. Walker

Texas Instruments

P.O. Box 225012, MS-54, Dallas, Texas 75265

\$14.95 softcover, 274 pages

By Chris Conrad

COMPUTERS ARE all around us. They write our paychecks, keep tab of our bank accounts, remind us when we don't pay a bill, print status reports of business activity, etc.

In "Understanding Computer Science," Roger S. Walker tries to tell us how this is all done—in other words, how computer hardware is designed, how computers are programmed, how data is structured in memory, how an operating system controls a computer

Chris Conrad is manager of treasury operations for UCCEL Corp. in Dallas, a provider of data processing services.

### books & ideas

and more.

Admittedly, this is a large task. The author attempts to bring the reader a basic understanding of the use of computers.

The term "science" in the title of this book, however, defies any discussion to remain purely basic. The book is very textbook-like and highly technical—but then, so is the subject.

For the reader who wants an in-depth, technical explanation of the electronics of computers, this book appears to be good. There are many diagrams and illustrations in each chapter to aid the reader in understanding the technical concepts presented. There also is a very helpful quiz at the end of each chapter to confirm that the reader has a thorough understanding of that chapter's content before proceeding to the next topic.

The topics covered in the book's 10 chapters include the 30-year history of the computer age, including the

major developments and their impact on computer capabilities; computer hardware, how it functions and how it works with software; computer programming and execution, and specific computer languages, including BASIC, Pascal, FORTRAN, COBOL and PL/I; and how an operating system functions for monitoring and controlling the computer system and job execution.

Also covered are, data structures, including bits and bytes, fields, records and files, and a detailed discussion of linked lists; language translators, loaders, assemblers and compilers and their applications for conversion from human instructions to machine instructions; and a discussion of systems analysis and some practical applications of computer science.

For the reader who is interested in a text on electronic technology, this book offers a complete and thorough adventure in computer science.

However, for the majority of readers, the book contains more detail at too technical a level to satisfy either curiosity or a business need for a basic understanding of the computer revolution.

# Loss prevention, reduction methods assessed

By The Insurance Institute of America

The following question and answer are drawn from the curriculum for the Associate in Risk Management (A.R.M.) designation awarded by the Insurance Institute of America. They represent the type of question asked, and possible answers to, the three examinations for the Associate in Risk Management designation.

Efforts to minimize any type of accidental loss attack either loss frequency or loss severity. Some measures, like driving vehicles more slowly, tend to reduce both frequency and severity. Loss control measures that reduce frequency usually are called loss prevention; those that control loss severity typically are called loss reduction.

An important reason for distinguishing between loss prevention and loss reduction is that all loss prevention measures must be taken before a loss occurs, while loss reduction measures may be effective either before or after a loss. As the following question illustrates, nowhere are pre-loss and post-loss actions more important to loss reduction than in controlling the severity of losses that may strike an organization's computer facilities.

**Q:** A regional credit card and billing center for a large petroleum company is housed in a concrete and steel office building near a river. What actions should the firm's risk management professional recommend be taken both before and after a loss to minimize the severity of losses to the computer facilities from:

- Vandals' attack?
- Fire damage?
- Flood damage?

**A:** • Before vandals attack, it would be appropriate to establish a security system to monitor entry to the computer area, erect barriers to vandals' entry to the

## A.R.M. exercises

building, minimize the amount of property exposed to such an attack and make plans for maintaining computer operations (in current facilities or elsewhere) in spite of any attack.

Immediately after an act of vandalism, the computer personnel should first safeguard from further damage both the computer equipment and the software being used at the time.

Computer operations themselves may be maintained by calling upon duplicate records stored at another location.

Second, salvage possibilities—for both the hardware and the software—should be explored.

Third, analysis of this incident may reveal ways in which future attacks could be thwarted.

Fourth, if the attack gained public attention, it might be appropriate to inform the public that the damage to the computer center has not impaired the company's ability to serve them or to handle payments of their accounts.

• In principle, many of the preloss steps taken to minimize vandalism losses also would be effective, appropriately modified, for minimizing fire losses. For example, security personnel should be alert to and trained in extinguishing any fires that occur in the computer area.

Reducing property exposed to loss would involve primarily eliminating unnecessary combustibles from the computer area.

A fire detection/suppression system specially selected to be appropriate for computer operations should be installed.

The relevant physical barriers to loss would be the use of fire-resistant walls, floors and ceilings to protect the computer facility from external fires and, if feasible, firewalls or other barriers within the computer area to check the spread of a fire originating there.

Plans for responding to a fire should include assignments made to particular employees about specific emergency actions that they should take during any fire.

After a fire has occurred, post-loss severity controls again quite closely parallel those for vandalism.

Even greater care should be taken, however, in salvaging computer hardware or software partially damaged by heat or smoke during a fire.

Preventing a recurrence may be more difficult for fire than for vandalism, however, because most fires that damage computers originate elsewhere, often beyond the control of the computer facility's management.

• Before any flood strikes, the computer facilities should be placed on one of the upper floors of the building or within an area that can be sealed with water-tight protection.

Plans also can be made for moving vital equipment or software to higher locations or for shifting the billing activity of this regional center to some other center.

In addition, some flood protection also may be gained by building dikes around the perimeter of the entire building.

After a flood, as after a vandals' attack or fire, the pre-loss plans must be translated into post-loss actions. Post-flood salvage probably will be much like that following a fire.

Informing the public that the flood has not shut down billing operations is likely to remain an essential loss control.

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 A.R.M. program, write Dr. G.L. Head, Vp, Insurance Institute of America, P.O. Box 314, Malvern, Pa. 19355.

# Cost of replacing carpeting excluded under CGL

Claims for the cost of replacing allegedly defective carpeting fell within a "business risk" exclusion of a comprehensive general liability insurance policy, despite an exception to the exclusion for liability assumed by the insured for matters of warranty of fitness or quality, the Supreme Court of Hawaii ruled.

Sturda Inc., a distributor of carpeting manufactured by E.T. Barwick Industries, furnished carpeting for a condominium-hotel project. Shortly after delivery and installation, the carpet faded excessively and unevenly.

Sturda denied the product was defective and attributed the cause to atmospheric conditions prevailing in the area.

The project owner sued Sturda, the manufacturer and the carpet installer, seeking the cost of replacement for the allegedly defective product and for consequential damages.

Barwick was insured under a comprehensive general liability policy issued by Fireman's Fund Insurance Cos. that contained a vendor's endorsement extending coverage to Sturda. However,

These abstracts were prepared by Cases Unlimited Inc. A copy of an entire decision may be obtained by sending a check for \$5 made out to Cases Unlimited to Business Insurance, 740 N. Rush St., Chicago, Ill. 60611. List the number for each opinion.

## legal briefs

Fireman's Fund refused to defend the suit, claiming that the policy excluded coverage for loss of use of property that had not been physically injured or destroyed. The trial court agreed with Fireman's Fund.

On appeal, the court concluded that the policy exclusions did restrict coverage for the contractual liability of the insured as a source of goods to make good on products that were defective because they were lacking in some capacity. The court emphasized that the risks insured under a comprehensive general liability policy are "injury to people and damages to property caused by a faulty product or workmanship." *Sturda Inc. vs. Fireman's Fund Insurance Cos.*, Supreme Court of Hawaii, June 15, 1984 (BI/01/My.—\$5)

### Heart disease job-related

An employee's heart disease caused by job-related stress constituted an accidental injury that arose out of and in the course of his employment, a Georgia appellate court ruled.

From 1979 to July 1981, Mr. Fender, an employee of Zippy Mart Inc., was employed as a supervisor of nine stores, which required him to work 10 to 12 hours per day, six days per week. Mr. Fender developed coronary artery disease and required quintuple coronary bypass surgery. He filed for workers

compensation benefits claiming that his coronary artery disease was the result of job stress. Benefits were allowed, but the employer appealed.

The appellate court noted that expert medical testimony confirmed that stress could contribute over a period of time to development of arteriosclerosis.

"Neither law nor medicine are exact sciences," the court observed, "and we have not reached that degree of certainty where a medical expert can state a definite and certain diagnosis that the claimant's heart disease did not arise out of and in the course of his employment."

The court was satisfied that there was direct evidence of the required causal connection between the stress and the resulting heart disease requiring surgery, thus supporting an award of benefits. *Zippy Marts vs. Fender*, Court of Appeals of Georgia, March 12, 1984, rehearing denied April 2, 1984, certiorari denied April 19, 1984 (BI/02/My.—\$5)

### Psychosomatic pain ruling

A claimant's psychosomatic, hyponchondriacal pain, resulting from a physical injury, could probably be considered in determining disability to earn under the workers compensation law, an Alabama appellate court ruled.

William Armstrong was employed as a general laborer by a construction

company. He injured his back on the job, and he received medical treatment for the injury.

Because of continuing pain, however, Mr. Armstrong was referred to a pain clinic for psychological counseling. He was determined to have "somaticized his difficulties and developed a hypochondriacal neurosis."

His orthopedic physician brought an action seeking total and permanent disability. The trial court awarded him just 5% loss of ability to earn as a result of the injury.

The appellate court said that factors other than strict medical physical disability are properly considered in determining workers compensation cases.

The court noted that there was no evidence that Mr. Armstrong was malingering but there was evidence that he had a psychological disorder wherein his current symptoms were exacerbated by his psychological functioning.

The court noted that the trial court finding of 5% loss of ability to earn was the same percentage of permanent disability assigned by the orthopedic physician who had not considered Mr. Armstrong's psychological condition. Thus, the court reversed the trial court judgment and remanded the case for further proceedings. *Armstrong v. Lewis & Associates Construction Co.*, Court of Civic Appeals of Alabama, May 9, 1984 (BI/05/My.—\$5)

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## New York City taps Gwynne as employee benefits director

**Donna Gwynne**, 31, has been named employee benefits program director for the city of New York. In this newly created position, Ms. Gwynne is responsible for the administration of the city's health insurance program and the supervision of the city's other benefit programs. She also will monitor the administration and operation of city unions' welfare plans. She reports to Robert W. Linn, director of the office of municipal labor relations. Previously, Ms. Gwynne was a deputy director in the Mayor's Office of Municipal Labor Relations for the city of New York. She received a bachelor of arts degree in economics from the University of New Hampshire in 1974 and a master's degree in public administration from George Washington University in Washington in 1976. She currently is studying for the Certified Employee Benefit Specialist designation.

**George B. Netherton**, 37, has been promoted to assistant director of the corporate risk management department of The Coca-Cola Co. in Atlanta. In this newly created position, Mr. Netherton is responsible for the design, purchase, implementation and administration of the property/casualty and workers compensation programs for the company. He also will retain the responsibilities of his previous job,

### comings & goings: buyers

entertainment risk manager for the company's Columbia Pictures subsidiary. He reports to William H. Quay Jr., Coca-Cola Co.'s assistant treasurer and director of risk management. Mr. Netherton received a bachelor of business administration degree from The College of Insurance in business administration from Fordham University in New York in 1983. He has both the Chartered Property & Casualty Underwriter and the Associate in Risk Management designations.

**Frances Quinn Mylett**, 36, has been promoted to assistant vp at Fidelity Bank in Philadelphia. In this newly created position, Ms. Mylett is responsible for the design, purchase and implementation of property/casualty insurance programs, as well as loss control and workers compensation supervision. She reports to Frank Noonan, senior vp and controller. Previously, Ms. Mylett was senior insurance officer for Fidelity. She is director of both the Delaware Valley Chapter of the Risk & Insurance Management Society and the Insurance Society of Philadelphia.



Ms. Mylett

**Bettina B. Browne**, 33, has been promoted to assistant vp and risk manager for International Service System, a security and management service company in New York. In this newly created position, Ms. Browne is responsible for the design and administration of all property/casualty insurance programs as well as all group life, medical and income protection plans for the corporation. She reports to Henrik Slipsager, senior vp. Previously, Ms. Browne was risk manager for the company. She received a bachelor of science degree in business from Pace University in White Plains, N.Y. in 1981 and currently is studying for a juris doctor degree at Pace University.

**Sharon Harshman**, 44, has joined Washington Mutual Service Corp. in Seattle as operations officer and risk manager. In this newly created position, Ms. Harshman will design, implement and coordinate the company's insurance and loss-control programs. She reports to company President James Rensel. Previously, Ms. Harshman was account executive for the Jenkins Insurance Agency Inc. in Spokane, Wash.

**Salvatore Saputo**, 34, is the new director of risk management for Wayne County, Mich. Mr. Saputo is responsible for supervising a staff of 19 people in various areas of risk management and employee benefits, including general liability insurance, property/casualty insurance, safety and loss control pro-

grams and workers compensation. He reports to Fred Todd, chief financial officer and replaces **Lyle Self**, who is now manager of insurance products and services for the Michigan Dental Assn. in Lansing. Previously, Mr. Saputo was purchasing agent/risk manager for the city of Battle Creek, Mich. He received a bachelor of science degree in history and English from Western Michigan University in 1977 and a master's degree in public health from Western Michigan in 1978. He currently is studying for the Certified Employee Benefit Specialist designation.

**Kenneth R. Swisher**, 39, is the new purchasing agent/risk manager for the city of Battle Creek, Mich., replacing Mr. Saputo. Mr. Swisher is responsible for supervising the purchase of all insurance policies and other risk management functions, including loss control and safety, for the city. He also will be responsible for the city's self-insured workers compensation program. He reports to Merrill Stanley, finance director. Previously, Mr. Swisher was risk manager for the city of Kalamazoo, Mich. He received a bachelor of science degree in management and administration from Indiana University in Indianapolis in 1972 and a master's degree in business administration, specializing in finance and international business, from Indiana University in Bloomington in 1976. He also has the Associate in Risk Management designation and is president of the Michigan Public Risk & Insurance Management Assn.

**John C. Andrews**, 49, is the new risk manager for Cluett, Peabody & Co. in New York. Mr. Andrews is responsible for the design, coordination and implementation of risk management and insurance programs for the company and its 21 national and international subsidiaries. He reports to J. Kirk Barefoot, director of corporate risk management and replaces **Neuman Wood**, who is doing consulting work for Cluett. Previously, Mr. Andrews was president of his own insurance agency, Andrews & Smalley, in Waterloo, N.Y. He received a bachelor of business administration degree from Manhattan College in 1957.

We'd like to report on staff changes in your company's risk management, safety or employee benefits department. Just drop a note to Diane Kastiel, Business Insurance, 740 N. Rush St., Chicago, Ill. 60611, or call 312-649-5393. Please send a photograph, too.

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## Storm damage estimate is \$55 million

NEW YORK—Wind, hail, tornadoes and flooding caused an estimated \$55 million in insured property damage in parts of Texas, New Mexico and Oklahoma on April 25-30, according to C.E. Hermanson, vp of the Property Claim Services division of the American Insurance Services Group Inc.

Most of the damage—\$35 million

—occurred in Texas. Hardest-hit were Gray, Cherokee, Gregg and Kaufman counties.

Insured losses in New Mexico were estimated at \$15 million. Damage in Oklahoma was estimated at \$5 million.

The storm was assigned Catastrophe Number 65 by the Insurance Services Office. ■



Photographed at Altos de Chavón, Dominican Republic.

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### info

- A new book from the Employee Benefit Research Institute will help educate consumers and employers about **employee benefits**. The 28-chapter "Fundamentals of Employee Benefit Programs" discusses Social Security, pensions, Individual Retirement Accounts, health insurance and education benefits. To order, send \$15 for a paperback copy to EBRI-ERF Publications, 2121 K St. N.W., Suite 860, Washington, D.C. 20037-2121.

- An examination of the major changes affecting **self-insurance** resulting from the 1984 Deficit Reduction Act is now available from D.A. Betterley Risk Consultants Inc. The publication reviews DEFRA's implications for self-insurance and captives. To order, send \$20 to D.A. Betterley Risk

Consultants Inc., 446 Main St., Worcester Plaza, Worcester, Mass. 01608.

- The National Advisory Committee for State Data Commission's final report and recommendations for the collection and disclosure of **provider specific health care data** is available for \$10 from the Washington Business Group on Health, 922 Pennsylvania Ave. S.E., Washington, D.C. 20003.

- Each state's requirements for employers that want to **self-insure workers compensation risks** are detailed in a booklet from the National Council of Self-Insurers. It was compiled by John J. Molloy, manager of workers compensation for K mart Corp. in Troy, Mich. K mart self-insures its work comp risks in every state where self-insurance is permitted. The booklet costs \$10 for NCSI members and \$20 for non-members and is available from the NCSI, 10 South Riverside Plaza, Suite 1530, Chicago, Ill. 60606.

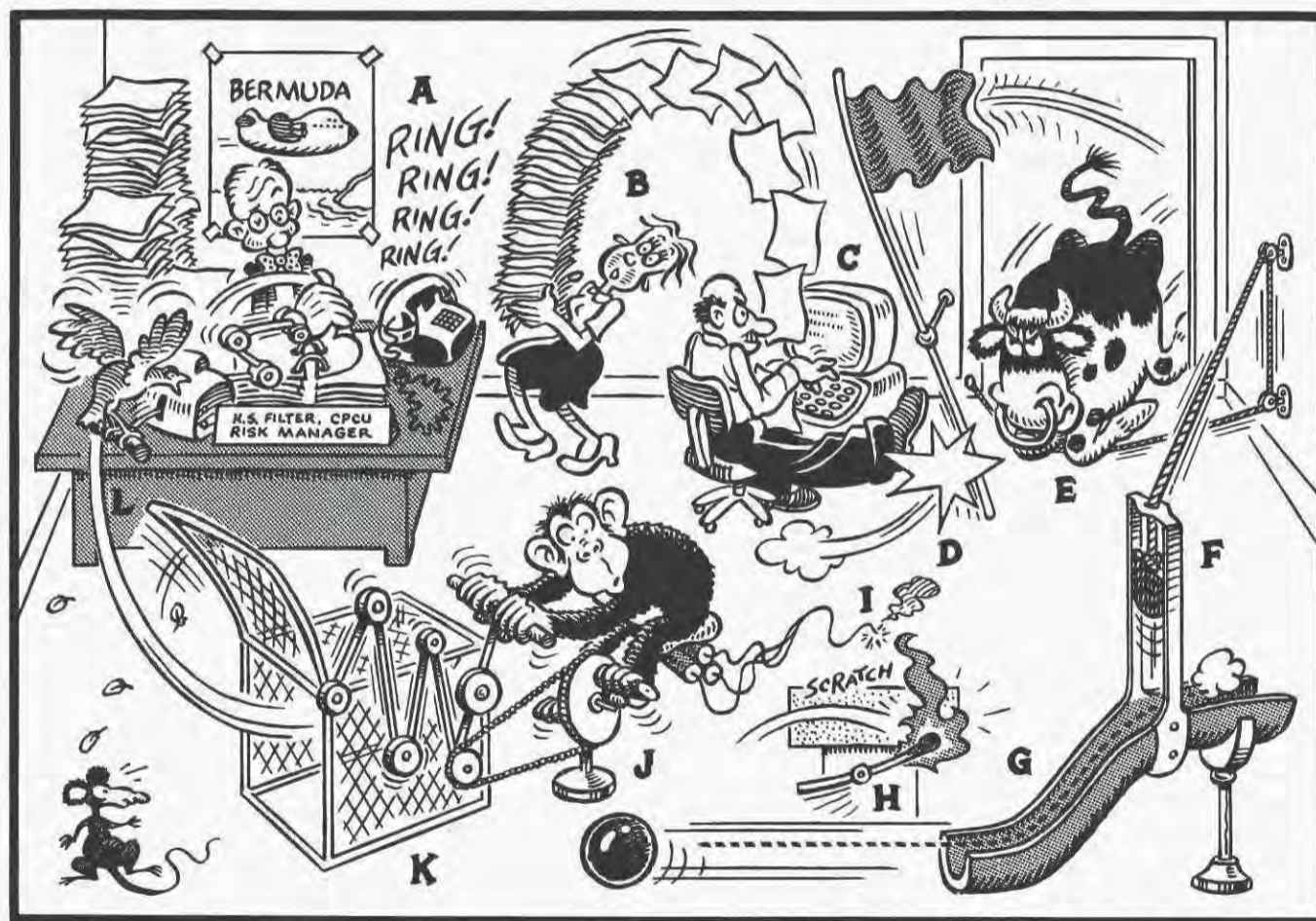
- The International Foundation of Employee Benefit Plans' "1985 Information Booklet" can be a valuable tool in researching **employee benefits**. The publication lists books, periodicals and research reports published by the foundation, and it also lists the foundation officers, directors, committee members and key staff personnel. For a free copy, write IFEBP, 18700 W. Bluemound Road, P.O. Box 69, Brookfield, Wis. 53005.

- Current strategies for **managing the cost of health care benefits** are discussed in the new study, "Health Care Cost Management: Private Sector Initiatives." The 216-page softbound book covers benefit plan designs; alternative health care delivery systems; utilization review; health care coalitions; and worksite wellness programs. To order, send \$22.50 to Health Administration Press, Department FWG, 1021 E. Huron St., The University of Michigan, Ann Arbor, Mich. 48109.

- For multinational companies, the cost of providing insured employee benefits to their overseas workforces can sometimes exceed 20% of those workers' salaries. A book by Mercer International discusses the advantages and disadvantages of **multinational pooling**. It explains how to create a pooling system that fits a company's needs and gives a detailed analysis of the international pools and the benefits each insures. For a free copy of "Multinational Pooling: A Guide for Multinational Companies with Employee Benefit Plans," write Giles Archibald, William M. Mercer International, 1211 Avenue of the Americas, New York, N.Y. 10036.

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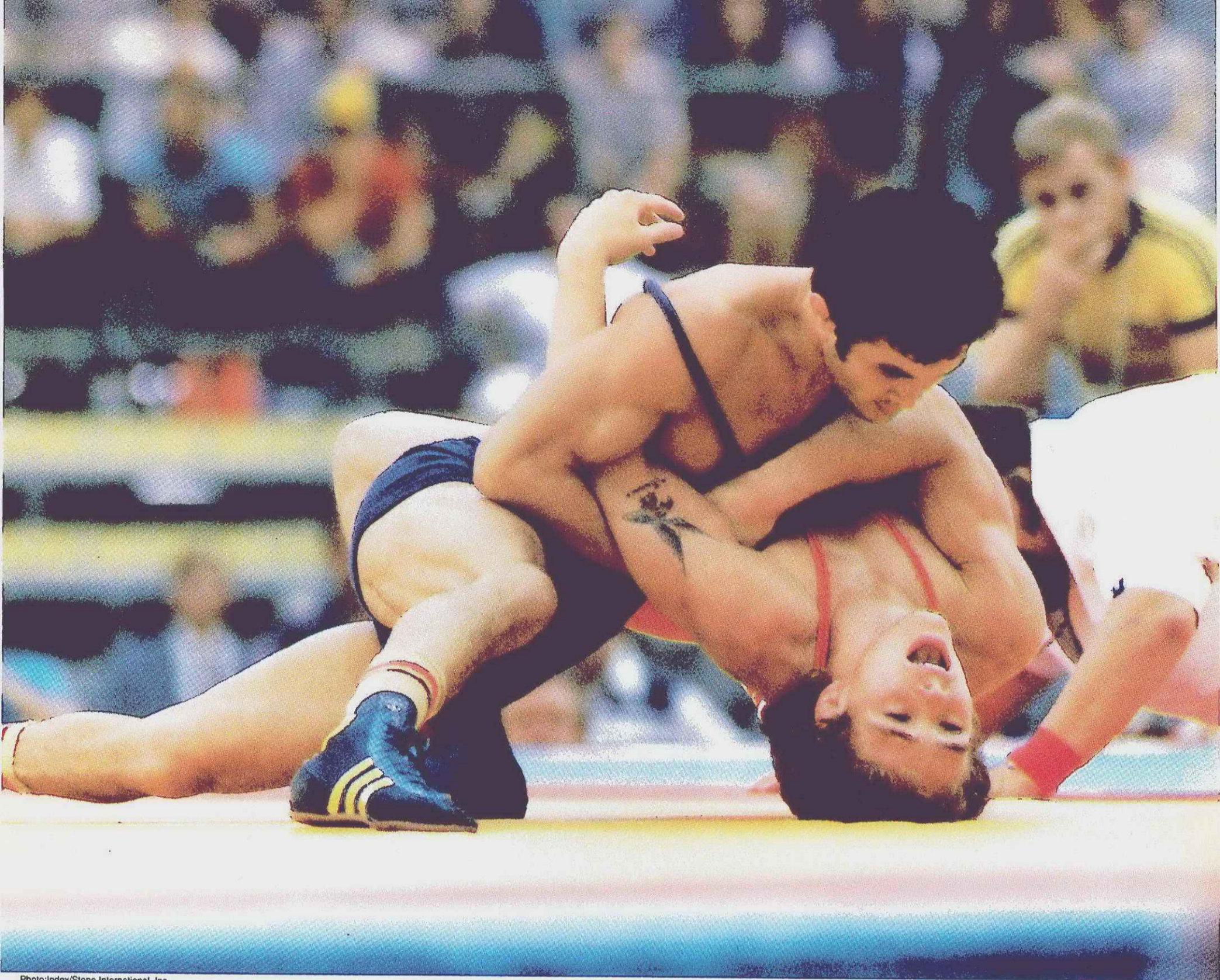


Photo: Index/Stone International, Inc.

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<sup>1</sup>**dom-i-nance** \ˈdam(-e)-nen(t)s\ *n*: the fact or state of being dominant\*

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# Illinois Chamber affiliate urges changes in comp procedures

By CAROL CAIN

SPRINGFIELD, Ill.—A consumer affiliate of the Illinois Chamber of Commerce is recommending that the Illinois Industrial Commission change some of its administrative procedures to improve its handling of disputed workers compensation cases.

The preliminary findings of a recent study of the state Industrial

Commission completed by the Illinois Alliance for Economic Initiatives identified four areas for reform. The IAEL, the Chamber affiliate, is a coalition of concerned citizens, associations and government representatives dedicated to improving Illinois' business climate and economic growth.

The recommendations are:

- Amend the Illinois Workers' Compensation Act so that employ-

ers would report only those injuries that result in loss of time of more than three working days by an injured worker.

- The state's Bureau of the Budget should provide adequate funding for the Industrial Commission so it can compile valid statistics.

- The Industrial Commission should enter into a pilot project with the National Council on Compensation Insurance—the national workers compensation ratemaking and statistical organization—to provide for an on-line computer linkup to provide required insurance coverage information.

- The development of uniform standards by the Industrial Commission to expedite hearings and eliminate continuances.

The Chamber is looking for appropriate legislation in the Illinois General Assembly to attach the coalition's first recommendation of requiring employers to report only those workplace injuries that result in loss of time of more than three working days, according to Steven Rosenbaum, the Chamber's manager of workers compensation and unemployment insurance programs.

Such a change would substan-

**Without funding, accident forms are 'serving no useful purpose,' the coalition report says.**

tially reduce the number of reports employers would be required to file, and yet provide a manageable number of reports to form a vital, accurate, statistical base, noted Eric Canada, director of the IAEL.

A survey of the accident reporting requirements of other large industrial states indicates that, though requirements differ, Illinois is second only to California in the number of reports required by law, Mr. Canada said.

"By law, the Industrial Commission is required to compile and distribute aggregate accident statistics to assist employers in their loss prevention programs. However, the Bureau of the Budget has failed to provide funds for the Industrial Commission to computerize these statistics. Lacking funding, these forms are merely gathering in the basement of (a state building) —in most cases unopened—and serving no useful purpose whatsoever," notes the coalition's report.

The Chamber will be talking with state legislators and others in an attempt to secure more funds for the Industrial Commission for collecting data, Mr. Rosenbaum said.

The coalition's other recommendations are being studied by Mervin Bachman, chairman of the Industrial Commission. Mr. Bachman has appointed a subcommittee to take a closer look at developing uniform motion standards.

The lack of uniformity among the Industrial Commission's 14 arbitrators confuses attorneys, insurers, employers and injured workers, and creates delays, which increase costs and increase case backlog, notes the report.

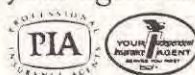
But this isn't the only item that Mr. Bachman wants to study. He has asked the IAEL to analyze the administrative procedures of industrial commissions in several states. On-site studies already are under way in Massachusetts, New York, California, Kentucky, Michigan and Florida, and a report is expected by mid-June.



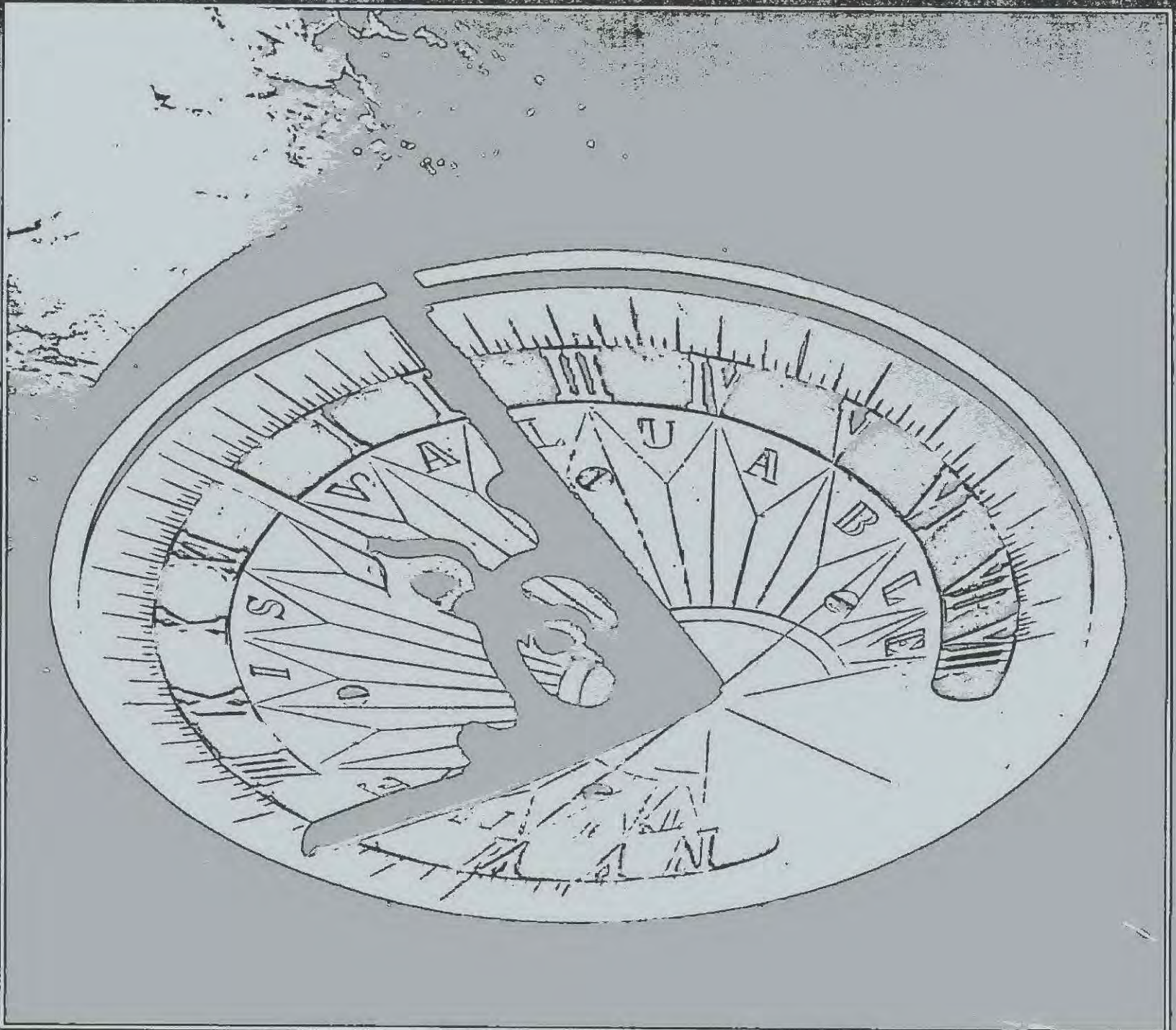
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# N.Y. exchange syndicate to start writing in June

First Riverside Syndicate Inc., a new New York Insurance Exchange syndicate capitalized at \$3.5 million, is expected to begin writing reinsurance by June 15.

The new syndicate is owned by Hospital Underwriting Group Inc., a property/casualty insurer based in Nashville, Tenn.

John J. Middleton, vp and chief operating officer of Hospital Underwriting, said First Riverside would be managed by CIGNA Syndicate Managers Inc.

"We've formed this syndicate as a means of strengthening our corporation through diversification in a manageable and orderly fashion," Mr. Middleton said.

"The market is continuing to harden, and we think the time is particularly favorable for expansion into the U.S. and international

## markets

arenas accessible via the exchange," he said.

The new syndicate, which is the 47th member of the New York exchange, was approved by the exchange's board of governors at its annual meeting earlier this year.

### Doctors' reciprocal

The Florida Physicians Insurance Reciprocal will be converted to stock ownership next Jan. 1 if policyholders and regulatory authorities approve the change.

The newly formed company will be renamed the Florida Physicians Insurance Co., and its headquarters

will continue to be in Jacksonville.

Dr. Frank C. Coleman, chairman of the company's board of directors, said the move is one of several actions designed to make FPIR "a major writer of medical professional liability insurance" in Florida.

David L. Rader, president of FPIR, said the conversion "makes sense for all concerned."

"The insured will become a direct owner, the company will be better-managed and the Florida Medical Assn. will be offered an ownership position or will have an opportunity to gain an ownership position," according to Mr. Rader.

Mr. Rader said approval of two-

thirds of FPIR's policyholders as well as Florida's Department of Insurance and Division of Securities was needed for the change.

The Florida Physicians Insurance Reciprocal has 1,550 policyholders and about \$22 million in annual premiums, according to Dr. Coleman.

### Insurer purchase

The Equitable Life Assurance Society of the United States has agreed to purchase the Monumental National Life Insurance Co. of New York for around \$9 million, according to Equitable.

Monumental is a subsidiary of Monumental Life Insurance Co. in Baltimore, which is owned by the Monumental Corp., which is also in Baltimore. The sale is expected to

be completed by June 30, pending the approval of regulatory authorities.

Monumental National's revenues in 1984 were about \$1.8 million, according to figures released by Equitable.

### Mergers/acquisitions

Marsh & McLennan Associates Inc. in San Francisco has acquired the business of McNary & McNary Jewelers Insurance Services Inc., the broker for insurance programs sponsored by the California Jewelers Assn. The McNary staff has moved to the M&M office at Three Embarcadero Center, P.O. Box 7157, San Francisco, Calif. 94120; 415-393-5300.

Corroon & Black Corp. has agreed to acquire Dale K. Larson Inc., an agency and brokerage in Royal Oak, Mich., in exchange for shares of Corroon & Black common stock. Larson, which specializes in placing insurance for municipalities, will be combined with Corroon & Black of Michigan Inc. in Detroit. Dale Larson, owner and manager of Larson, will be a senior executive of C&B of Michigan.

CIGNA Corp. has acquired Trilog Inc., a Philadelphia-based marketer of mainframe and personal computer software for administering pension services. Trilog also provides recordkeeping for defined contribution and defined benefit retirement plans. The value of the transaction was not disclosed.

Thomas J. Inglott Associates Inc., an insurance agency in Long Beach, Calif., has merged with Mason-McDuffie Insurance Service Inc., an independent agency based in Pleasant Hill, Calif. The new operation, Mason McDuffie-Inglott & Associates, will be located at the Fullerton, Calif., offices of Mason-McDuffie.

ABI Management Inc. in San Francisco has acquired Los Angeles insurance brokerage Wellington Insurance Services.

Starkweather & Shepley Inc., a Providence, R.I., insurance agency, has acquired the Robert H. Lang Insurance Agency, also of Providence.

### New offices

Meadowbrook Insurance Group of Southfield, Mich. has formed two subsidiaries in New York. Meadowbrook Intermediaries Inc. is a new reinsurance intermediary that will place all types of reinsurance, and Meadowbrook Risk Management Inc. has been formed to provide risk management services for insurance companies. Both are located at 23 E. 39th St., New York, N.Y. 10016; 212-972-2166.

Transco Insurance Services has moved to 55 E. Monroe St., Suite 4440, Chicago, Ill., 60603; 312-1027.

Hope Agency Inc. has moved to 36-28 Union St., Flushing, N.Y., 11354; 718-961-5000.

The FPE Group has relocated to 3687 Mount Diablo Blvd., Suite 200, Lafayette, Calif. 94549; 415-283-8860.

Beck/Wm. Schwartz Inc. has moved its world headquarters to 3050 Post Oak Blvd., Suite 1700, Houston, Texas 77056; 713-622-4364.

Independent Insurance Wholesalers Inc., a wholesale brokerage based in Tigard, Ore., is opening a new California office. The address is Heritage Park Corporate Center, 11883 Dublin Ave., Suite B-210, Dublin, Calif. 94568.

Bryson Associates Inc., a surplus lines brokerage based in Jenkintown, Pa., has opened an office at 111 John St., New York, N.Y. 10038.



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# Child-care benefit still rare despite growth: EBRI

WASHINGTON—Although the number of companies offering child care as an employee benefit has tripled since 1982, only about 1,800 employers offer the benefit, according to the Employee Benefit Research Institute in Washington.

The number of employers offering the benefit is small, EBRI notes, despite changes in the demographics of the workforce and reports by employers that offer child care which indicate the benefit has decreased turnover and increased employee productivity.

Changes in the workforce point to an increased need for child care, EBRI says. For example, by 1990, an estimated 10.4 million children under the age of 6 will have working mothers.

Nearly 60% of married mothers with children age 5 or under are currently in the workforce, compared with 37% in 1970. And, increases in divorce and single parenthood have caused a steady increase in recent years in the percentage of single-parent households.

In fact, EBRI says, the number of young children being reared in two-parent households in which only one parent works outside the home actually may decline, if current trends continue.

EBRI also contends that child care is a benefit for employers as well.

to be licensed. However, employees seem to prefer small-group child-care situations, like care in their home or the home of another adult, and such child-care situations usually are not licensed.

- Some employers may not realize the growing need for child-care, and the types of options available.

- The cost, administrative burden and potential liability involved in an on-site center may be prohibitive to some employers.

- Proposed changes in the tax-preferred status of child-care and other employee benefits could cause administrative problems if, for example, an employer had to determine the per-employee share of the cost of running an on-site day-care center.

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**Only about 1,800 of the estimated 6 million U.S. employers offer a child-care benefit.**

According to surveys of employers that offer a child-care benefit to employees, the employers report less turnover and absenteeism, high employee morale and productivity and an enhanced ability to recruit new employees.

However, employers that offer a child-care benefit are the exception rather than the rule, according to EBRI.

The number of employers offering some kind of child-care help—ranging from on-site care facilities to referral services to financial assistance—has tripled in the last three years. However, only about 1,800 of the estimated 6 million U.S. employers offer the benefit.

According to the Work & Family Information Center of the Conference Board, a non-profit New York research organization, about 550 employers offer on-site or near-site child-care centers; 30 offer support for family day care; 50 offer after-school child-care; 20 offer sick child-care programs; 300 offer information and referral services; and 825 offer financial assistance, including vouchers, discounts and a child-care option for a flexible spending account.

In addition, the Conference Board estimates that between 500 and 1,000 companies offer parent education seminars, and a similar number make corporate contributions to community child-care services, according to EBRI.

EBRI suggests several reasons employers may be reluctant to provide child-care benefits to their employees:

- Some employers may be discouraged because utilization rates are low—typically 4% to 10% of employees. Similarly, demand for the benefit is low.

EBRI suggests that one reason is that employers usually require child-care they sponsor or support

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**JUNE 16. Structured Settlements and Risk Management** seminar in Minneapolis, sponsored by Settlement Planning Inc., \$95. Dave Terwilliger, Settlement Planning Inc., 6800 France Ave. South, Minneapolis, Minn. 55435; 800-922-6800, 612-920-6166.

**JUNE 17-18. Health Care Cost Containment** workshop in New York, sponsored by Health Research Institute; \$395. Workshop Coordinator, Health Research Institute, 49 Quail Court, Suite 200, Walnut Creek, Calif. 94596.

**JUNE 17-19. 1985 Trustees and Administrators Institutes** in Lake Tahoe, Nev., sponsored by The International Foundation of Employee Benefit Plans; \$420 for members; \$495 for non-members. Also Sept. 23-25 in Banff, Alberta, Canada. Regis-

tration Department, IFEBP, P.O. Box 69, Brookfield, Wis. 53008-0069.

**JUNE 18. Defending Insurance Claims for Hazardous Waste Damages** seminar in New York, sponsored by The College of Insurance; \$295. Ronnie Krannis, Professional Development Programs, The College of Insurance, One Insurance Plaza—101 Murray St., New York, N.Y. 10007; 212-962-4111.

**JUNE 18-20. Industrial Fire School** in Marinette, Wis., sponsored by Ansul Fire Protection; \$650. Also Aug. 6-8, Sept. 17-19 and Oct. 7-9, all in Marinette. Sara Lambrecht, Ansul Fire Protection, 1 Stanton St., Marinette, Wis. 54143.

**JUNE 19. Long Island Update: Cost Contain-**

**ment Through Benefits Design and Administration** seminar in Plainview, N.Y., sponsored by The New York Business Group on Health; \$10 for members; \$25 for non-members. Registrar, The New York Business Group on Health Inc., 1633 Broadway, 46th floor, New York, N.Y. 10019; 212-397-1260.

**JUNE 19. Health Improvement/Prevention Workshop** in New York, sponsored by the Health Research Institute; \$195. Contact Workshop Coordinator, Health Research Institute, 49 Quail Court, Suite 200, Walnut Creek, Calif. 94596; 415-676-2320.

**JUNE 19. Advanced Cost Containment** workshop in New York, sponsored by Health Research Institute; \$195. Workshop Coordinator, Health Research Institute, 49 Quail Court, Suite 200, Walnut Creek, Calif. 94596; 415-676-2320.

**JUNE 19. Third-Party Administrator** work-

shop in New York, sponsored by Health Research Institute; \$395; \$195 for subsequent registrants from same company. Workshop Coordinator, Health Research Coordinator, 49 Quail Court, Suite 200, Walnut Creek, Calif. 94596; 415-676-2320.

**JUNE 19-21. 16th Annual Ohio Self-Insurers Assn.** conference in Dayton, Ohio; \$125 for members; \$250 for non-members. Make checks payable to Gerald Thomas, 313 S. Algonquin Ave., Columbus, Ohio 43204; for information, call Richard Schafstall, Ohio Self-Insurers Assn., president, 513-632-3331.

**JUNE 19-21. Florida Assn. of Self Insurers** fourth annual seminar in Orlando Fla.; \$150 for members; \$175 for non-members. Registrar, FASI, P.O. Box 4850, Winter Park, Fla. 32793; 305-657-9574.

**JUNE 19-21. Fourth Annual Workers Compensation** seminar in Orlando, Fla., sponsored by the Florida Assn. of Self Insurers; \$150 for members;

\$175 for non-members. Keylon Patch, executive director, FASI, P.O. Box 4850, Winter Park, Fla. 32793; 305-657-9574.

**JUNE 20. Medical Directors** workshop in New York, sponsored by the Health Research Institute; \$195. Registrar, Health Research Institute, 49 Quail Court, Suite 200, Walnut Creek, Calif. 94596; 415-676-2320.

**JUNE 20-21. Perinatal Risk Management: Understanding and Preventing the Multimillion Dollar Claim** seminar in Houston, sponsored by the American Society for Hospital Risk Management and The Structured Settlements Co.; \$175 for ASHRM members; \$235 for non-members. Also Sept. 30-Oct. 1 in San Francisco. Registrar, American Hospital Assn., Division of Education, 840 N. Lake Shore Drive, Chicago, Ill. 60611; 312-280-6083.

**JUNE 20-21. Labor/Management** conference in New York, sponsored by Health Research Institute; \$195. Workshop Coordinator, Health Research Institute, 49 Quail Court, Suite 200, Walnut Creek, Calif. 94596; 415-676-2320.

**JUNE 20-21. The Brief Course in Reinsurance** in New York, sponsored by The College of Insurance; \$145. Laura McKeon, Professional Development Programs, The College of Insurance, One Insurance Plaza—101 Murray St., New York, N.Y. 10007; 212-962-4111.

**JUNE 23-27. The Advanced Course in Reinsurance** in New York, sponsored by The College of Insurance; \$825 for college sponsors; \$950 for others. Laura McKeon, Professional Development Programs, The College of Insurance, One Insurance Plaza—101 Murray St., New York, N.Y. 10007; 212-962-4111.

**JUNE 23-28. The Management Program** in New York, sponsored by The College of Insurance; \$825 for college sponsors; \$950 for others. Call or write Russel Fershleiser, Professional Development Programs, The College of Insurance, One Insurance Plaza—101 Murray St., New York, N.Y. 10007; 212-962-4111.

**JUNE 24. Tax Reform Implications for Employee Benefit Plans** program in New York, sponsored by the International Foundation of Employee Benefit Plans; \$140 for members; \$165 for non-members. Also June 25 in Detroit, June 26 in Seattle, June 27 in Los Angeles, July 8 in Boston, July 9 in Chicago, July 10 in Minneapolis and July 11 in San Francisco. Registrar, IFEBP, P.O. Box 69, Brookfield, Wis. 53008-0069.

**JUNE 24-26. Petroleum/Chemical Fire School** in Marinette, Wis., sponsored by Ansul Fire Protection; \$650. Also July 16-18, Aug. 20-22, Sept. 10-12 and Oct. 1-3, all in Marinette. Sara Lambrecht, Ansul Fire Protection, 1 Stanton St., Marinette, Wis. 54143.

**JUNE 24-26. Wellness Strategies** conference in Trenton, N.J., sponsored by the National Wellness Institute; \$250; \$25 discount to members. To register, contact the Registrar, National Wellness Institute, South Hall, University of Wisconsin-Stevens Point Foundation, Stevens Point, Wis. 54481; 715-346-2172/2572.

**JUNE 26-28. Successful Retirement Planning Programs** workshop in Chicago, sponsored by Retirement Advisors Inc.; \$450. Also Oct. 16-18 in Kansas City, Kan., and Nov. 6-8 in New York. Registrar, 919 Third Ave., New York, N.Y.; 212-421-2400.

**JUNE 27. Stress Management: Sharing Japan's and America's Experiences** conference in New York, by The New York Business Group on Health Inc.; fees to be announced. The New York Business Group on Health Inc., 1633 Broadway, 46th floor, New York, N.Y. 10019; 212-397-1260.

**JUNE 27-28. Media Insurance and Risk Management** seminar in New York, sponsored by the Practising Law Institute; \$390. Ann Tracy, PLI, 810 Seventh Ave., New York, New York 10019; 212-765-5700.

**JULY 15-19. Occupational Respiratory Protection** course in Los Angeles, sponsored by the University of Southern California; \$750. Registrar, Office of Extension and In-Service Programs, Institute of Safety and Systems Management, University of Southern California, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**JULY 16. Preparedness for Chemical Emergencies** conference in Chicago, sponsored by Illinois State Chamber of Commerce; \$90 for members; \$135 for non-members. Carol Jensen, ISCC, 20 N. Wacker Dr., Chicago, Ill. 60606; 312-372-7373.

**JULY 17. Health Care Cost Containment** conference in Chicago, sponsored by Illinois State Chamber of Commerce; \$90 for members; \$135 for non-members. For information, contact Carol Jensen, ISCC, 20 N. Wacker Dr., Chicago, Ill. 60606; 312-372-7373.

**JULY 17. Plan Design** conference in Chicago, offered by the Illinois State Chamber of Commerce; \$90 for members; \$135 for non-members. Registrar, ISCC, Center for Business Management, 20 N. Wacker Dr., Chicago, Ill. 60606; 312-372-7373.

**JULY 21-27. National Wellness** conference in Stevens Point, Wis., sponsored by the University of Wisconsin—Stevens Point; \$325 for the week; \$75 per day; members of the National Wellness Assn. receive \$15 discount on full registration; organizations with three or more attendants receive special discounts. Registrar, National Wellness Conference, South Hall, UWSP, South Point, Wis. 54481; 715-346-2172/2572.

**JULY 22-23. Asset/Liability Management: Profitability and Risk in a Time of Change** conference in Boston, sponsored by Peat Marwick and Darling & Associates; \$675. Registrar, Executive Education Department, 810 Seventh Ave., 28th Floor, New York, N.Y. 10019; 1-800-762-3932.

*Continued on next page*

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**JULY 22-26. Sampling and Evaluating Airborne Asbestos Dust** course in Los Angeles, sponsored by the University of Southern California; \$675. Registrar, Office of Extension and In-Service Programs, Institute of Safety and Systems Management, University of Southern California, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**JULY 29-31. Industrial Hygiene Sampling Strategies** course in Los Angeles, sponsored by the University of Southern California; \$425. Registrar, Office of Extension and In-Service Programs, Institute of Safety and Systems Management, University of Southern California, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**JULY 30-AUG. 1. Utilities Fire School** in Marinette, Wis., sponsored by Ansol Fire Protection; \$650. Also, **Aug. 27-29** in Marinette. Sara Lambrecht, Ansol Fire Protection, 1 Stanton St., Marinette, Wis. 54143.

**AUG. 4-6. Business Insurance Employee Benefits Communications** conference in New York, sponsored by *Business Insurance*; \$575. Registrar, Business Insurance Communications Services Department, Business Insurance, 220 E. 42nd St., New York, N.Y. 10017; 212-210-0137.

**AUG. 5-7. Recognition of Accident Potential in the Workplace Due to Human Factors** course in Los Angeles, sponsored by the University of Southern California; \$425. Registrar, Office of Extension and In-Service Programs, Institute of Safety and Systems Management, University of Southern California, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**AUG. 8-9. Legal Aspects of Occupational Safety and Health** course in Los Angeles, sponsored by the University of Southern California; \$375. Registrar, Office of Extension and In-Service Programs, Institute of Safety and Systems Management, University of Southern California, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**AUG. 11-14. 1985 Communications Institute** program in Monterey, Calif., sponsored by the International Foundation of Employee Benefit Plans; \$420 for members; \$495 for non-members. Registrar, IFEBP, 18700 W. Bluemound Road, P.O. Box 69, Brookfield, Wis. 53005-0069; 414-786-6700.

**AUG. 12. Plan Administration** conference in Chicago, sponsored by the Illinois State Chamber of Commerce; \$90 for members; \$135 for non-members. Registrar, ISSC, Center for Business Management, 20 N. Wacker Drive, Chicago, Ill. 60606; 312-372-7373.

**AUG. 18-21. 1985 Corporate Benefits Management** conference in Lake Tahoe, Nev., sponsored by the International Foundation of Employee Benefit Plans; \$500 for members; \$575 for non-members. Registrar, IFEBP, 18700 W. Bluemound Road, P.O. Box 69, Brookfield, Wis., 53005-0069; 414-786-6700.

**AUG. 18-22. 71st Annual Convention of the International Assn. of Industrial Accident Boards and Commissions** in Sun Valley, Idaho; \$175 for members; \$240 for non-members. Larry Spjute, IAABC, P.O. Box 1252, Boise, Idaho 83701; 208-334-2193.

**AUG. 19-23. Developing and Managing a Basic Safety and Health Program** course in Long Grove, Ill., sponsored by the National Loss Control Service Corp.; \$650. Also **Oct. 28-Nov. 1** in Long Grove. Tommy Thomas, NATLSCO, Route 22 and Kemper Drive, Long Grove, Ill. 60049; 312-540-2400, 800-323-9585.

**AUG. 19-23. Recognition of Occupational Health Hazards** course in Los Angeles, sponsored by the University of Southern California; \$675. Registrar, Office of Extension and In-Service Programs, Institute of Safety and Systems Management, University of Southern California, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**SEPT. 3-6. Reinsurance Accounting & Finance for Cedents & Assurers** seminar in Crotonville, N.Y., sponsored by Robert W. Strain Seminars Inc.; \$1,245. Registrar, Strain Seminars Inc., P.O. Box 1000, Wingdale, N.Y. 12594; 914-832-9384.

**SEPT. 6-7. Workers Compensation: Your Safety & Health Balance Sheet** course in Los Angeles, sponsored by the University of Southern California; \$250. Registrar, Office of Extension and In-Service Programs, Institute of Safety and Systems Management, University of Southern California, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**SEPT. 9-13. Fundamentals of Industrial Hygiene Monitoring** course in Long Grove, Ill., sponsored by the National Loss Control Service Corp.; \$500; 10% discount for two or more registrants from the same company. Also **Nov. 11-15** in Long Grove. John Garis, NATLSCO, Long Grove, Ill. 60049; 312-540-2026.

**SEPT. 9-13. Fundamentals of Money Management** workshops in Philadelphia, sponsored by the International Foundation of Employee Benefit Plans; \$700 for members; \$825 for non-members. Registrar, IFEBP, 18700 W. Bluemound Road, P.O. Box 69, Brookfield, Wis. 53005-0069; 414-786-6701.

**SEPT. 9-13. Hazardous Materials: Handling and Disposal** course in Los Angeles, sponsored by the University of Southern California; \$675. Registrar, USC, Institute of Safety and Systems Management, Office of Extension and In-Service Programs, Los Angeles, Calif. 90089-0021; 213-743-6523/6524.

**SEPT. 20. Employee Education** conference in Chicago, sponsored by the Illinois State Chamber of Commerce; \$90 for members; \$135 for non-members. Registrar, ISSC, Center for Business Management, 20 N. Wacker Drive, Chicago, Ill. 60606; 312-372-7373.

**SEPT. 21-24. International Benefits** seminar in St. Thomas, Virgin Islands, sponsored by the International Foundation of Employee Benefit Plans; \$500 for members; \$575 for non-members.

Registrar, IFEBP, 18700 W. Bluemound Road, P.O. Box 69, Brookfield, Wis. 53005-0069; 414-786-6701.

**OCT. 1-3. Effective Training Skills** workshop in Norwood, Mass., sponsored by Factory Mutual Engineering Corp.; \$485. Registrar, Training Department, Factory Mutual Engineering, 1151 Boston-Providence Turnpike, P.O. Box 9102, Norwood, Mass. 02062.

**OCT. 3-4. Quantitative Techniques for Risk Management** seminar in New York, sponsored by The College of Insurance; \$495 for sponsoring participants; \$535 for all others. Registrar, Professional Development Programs Division, The College of Insurance, One Insurance Plaza, 101 Murray St., New York, N.Y. 10007; 212-962-4111.

**OCT. 3-6. The Fitness Providers Challenge: Marketing and Managing Employee Health Programs** conference in Fort Worth, Texas, sponsored by the Assn. for Fitness in Business; price not yet set. Susan Hagerty, AFB, 1312 Washington Blvd., Stamford, Conn. 06902.

**OCT. 7-10. Highly Protected Risk Property Conservation** course in Long Grove, Ill., sponsored by the Kemper Group; \$400; free for Kemper HPR-insured property owners. W.P. Thomas Jr., Manager, Engineering Research & Staff Development, HPR Department, A-1, Long Grove, Ill. 60049; 312-540-3380.

**OCT. 16. Health Promotion** conference in Chicago, sponsored by the Illinois State Chamber of Commerce; \$90 for members; \$135 for non-members.

Registrar, ISSC, Center for Business Management, 20 N. Wacker Drive, Chicago, Ill. 60606; 312-372-7373.

**OCT. 28-31. 5th Annual Construction Insurance** conference, New Orleans, by the International Risk Management Institute Inc.; \$585. Conference Coordinator, International Risk Management Institute Inc., 10300 N. Central Expressway, Building 3, Suite 208, Dallas, Texas 75231; 214-363-9656.

**OCT. 31. Rising to the Challenge** conference in Philadelphia, sponsored by the Philadelphia Chapter of the Society of Chartered Property and Casualty Underwriters, Independent Insurance Agents & Brokers Assn. of Philadelphia and Suburbs, Delaware Valley Chapter of The Risk & Insurance Management Society and the Insurance Society of Philadelphia; \$35. Peter Raymond, Aetna Life & Casualty, 1 Logan Square, Philadelphia, Pa. 19103; 215-854-7350.

**NOV. 19. Utilization/Data Management** conference in Chicago, sponsored by the Illinois State Chamber of Commerce; \$90 for members; \$135 for non-members. Registrar, ISSC, Center for Business Management, 20 N. Wacker Dr., Chicago, Ill. 60606; 312-372-7373.

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# U.S. courts make British underwriters wary

By STACY SHAPIRO

LONDON—Until Americans solve the liability problems that U.S. courts have created, British underwriters will continue to be

wary of North American casualty risks, said Lloyd's of London Deputy Chairman Murray Lawrence.

"We do not think our reaction to the U.S. is hysterical at all," Mr. Lawrence said at the recent confer-

ence of the British Insurance Brokers Assn.

"How can you play a game when you don't know what the rules will be? . . . This isn't a problem that can be resolved by throwing money at it. We cannot go on entering contracts today when we do not know how the courts will interpret those contracts in 30 years' time," he said.

Mr. Lawrence was responding to a BIBA member who asked if clients can expect a more-relaxed attitude by underwriters in 1986 toward underwriting U.S. casualty risks of North American companies or European companies that have North American exposures.

Clearly, Mr. Lawrence's answer was no. He said rate increases of 300% or more still are not enough to convince some Lloyd's non-marine underwriters to write many North American casualty risks.

"These particular horses are very frightened, and it will take a long time to get them back to the trough to drink again," said Mr. Lawrence, a non-marine underwriter and chairman of Lloyd's underwriting agency Murray Lawrence & Partners.

Another conference attendee asked if Lloyd's underwriters would prefer casualty risks to be written on a claims-made basis rather than an occurrence basis. A claims-made policy responds only to claims filed during the policy period, while an occurrence policy responds to any claims that occur during the policy period, regardless of when they are filed.

"Claims-made is not the panacea for all troubles, but it does go in the right direction," Mr. Lawrence replied. "But, I hate for people to think that it is the panacea for all ills. . . There are other problems to deal with, too, particularly in the U.S."

The Insurance Services Office has proposed two new commercial general liability forms, one a claims-made form, for adoption in

the United States next year (BI, May 20). And, Lloyd's underwriters are considering writing their own revised general liability form.

The question-and-answer session took place after Mr. Lawrence's speech to BIBA members on the role of Lloyd's and Lloyd's brokers.

Mr. Lawrence pointed out that it is a time of "great change" in the commercial and regulatory fields, not just at Lloyd's but everywhere in the industry.

In particular, the British government is moving to establish self-regulatory bodies to regulate companies involved in personal investments (see story, page 62).

Lloyd's hopes its brokers will continue to be self-regulated by the Council of Lloyd's and not be placed under another self-regulatory body, Mr. Lawrence said.

"Clearly, they must be regulated by Lloyd's, as at present, or by some other body either presently in existence or that might be set up. . . If the latter, it is difficult to see how the title Lloyd's broker could be retained and the effect of this would therefore be to do away with that title and throw open to Lloyd's every broker approved by that body," he said.

"There is, I believe, a general feeling that we would all be loath to see the demise of the title of Lloyd's broker, and therefore a general agreement that Lloyd's should be the body responsible for their regulation," he said.

If Lloyd's brokers are to remain self-regulated, the Council of Lloyd's will have to consider what other areas of brokers' business it should regulate, he said.

"We have seen so often in the past that any action by a firm that is a Lloyd's (firm) or is a company in the same group as a Lloyd's broker. . . rebounds well or badly on the reputation of Lloyd's as a whole. This is regardless of whether that action involves Lloyd's underwriters, or very often whether it is connected with insurance broking at all."

Lloyd's will draw up a code of conduct for all Lloyd's brokers as a "vital part of the regulatory machinery," said Mr. Lawrence.

Commercial and regulatory changes are also creating giant fi-

ancial services conglomerates that are making inroads into the insurance industry, particularly into the personal lines business, he said.

"You are all well aware of the heavy breathing down your necks of the banks and building societies (savings and loans)—all of them runners in the same race. That race seems to attract new entrants and ideas and become more competitive every day," he said.

"All of this you might think would be of little interest to Lloyd's, but it is."

He said that, as a result of these changes, Lloyd's is considering expanding its personal lines business, as it has done in the British automobile insurance sector.

"I have no doubt that we shall see more market initiatives to extend this general concept to other classes of business in the future, especially when our new business processing systems are in place," said Mr. Lawrence.

"This is most likely to develop in the householder, motor and small commercial areas and other small premium business where underwriters believe there is a profit to be made."

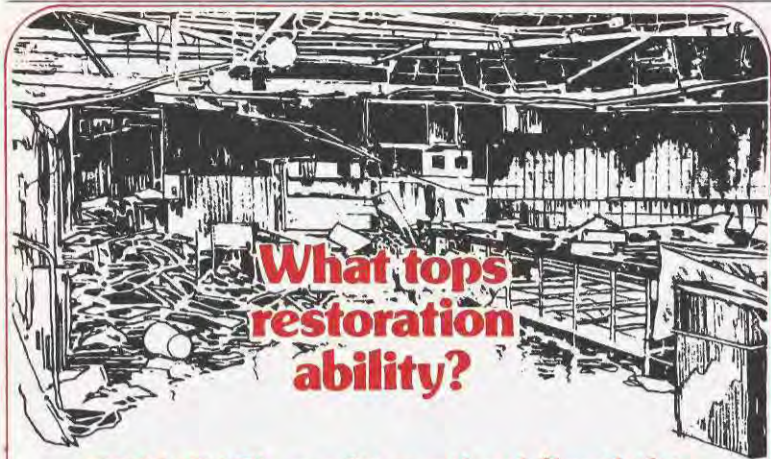
Also, Lloyd's brokerages appear to be getting involved in the "supermarket" approach of offering many services under one operation, Mr. Lawrence said, adding that he hopes this move is not being made too hastily.

"We shall see too many firms taking this route for the wrong reasons simply because it is the current fashion. In which case, if I am correct, these same companies will be hastily unbundling themselves at the end of this decade and through the 1990s," he said.

But, Mr. Lawrence concluded, the heart of the entire Lloyd's industry is "the interests of the client—his confidence in whatever new format is developed for the future must be safeguarded, and hence we are right back to regulation."

"Whatever system evolves in the future must be seen to be properly regulated. . . We cannot afford to wait for problems to come to light, before putting that regulation in place," he said.

"No more closing of stable doors, after the horse has bolted." ■



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## BIBA conference draws 400 brokers

LONDON—More than 400 brokers from England, Scotland, Wales and Northern Ireland attended the one-day British Insurance Brokers' Assn. conference last month in London.

The first speaker at the conference was the Lord Mayor of London, Sir Alan Traill, who is also chairman of Lloyd's broker Langbourn Holdings Ltd.

In his address, Sir Alan questioned the wisdom of creating financial conglomerates designed to provide "one-stop shopping" for customers.

"I question if it is right, if it will provide a real service," he told conference members.

At least seven insurance brokers rank among the largest 500 companies in Britain, according to A.V. Alexander, a director of Sedgwick Group P.L.C. who is serving as BIBA chairman this year.

BIBA members also broker some 80% of all the commercial insurance in Britain, Mr. Alexander added.

Among those attending were John Regan, chairman and chief executive of Marsh & McLennan Cos. Inc.; Lloyd's Chief Executive Ian Davison; Robin Leigh-Pemberton, governor of the Bank of England; and Lord Aldington, chairman of the Sun-Alliance Group. ■

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Index to Advertisers

Adams & Porter..... 76	Employers Reinsurance..... 18-19	Nils Publ. Co..... 66
American International Group..... 25,41	Equitable Life Assurance..... 22-23	Northwestern National Life..... 5
American Re-Insurance..... 6-7	Fidelity & Deposit of MD..... 52	Paige Ruane..... 57
American Truck Underwriters..... 64	GAB..... 21	Parker Services..... 17
Andrews Publications..... 16	Genstar Mgmt..... 9	Pinnacle..... 58
ARC Health Services..... 75	Graham Communicational..... 56	Prudential..... 31
Arkwright-Boston..... 42-43	Global Special Risks..... 64	Program Specialist..... 80
Associated Aviation Underwriters..... 54	Frank B. Hall..... 33	Professional Coverage..... 72
Assurex..... 24	Hampton Insurance..... 23	Rearick & Lenihan..... 55,57
Burns & Wilcox..... 55	John Hancock Re-Ins..... 71	Rhulen..... 73
BMS Catastrophe..... 58	Hartford Insurance Group..... 82	Schirmer Engineering..... 52
Bedford Insurance..... 72	Hartford Specialty..... 32,33,35,36	Sentry Ins..... 69
Business Insurance..... 51,65,67,71,79	Hull & Co..... 62	Southeastern Aviation Underwriters..... 63,75
Cal Group..... 69	I.I.A..... 4	Stewart Smith..... 67
Cameron & Colby..... 13	Informatics..... 10-11	Shand Morahan..... 59
Chubb Insurance..... 35	Intere Intermediaries..... 38	Swett & Crawford..... 53
CIGNA..... 47	International SOS Assistance..... 77	Structured Settlements..... 40,56
Cox Insurance..... 50	Jersey International..... 74	Transport Ins..... 68
Crawford & Co..... 50A,B,C,D	Johnson & Higgins..... 30	UAC..... 14-15
The Crump Companies..... 73,77	Liberty Mutual..... 26-27	Vision Service Plan..... 76
Cravens Darean & Co..... 40	Lockwood, Dipple & Green..... 32	Washington National Ins..... 39
Dar Allen..... 64	William H. McGee..... 36	Employers of Wausau..... 74
Delaware Valley Underwriters..... 30	Metropolitan Life..... 29,44,61	Western Employers..... 16
Dependable Ins. Co..... 63	Mutual Marine..... 20	Wetzel Co..... 50
Domain Managers Ins..... 77	Nationwide Insurance..... 12	VIP Resources..... 66
Dow Jones News/Retrieval..... 28	New York Insurance Exchange..... 20	Zurich American..... 70
DSI..... 72		

# British brokers told to invest in education for employees

By STACY SHAPIRO

LONDON—British brokerage firms should invest in training and education for their employees if the brokers want to be competitive, says David Rowland, chairman of Lloyd's of London broker Stewart Wrightson Holdings P.L.C.

Mr. Rowland says British brokers have too long lagged behind West German, Japanese and U.S. companies in investing in the education of their employees.

And, the lack of training has caused professional standards to decline at British brokerage firms, creating a huge increase in professional indemnity claims, Mr. Rowland added.

Together, these factors could force other clients to use more-educat-

ed markets, Mr. Rowland suggested.

"Because our native wit enables us to be peculiarly suited to the provision of sophisticated financial services, it should encourage us to reinforce talent with disciplined learning," Mr. Rowland told those attending the recent British Insurance Brokers Assn. conference.

"If we were organized to train ourselves, we could knock the pants off of everybody," Mr. Rowland added. "If we don't, I am afraid we will go the paths of other industries here and see our ranks diminish."

Mr. Rowland criticized the professional standards of British brokers in his speech to the BIBA conference. He said the trust among brokers, clients and underwriters has eroded in the British insurance market.

He said part of the erosion was caused by misconduct by a few senior broker officials in the 1960s and 1970s. That misconduct, he said, caused "real shock" in the market.

"If people within the market, whose very watchword is 'the utmost good faith,' can be so cynical in their manipulation for personal gain, what hope is there for the future?" Mr. Rowland asked.

Also, broker/client/underwriter trust has eroded as today's huge claims force more people to question the conduct of intermediaries in insurance and reinsurance transactions.

"We are well-aware of our vulnerability as brokers to allegations of negligence made by our clients; to the consequence of error or omission," he said.

"The very scale of underwriting losses would naturally make examination of claims a special activity," Mr. Rowland added.

He also stressed that if British brokers spent more on training and education, then they could start spending less on their errors and omissions insurance, which is rapidly growing more costly (BI, Feb. 18).

"Who at present can claim that his training expenditure equals his professional indemnity premium?" Mr. Rowland asked BIBA members.

Today, British brokers spend anywhere from 1% to 15% of their brokerage profits on E&O coverage, Mr. Rowland said. The increased cost of the coverage—which all brokers in Britain are required by law to have—arises from increased claims.

"If standards have declined, we must make every possible effort to reverse this trend. Surely it must be preferable to endeavor to reduce the cost of paying for errors by a greater commitment to producing the standards which will help to avoid them."

But, Mr. Rowland did praise the British brokers for the strides they have made in carving a niche for themselves in the world insurance market.

"We are speaking of an outstanding success story," he said. "Nationally and internationally, British insurance and British insurance brokers have established a unique position and reputation."

But, he said Britain must improve its professional standards in order to keep its share of the world market.

"We display a national weakness in this area (training)," Mr. Rowland said.

"Statistics are virtually non-existent, but there is no evidence whatsoever that the British insurance industry is showing a greater commitment to education and training than its leading international competitors."



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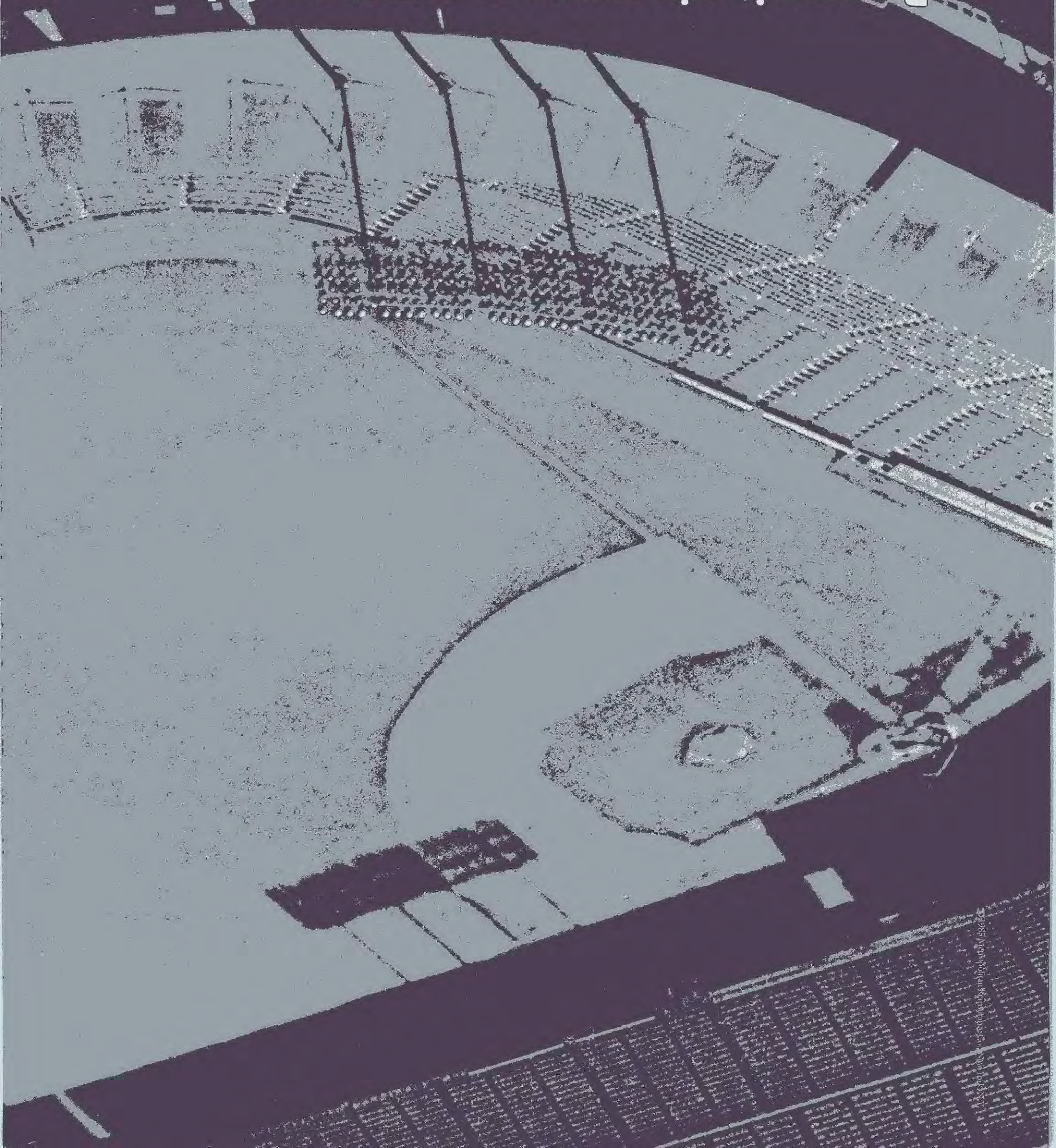
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# New U.K. rules won't cover non-life insurance

By STACY SHAPIRO

LONDON—The British government will not include non-life insurance underwriters, agents or brokers in sweeping legislation that will affect the life insurance industry, says Alex Fletcher, undersecretary of state for Trade and Industry.

Mr. Fletcher made his remarks at the recent conference of the British Insurance Brokers Assn., where many of the brokers called for the regulation of non-life insurance under the new self-regulation legislation.

"Can I first of all say that I take this as a compliment," Mr. Fletcher said. "It must be said that the usual response of an industry to government plans for regulation is a chorus of pleas for exemption. I must

say therefore that I take some pleasure in receiving pleas for the extension of the system, particularly from those who will bear the brunt of the regulation."

Non-life brokers say they want to be included under the new legislation so that all brokers are regulated similarly.

However, he said the British government will not include non-life insurance in the legislation designed to protect consumer investments. The proposal will be presented to Parliament later this year.

"Any piece of legislation must have its boundaries," Mr. Fletcher said. "The boundary to this legislation is investor protection. We are not covering the antiques or fine art markets. Similarly we are not covering gambling. This is because

although they have some features like investments, we do not consider that they are investments.

"In the same way we are not proposing to cover general insurance—although we accept all you say about its importance."

Mr. Fletcher explained to the brokers the government's position on wide-ranging changes expected to be made in the industries that invest consumer funds, including life insurance underwriters and agents.

The government's proposals were outlined earlier this year in a "white paper" called "Financial Services in the United Kingdom—A New Framework for Investor Protection."

The government already has appointed an organizing committee, called the Marketing of Investments Board, to fine-tune the de-

tails of self-regulation before legislation is submitted to Parliament. The committee is headed by Mark Weinberg, chairman of Hambro Life Assurance P.L.C., and includes BIBA Chairman A.V. Alexander.

The government's proposals have four objectives, said Mr. Fletcher: to ensure that services are supplied in the most effective way, that regulation does not stifle competition and innovation, that investors in Britain are provided with a fair marketplace and that the regulatory system can respond to all events.

Any company or agent involved in placing investments for consumers—including those in the life insurance industry—will be under the self-regulatory Marketing of Investments Board either directly

or through an approved association like the Insurance Brokers' Registration Council, the Stock Exchange or Lloyd's of London.

In the area of life insurance, the government has proposed that all commissions to brokers and managing agents involved in life insurance transactions be disclosed to the customer, Mr. Fletcher noted. Their proposal also calls for full disclosure of all other business terms and for improvements in the keeping of records and accounts.

After Mr. Fletcher's speech, many BIBA members voiced their displeasure over the disclosure of commissions and over excluding the non-life insurance industry from the self-regulation provisions of the legislation.

Mr. Fletcher stood his ground. However, he pointed out that, at least in Britain, disclosure will be under self-regulation and not under direct regulation like in other countries.

And, regarding non-life insurance regulation, Mr. Fletcher said, "It is a problem to study further, but the new act will not be involved in non-life insurance. The brokers and companies should be able to get together and set up a parallel scheme. I do think there are real opportunities for self-regulation there."

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## 401(k)s cover 20 million, study reveals

WASHINGTON—More than one out of every four U.S. employees currently is covered by a 401(k) salary reduction plan.

A recent nationwide survey found some 20 million employees out of the total private workforce of 74 million work for employers that offer a 401(k) plan.

The survey, conducted for the Employers Council on Flexible Compensation by Swinehart Consulting Inc., an Atlanta-based market research firm, also found that about 10% of companies with between one and 100 employees now offer 401(k) plans, while about 28% of employers with more than 100 workers provide the plans.

Of small companies that have 401(k) plans, some 37% reported that a 401(k) plan is the only retirement plan they provide.

And, 33% of the larger companies with the plans said 401(k)s were their sole retirement plans, the survey said.

A total of 482,280 employers offer 401(k) plans, and 130,783 companies intend to set up plans in the future, according to the study.

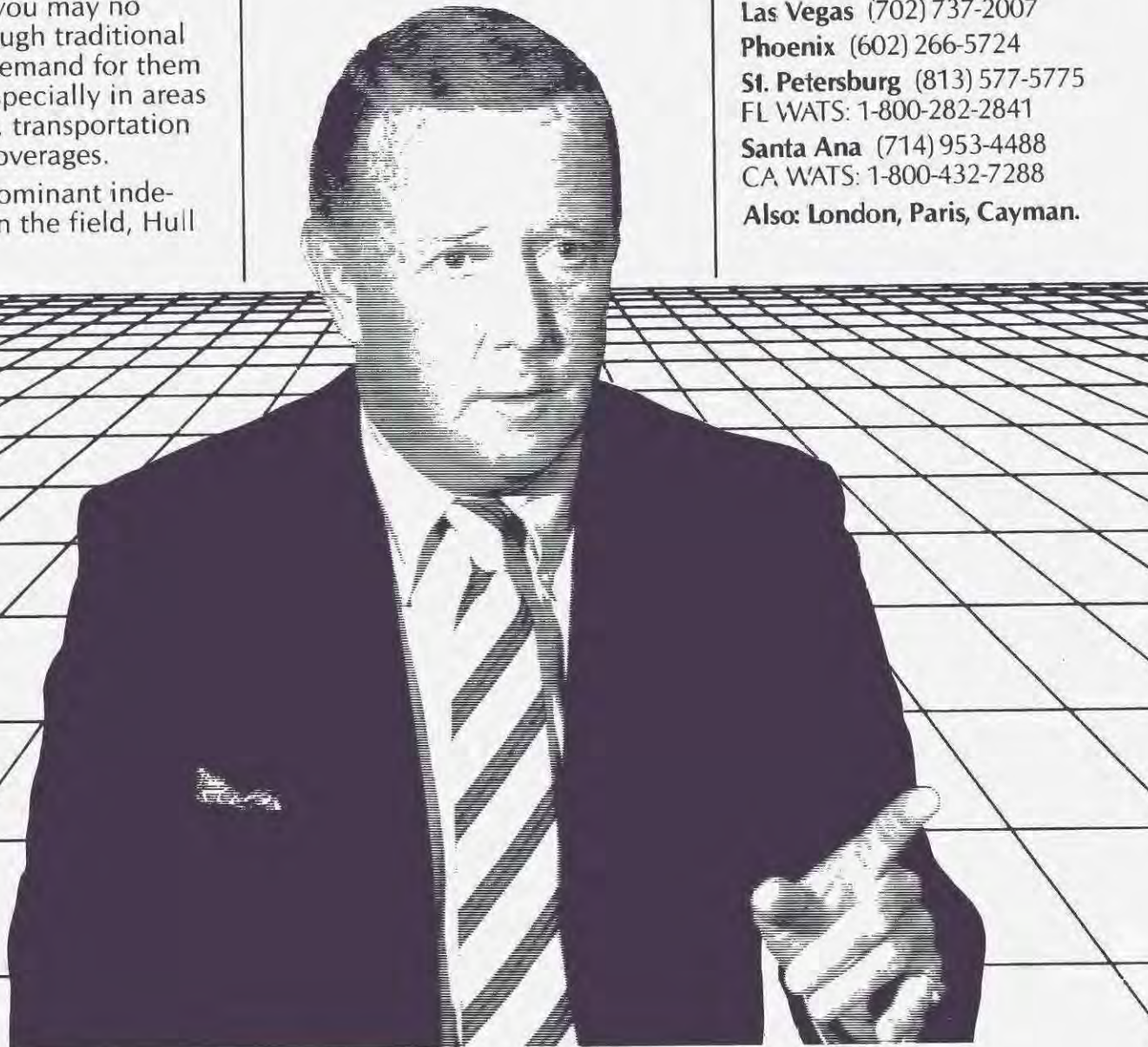
The survey, based on telephone interviews with 600 employers randomly chosen, clashes with earlier Treasury Department estimates that only 6 million employees were covered by 401(k) plans.

The Treasury estimate was based on "speculation" and "wild guesses," while the ECFC survey is the first scientific analysis of employee coverage under 401(k) plans, said William Chip, counsel for the Washington-based ECFC.

"No one has really known how many people were covered in these plans," added Ken Felton, ECFC director of government relations.

As Congress becomes aware of how many people are covered under 401(k) plans, legislators may be more reluctant to make drastic changes to the plans, he said.

Treasury last year proposed eliminating the plans as part of its tax simplification plan. A revised plan, expected this week, probably will allow the plans to continue, with restrictions (BI, April 8).



SRMC conference

# Consultants looking for ways to cope with market changes

By MEG FLETCHER

CHICAGO—The current tightening commercial insurance market is causing a cyclical seven-year "itch" that has risk management consultants scratching for alternative ways to serve clients' needs.

Mass coverage cancellations and midstream re-rating and rewriting of policies have become a recurrent problem in the insurance industry, according to Larry W. Buck of Houston-based risk management consultant Larry W. Buck & Associates Inc.

Risk managers have reacted to paying higher prices for reduced capacity and stricter terms with "disbelief and some mild chaos," said Mr. Buck, who chaired a session on the impact of changing insurance markets at the Society of Risk Management Consultants' conference earlier this month.

Risk managers are also facing two "crises" that have occurred as a result of increased use of claims-made general liability forms and the proposed elimination of sudden and accidental pollution coverage from the Insurance Services Office's new commercial general liability policies, said society President Charles T. Tagman Jr., a principal with Tillinghast, Nelson & Warren Inc. in Newton, Mass.

Public entities face special problems in the tight market, especially since some of them are legally required to seek competitive bids for insurance coverage at a time when it's difficult to find even a single bidder, one consultant attending the conference said.

The hard market has caused more corporate insurance buyers to seek help from risk management consultants, according to some of the 50 consultants who attended the daylong conference.

Buyers want help in evaluating their risks and developing alternative loss-control measures. This is especially true for less-experienced risk managers, who have only observed the soft market of the past seven years, some consultants agreed.

"It is going to be a world of managing risk, not buying insurance," one member of the audience told the group.

Managing risk requires detailed analysis of risk, including the kinds of exposures the client faces, the types of insurance it purchases and the loss-control measures it applies, consultants said.

Risk management consultants are also sought by risk managers for help in determining what insurance limits would be sufficient. Decisions on how to handle exposures must be made on a case-by-case basis, one member of the audience said.

Employers no longer have the luxury of buying affordable "sleep" insurance nor can avoid the problems posed by having lean coverage in an area where exposure exists, said Warren G. Brockmeier, vp of risk management services for The Wyatt Co. in Chicago.

Other consultants said they can suggest options to buying insurance, including self-insurance and risk-pooling devices that include association captives.

Such "group solutions" should be encouraged to answer problems that the insurance industry fails to address itself, Mr. Tagman said.

It also may be necessary to take a long-range view of the risk-control process, rather than operate on a normal 12-month cycle, another conference attendee said.

Risk management consultants can help each other by sharing in-

formation about the market for specific coverages to create a common data base. The Wyatt Co. is now considering creation of such a data base, Mr. Brockmeier said.

Information on insurance market conditions must also be shared with top management of client companies, said one member of the audience. It's important to deal with top management rather than a safety committee, which may be powerful only on paper, said Herbert H. Feldman of Herbert H. Feldman Insurance Consulting Associates in Great Neck, N.Y.

"It doesn't rain up," he noted.

Risk management consultants

also can suggest strategies to clients for coping with midterm cancellations, like lobbying for laws requiring insurers to provide earlier notice of policy cancellation or non-renewal.

Companies facing midterm cancellations may find an ally in the state insurance commissioner, who may be able to lobby the canceling insurer by using "moral sway," one consultant attending the conference said.

However, that approach may not work when midterm cancellation occurs because the insurance company has lost its reinsurance, Mr. Buck

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## Consultants' group may lobby to change licensing regulations

By MEG FLETCHER

CHICAGO—The newly formed Society of Risk Management Consultants may take action to loosen licensing regulations that hamper risk management and insurance consulting activities in some states.

The society says it may undertake lobbying efforts to change some of the state laws that restrict consultants' operations and independence.

These laws and their repercussions were discussed at the society's spring conference earlier this month.

Part of the consultants' concern stems from the fact that licensing regulations vary by state, and consultants say it is difficult to keep them straight.

According to an SRMC draft report on the problem that was presented at the conference in Chicago, 26 states require risk management and insurance consultants to be licensed.

In six of these states—Kentucky, Montana, North Dakota, Oklahoma, Vermont and Wyoming—risk management consultants cannot hold an agent's license.

On the other hand, in Alabama, Florida, Illinois, Pennsylvania, South Dakota and Texas, anyone who seeks a consulting license also must be licensed as an agent or a broker. This has caused some risk management consultants to be concerned about charges of conflict of interest.

Regulations affecting risk management consultants also can con-

tain different residency requirements.

For example, a consultant who lives in Florida must hold an agent's license. But, a person who doesn't live in Florida but holds a consulting license there does not need to be affiliated with an agency, according to consultants at the session.

And, the organization is keeping tabs on potentially precedent-setting court rulings that could affect residency requirements for consultants.

For example, elimination of Puerto Rico's residency requirement for risk management consultants was affirmed last month by the 1st U.S. Circuit Court of Appeals in Boston.

The appeals court upheld a decision by the U.S. District Court for the District of Puerto Rico that struck down the one-year resi-

dency requirement on the grounds it was a violation of constitutional rights.

The suit was filed on behalf of Leonard J. Silver and Alvin E. Mangold, both of First Risk Management Co., a consultant in Feasterville, Pa.

"In many states, there are exemptions for other professionals consulting on insurance in the course of their business activity," according to the society's draft report, which was presented at the meeting by Warren G. Brockmeier. Mr. Brockmeier is vp and head of the risk management consulting practice at The Wyatt Co. in Chicago.

The most common exemption, allowed for attorneys, has been approved in 18 states.

Also exempted from licensing requirements in some states are certi-

*Continued on next page*

### Consultants seek alternatives

*Continued from previous page*  
added.

While many risk management consultants say they expect to profit from the tightening commercial insurance market, they may have to work harder to succeed, conference participants said.

Mr. Buck said he doubled the size of his staff, which continues to work 12-hour days including Saturdays to meet clients' requests for help.

Working less—but reaping even greater benefits from the hard market—are insurance brokers, several audience members claimed.

"They are smiling all the way to the bank," said Mr. Buck. "They are certainly not doing anything to get four or five times the fee," he said.

Brokers can be put on the defensive if they are asked to provide an annual stewardship report, which describes what services the broker provided for the compensation he received, one audience member suggested.

Some risk management consultants recommended that clients consider asking to compensate brokers on a fee basis, rather than through commissions.

"These times are not good ones or easy ones," Mr. Buck said. Yet, it is a good opportunity to demonstrate to clients what risk management consultants can do, he added.

The conference was the first sponsored by the 120-member organization, which was formed in January through the consolidation of the Institute of Risk Management Consultants and the Insurance Consultants Society (BI, Feb. 18). The groups had previously been distinguished by the size of the consulting firms, with larger firms tending to be members of IRMC and smaller ones more likely to belong to ICS.

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fied public accountants, bank trust officers, licensed public adjusters, corporate risk managers, professors of insurance, chartered financial consultants and insurance agents.

Some states require that consulting licenses be held only by the individual who is doing the consulting.

However, other states require that either the individual or firm, or both, be licensed.

Some of these states require the firm to hold a license and the individual a sublicense, according to the draft report.

Licensing regulations can also be costly for consultants. Consultants who seek licenses in states other than those in which they reside often must take examinations, the cost of which can reach \$1,000, including transportation time and hotel fees, according to one consultant.

Some states will waive the exam requirement if certain qualifications—in many cases a Chartered Property & Casualty Underwriter designation—are met.

"Reciprocity exists only to a limited degree," according to the report.

Risk management consultants may also be required to post bonds or show proof of errors and omissions coverage.

In Kentucky, for instance, the law requires evidence of errors and

**'Reciprocity (in licensing) exists only to a limited degree,' according to the report.**

omissions coverage of \$50,000 or a \$10,000 bond.

Legislation affecting risk management consultants is frequently enacted in response to actions by agents or brokers who are concerned about competition from consultants or consultants' credibility.

While some attending the conference conceded that these laws sometimes are not enforced, risk management consultants do not want their livelihood affected by the restrictions.

They also fear that additional legislation will be passed if they do not lobby against these bills, according to Mr. Brockmeier.

"I think we can make a difference," he said.

The society may want to consider supporting model legislation on the licensing of risk management consultants that has been drafted by the National Assn. of Insurance Commissioners, suggested Al Waters of Waters Risk Management in Seminole, Fla.

An alternative would be for the society to draft its own version of licensing legislation to provide an acceptable guideline for state regulators, Mr. Waters added.

At the session, members also discussed ways to prevent or reduce their errors and omissions exposures.

Suggestions for office procedures that can be used to help prevent E&O losses were offered by a three-member panel consisting of First Risk Management's Mr. Silver; Bob Sterling, president of Industrial Risk Specialists in Great Neck, N.Y.; and Thomas E. Gold, executive vp of T.E. Brennan Co. in Milwaukee.

Suggestions from the panel on reducing losses include:

- Review incoming and outgoing mail and peer review of reports in an effort to eliminate or correct errors as soon as possible. An independent consultant can either periodically have correspondence reviewed by a professional or urge a secretary to question anything being typed that is not easily un-

derstood.

- Document efforts by staff members to continue their education and to keep their risk management consulting practice current.

- Offer opinions on risk management issues and contract language only when specifically asked. Urge clients to have their own attorneys review proposed contract wording.

- Provide a clear statement of the scope of any project undertaken, and document calls and contacts that are made in connection with a project.

- Provide guidelines risk managers should review to determine the risk posed by potential acquisitions of clients.

- Provide detailed bidding specifications and cite the source of information.

The society is also studying the feasibility of initiating an association-sponsored E&O coverage program to help members reduce their own insurance costs. ■



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# 'Creativity' often needed, consultants say

By MEG FLETCHER

CHICAGO—"Creative interpretation" of policy language is just one technique that can be used to reduce policyholders' losses, risk management consultants suggest.

By swapping "war stories" at the Society of Risk Management Consultants' conference earlier this month, society members were provided with a forum that allowed for a lively exchange of ideas. The discussions were in keeping with

the theme of the conference: "We can learn more from one another than we can from most outsiders," said session coordinator Herbert H. Feldman of Insurance Consulting Associates in Great Neck, N.Y.

Examples of using creative interpretations of policy language to help support clients' claims against insurers were cited by two consultants at the session.

In one case, a wine importer went to court seeking indemnification for a \$530,000 loss caused when a common table wine was substituted for a rarer vintage through a forged, French certificate of authenticity. The importer contended that his application for a letter of credit actually became a letter of credit when the forged shipping documents were attached to it.

Since those documents served as

an order to pay, the importer should be indemnified under his depositor's forgery bond, according to Leonard J. Silver, president of First Risk Management Co. in Feasterville, Pa.

In another case, a utility operating a waste-water treatment facility was sued by a neighboring small business that complained about noxious odors "trespassing" the company's boundaries onto his property, said Al Waters of Waters Risk Management in Seminole, Fla.

The utility's comprehensive general liability policy normally would not respond to the loss because it contained an exclusion for gradual pollution.

However, the unusual wording in the complaint prompted Mr. Waters to suggest the utility try to

**'We can learn more from one another than we can from most outsiders,' Mr. Feldman says.**

have at least its defense costs covered through its personal injury coverage. But, that approach was never tested in court because the utility bought the neighboring business, he said.

While risk management consultants are sometimes called upon to help think up creative defenses for clients, they also find themselves on the receiving end when insurers refuse to cover a claim, according

to some of the consultants.

Insurers have a tendency to deny claims on almost any basis, some risk consultants said. "You can make book that if you go over \$500,000 (in damages), they will trot out the lawyers," one observer said.

A policyholder's claim for flood damage was denied by its flood insurer because the water damage caused machinery to corrode and corrosion was not covered by the flood policy. The company had to sue to recover its losses, said one representative of a large consulting firm.

Another insurer denied coverage in the case of two banks that sustained a \$10 million loss in syndicated loans on leased equipment because fraudulent documents certified equipment that proved to be non-existent.

The bank had assumed its banker's blanket bond would respond to the loss, but the surety insurer denied the claim. The insurer refused to pay because the assignment from the lessor to the bank was legal, said one risk management consultant.

The case has not yet been resolved.

Although some claims cannot be settled for reasons beyond a consultant's control, there are steps that can be taken toward resolving the problem, said Mr. Silver.

In one case, a retail establishment was damaged by a fire that the local district attorney first declared as arson, but was later determined by investigators to have been accidental.

The insurer was refusing to settle even three years after the claim originally was filed because the public fire investigators' "arson" files still were open.

In anticipation of difficulty in settling with the insurer, the company filed suit against the insurer within months after the fire.

After three years passed, the company reminded the insurer that a proof-of-loss form had been sent immediately after the loss was reported and the insurer's lack of response to it signified acceptance.

The insurer, threatened with punitive damages, finally paid not only the settlement but the 9% interest required by state law from the date the proof-of-loss form was filed, Mr. Silver said.

However, insurers can justifiably deny coverage in cases where holes exist in policy language, the consultants pointed out, adding it is the consultant's job to help recommend ways to plug those holes.

In one case, a company shipped an expensive piece of equipment that later was damaged in transit. The company sustained a \$150,000 direct loss, which was reimbursed by a cargo policy.

However, six months of lost profits equaled a \$300,000 business interruption loss. When that claim was filed, it was denied because the equipment was not at the location described in the policy.

The situation could be have been prevented if blanket coverage had been obtained, the consultants said, but they conceded such coverage may not always be available.

Another risk management consultant told of an experience that taught him an important lesson.

His client, who leased a building on a harbor, sent only a portion of the policy for the risk management consultant to review. When a ship caused \$250,000 damage by ramming an adjacent dock, the consultant learned that the policy would cover replacement of the dock's support structure but not the dock itself.

As a result, that risk management consultant now asks for a complete copy of any policy a client gives him for review. ■

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## Insurers can 'make money' on EIL coverage: Scientist

By KATHRYN J. McINTYRE

SAN FRANCISCO—Pollution losses of the future are insurable, a scientist declares.

And, insurers could control their costs by settling pollution and other toxic-tort suits on a class-action basis, a plaintiffs' attorney advises.

But today, there's "quite a problem" obtaining pollution liability insurance, an executive of a waste disposal firm asserts.

These three speakers addressed the issue of "Apparent and Hidden Problems of Toxic Substances Exposures" during the annual meeting of the Alliance of American Insurers earlier this month in San Francisco.

In response, three insurance company panelists questioning the speakers expressed their concerns, and some pessimism, about what they had heard.

Insurers are not properly assessing pollution risks or properly pricing the insurance, maintained scientist Michael J. Murphy, chief operating officer of consultant Risk Sciences International in Washington.

Insurers could "make money" underwriting pollution liability insurance, he said. "The pollution exposure is insurable, but it is not being properly assessed or priced."

"There is enough science to define the degree and duration" of pollution risks, he asserted.

Mr. Murphy admitted he could not speak for insuring past pollution incidents, "but prospectively it can be evaluated," he said.

Insurers are not putting enough effort or expertise into controlling pollution exposures, Mr. Murphy continued. Too often, experienced fire prevention engineers are assigned the task of engineering for pollution, and they aren't experienced enough to handle the task.

"We do not see an adequate response," Mr. Murphy said.

"I am not indicting your industry," he stressed. But, there needs to be a "more technically competent response to pollution underwriting," he advised.

Mr. Murphy also emphasized that the issue is not only pollution caused by so-called hazardous wastes but pollution caused by all hazardous materials.

"You have clients who have hazardous materials. Whether it is hazardous waste is irrelevant," he advised the 150-person audience of insurance company chief executives and senior officers and their guests.

Dry cleaners, gas stations and hospitals all use hazardous materials, he noted.

In analyzing the exposure to liability for pollution damage, no one should assume that compliance with government regulations will exempt a company from liability, Mr. Murphy warned. "Compliance with regulations is a minimum standard."

A person holding a driver's license has met the minimum standard to drive, but that will not exempt the driver from liability if he hits a bicyclist, Mr. Murphy analogized.

Therefore, he advised insurers to "forget regulatory concerns" when analyzing pollution risks.

Plaintiffs' attorney Richard J. Lippes, a partner with the Buffalo, N.Y., firm of Allen, Lippes & Shonn, quipped:

"I expect to win big damages. It's a great time to be a plaintiffs' lawyer."

Mr. Lippes represented plaintiffs in their successful action against Occidental Chemical Corp., the successor of Hooker Chemical Co., involving the pollution damage in Love Canal, N.Y.

Insurers tend to avoid class-ac-

**Alliance**

tion suits, but class actions could reduce insurers' transaction costs, Mr. Lippes advised.

"You don't like them because they bring in more plaintiffs and more higher awards," he said. "I submit that is fallacious."

"If you had accepted a class action 15 years ago in asbestos, you'd probably be out of it for \$30 million," Mr. Lippes declared.

(Today, insurers' liability for asbestos claims is estimated at anywhere from a low of \$4 billion, to a median of \$10 billion to \$30 billion, to a high of \$135 billion, according

*Continued on next page*

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## Pollution losses

*Continued from previous page to three different studies.)*

Insurers benefit from class-action settlements because "very few people opt out of class actions," Mr. Lippes reported.

As a result, insurers will have a sense of the scope of the class of plaintiffs and they won't face a second wave of litigation on the same damages.

The ability to settle on a class-action basis is "easier and cheaper," Mr. Lippes asserted.

"This assumes a valid case" by the plaintiffs, the plaintiffs' attorney added. "If you think you will win all, go to trial," he advised.

Mr. Lippes also suggested that medical trust funds be established in settlements of toxic-tort suits to deal with plaintiffs who fear they will suffer injuries in the future caused by some event that has already occurred.

The alternative to establishing

these trust funds to cover future damages is to "wait 10 years for the person to sue."

"The medical trust fund sold the settlement in Love Canal," he reported.

The Love Canal litigation was settled for \$20 million, including \$1 million set aside in a medical trust fund.

"Most courts won't give damages for future injuries," Mr. Lippes noted, because judges don't want to create windfalls for plaintiffs who never suffer the future injury. But, "in a class action, you can set aside funds for people if they develop injuries, and it settles the cases for all time."

"I'm not suggesting that all counsel stipulate to class actions, but think about it," Mr. Lippes explained.

Mr. Lippes also commented that insurers hurt their own cause by testifying in Congress that they would withdraw from writing pollution liability insurance if a fed-

eral-cause-of-action is created.

"It doesn't do you any good to use scare tactics," he warned. "That received a bad reception in Congress."

He advised insurers, instead, to "sit down with the plaintiffs' bar and victims' committees" and "together bring a package to Congress."

He allowed, "I agree that multiple punitive damages are unfair. But I won't support that unless I get something."

Jeffrey R. Diver, vp and general counsel of Waste Management Inc. in Oak Brook, Ill., reported that corporations that handle wastes already "have a real problem" finding pollution liability insurance capacity.

And, the regulatory system does not govern all "hazardous things," while at the same time it is "vague and indefinite," he said.

As a result, Waste Management said, "Let's develop a control program to control our corporate liabil-

ities," he reported.

The company asks clients to identify exactly what wastes it is disposing of and the information is checked. "We evaluate each waste and determine how best it is handled," he said. That determination also is reviewed periodically.

The company also evaluates the socio-political implications of accepting a type of waste. There are certain wastes a company "may be crazy" to accept for these reasons.

Waste Management also requires waste generators to warrant that the description of the waste they have provided is accurate.

If it is different from the description and harm is caused, the waste generator is required by the contract to indemnify Waste Management for any damage claims paid.

Further, Waste Management will not let go of a waste until it knows where it is going and it audits the outlet.

In addition to training its personnel, Waste Management assigns a

compliance officer at each site who checks for compliance with regulations and with good sense. And, these compliance officers do not report through operations management.

A third entity audits annually for problems that may have been missed by the operations people and the compliance officers.

Waste Management does have \$10 million of liability insurance purchased from American International Group Inc., Mr. Diver later told *Business Insurance*. "It's basically a fronted program," he said.

Following the speakers' remarks, panelist Gary L. Countryman, president of Liberty Mutual Insurance Co. in Boston, suggested that the civil justice system in this country has not struck a proper balance between victims' interests and those of the waste generators or producers.

"It think they are saying fault doesn't matter. It's out of balance," he observed.

Mr. Lippes said that he agreed "the civil justice system needs some fine-tuning," but he suggested he would disagree with Mr. Countryman on how much and in what areas.

"Where an individual is exposed and injured, between the blameless person—the innocent victim—and the company that has made profits from selling a product or dumping waste, the company should pay," he asserted.

But, it is true that "there is a feeling that the insurance industry is a bottomless well. Everyone thinks insurers are making all sorts of money," Mr. Lippes said.

Insurers must inform the public and Congress that this is not true, he advised.

"We have an uninsurable risk," responded Mr. Countryman. "Without reform, there is no way it is insurable."

However, Mr. Murphy maintained his position that pollution is insurable on a prospective basis, even if joint and several liability is imposed.

He conceded, however, "I'd be scared" if he were an insurance company executive whose company had written pollution liability limits of \$30 million per occurrence and \$60 million aggregate four years ago and charged an \$18,000 premium without assessing the risk.

"That is suicide," he concluded. "Companies should not be forced to write insurance," Mr. Lippes said. "But that's a far cry from saying the victim should bear the cost."

"You can keep hitting at joint and several liability," Mr. Lippes added, but the insurers will not prevent it from being imposed on polluters.

"I agree, and that makes it uninsurable," Mr. Countryman responded.

Mr. Diver, however, was more optimistic. "We expect the insurance industry will need a period of time for insurers to feel a degree of comfort on predictability. I'm not sure predictive capability is fully there today."

While admitting "we have no grand expectation that the insurance industry will come roaring back," Mr. Diver suggested that he does think insurers may become interested in insuring pollution risks as they staff up and can better determine the predictability of pollution losses.

Andrew C. Garner, first vp-claims for Federated Mutual Insurance Co. in Owatonna, Minn., reported that his company has succeeded in reducing to \$32,000 from \$50,000 the average cost of a gasoline tank leak claim. He attributed the reduced cost to the insurance company's loss prevention program, which includes inspection of underground gasoline tanks and teaching dealers to promptly report claims.

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# Malpractice, municipal liability reform on the horizon, attorney predicts

By KATHRYN J. McINTYRE

SAN FRANCISCO—There will not be any significant tort reform enacted within the next three years, an attorney specializing in insurance law predicts.

But, there will be important reforms involving medical malpractice and municipal liability shortly, Donald J. Greene, senior partner with LeBoeuf, Lamb, Leiby & MacRae in New York, also forecasts.

Mr. Greene shared his predictions about tort reform in the United States while discussing how alien insurers will respond to U.S. insurance buyers' needs at the annual meeting of the Alliance of American Insurers held earlier this month in San Francisco.

LeBoeuf, Lamb represents Lloyd's of London in the United States.

While Mr. Greene expects sweeping tort reform efforts to fail within the next three years, there is growing public and political pressure that will force reform in medical malpractice and municipal liability, Mr. Greene observed.

Even The New York Times recently editorialized in favor of medical malpractice reform, he noted. "And if we've gone that far, it's almost certain we'll get a law."

Meanwhile, elected officials of cities and counties "will demand some kind of cap on awards against cities," Mr. Greene predicted, "because they cannot afford to raise taxes to fund the losses or to pay the premiums."

But, alien insurers will continue their withdrawal from writing U.S. risks over the next three years, Mr. Greene predicted.

The exception to this movement will be Lloyd's of London, which has increased its capital and hopes to increase it further in 1985-1986 to write profit-making business, Mr. Greene said.

Lloyds' increased capital "will help, but it will be nothing compared to the loss of capacity throughout the world," the attorney added.

Mr. Greene said alien insurers, which are insurers based in countries other than the United States, operate in the United States through four means:

- They own subsidiaries or branch offices writing direct and assumed business.
- They write direct business only as a surplus lines insurer.
- They write reinsurance only.
- The special group of captive insurers located offshore write their parent companies' business and swap business with each other.

"Although alien markets don't hold a large position, they are important because they usually support difficult lines of business—substandard, heavy casualty and reinsurance of those lines," Mr. Greene observed.

Assuming the current direct property/casualty insurance marketplace totals \$130 billion, Mr. Greene estimated alien insurers' share at around 2% to 2½%, emphasizing that these were rough estimates. The alien insurers' share of reinsurance is estimated at about \$1 billion, which may be high for this year since so many alien insurers have withdrawn from reinsuring U.S. risks.

Bermuda-based insurance com-

panies, meanwhile, took in \$6.5 billion in premiums in 1983, according to Bermuda government statistics.

But, these alien insurers "are hemorrhaging, very badly," Mr. Greene said, with their capital and surplus shrinking as they use it to pay losses incurred on policies written in prior years for which they did not adequately reserve.

Their retreat from the U.S. market, however, is "unlike any other retreat," Mr. Greene observed, because "it revolves around many apprehensions."

In addition to concern over their terrible underwriting results, alien insurers are concerned about numerous developments in the



United States, Mr. Greene said:

• Alien insurers that reinsured with U.S. reinsurers fear they may not be able to collect because some U.S. reinsurers are going into liquidation.

• Alien insurers are concerned that the Treasury Department is promoting the discounting of loss reserves for tax purposes at a time when insurers need to retain wealth within their companies to maintain solvency.

• Captive insurance companies  
*Continued on next page*

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# Malpractice, municipal liability reform predicted

Continued from previous page

are concerned the Internal Revenue Service will begin "real enforcement" of its position that captives are not insurance companies for tax purposes, which could be "a very serious blow" to them.

• Alien insurers with subsidiaries licensed in the United States are concerned about "the tendency to change the definition of covered claim under the guarantee funds."

Mr. Greene reported that there have been at least informal discussions to extend guarantee funds to cover "some pretty exotic areas," including financial guarantees.

• Alien reinsurers must fund their share of incurred but not reported losses with a letter of credit issued to a U.S. ceding company.

While Mr. Greene called the new

requirement a "healthy development," he also observed that it will add to alien reinsurers' costs and be "somewhat of a disincentive" for alien reinsurers to provide reinsurance to U.S. companies.

U.S. companies, desperate for reinsurance, may reinsure with alien reinsurers who do not fund the IBNR and take a penalty to their surplus, Mr. Greene added.

"If the market is so short, they will buy reinsurance on this basis and it will exacerbate the problem" of ceding companies' dwindling capacity, he observed.

• A.M. Best Co., which rates the financial solvency of U.S. companies, is considering whether to drop insurers' ratings to that of their largest reinsurer whenever a substantial amount of the insurer's reinsurance recoverable comes

from one or a few reinsurers with lower ratings than the ceding company.

However, Best's does not yet rate alien reinsurers, which leaves a question about how alien reinsurers will be treated.

• The stronger U.S. dollar against foreign currencies means alien insurers forced to add to the capital of their U.S. operations are paying high prices.

• The controversy over the switch to a claims-made form confuses alien insurers that don't understand why the new form is not being unanimously endorsed as necessary to control insurers' liabilities.

• The civil justice system in the United States is not understandable, and no one can predict what changes will be made in the future.

Mr. Greene criticized the erosion of two basic principles of the tort system: that there had to be fault to transfer money to a plaintiff, and that punitive damages be awarded only against those who were malicious and malevolent in consciously causing harm.

"In my judgment, neither of those principles apply in the United States anymore," he said. "The philosophy is that it is better to support the victim and to expense that through insurance."

But, while the philosophy changed, the benefits structure did not, Mr. Greene said. He recommended that wrongful death awards be capped and that vicarious punitive damages be abolished.

He also suggested that the United States might need a rule requiring that the court structure all

awards for pain and suffering and support compensation to prevent a windfall to the estates of victims and to protect victims' income.

But, while these concerns will cause alien insurers to withdraw from the U.S. market, mutual industry captive insurance companies "will thrive and will be very big," Mr. Greene predicted.

These industry captives "will be an exception to the captive dilemma," if the IRS steps up its attack on tax benefits claimed by captive insurance company owners.

If structured properly, industry-owned captives can qualify as bona fide insurers under IRS tests.

He predicted that in the long-term, there will be "an explosion of joint underwriting authorities." With tongue in cheek, he also predicted "the first will be for lawyers."

Mr. Greene noted that the tightening insurance marketplace, including the withdrawal of alien insurers, has reduced limits and raised the price of lawyers' professional liability insurance.

Leboeuf, Lamb's broker has reported that insurers are willing to write professional liability insurance for the firm of one-fifth the expiring limits at 400% of expiring premium, "but the deductible is negotiable."

"It's fortunate for us we have not had any claims," Mr. Greene added.

And, the law firm's broker says that next year the limit may be even less than offered this year.

But, in about six years, when U.S. insurers are making profits, "a new breed of manager will appear at alien insurers," he predicted.

"They will see opportunity in this great nation, interest rates will be rising, and they will come flooding back in. They'll try to take advantage of currency swings at that time. And whoops, we'll start all over again," he said.

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### Tax plan might spur rate hike: Expert

SAN FRANCISCO—If property/casualty insurers are forced to discount their loss reserves for tax purposes as the Treasury Department proposes, insurers will have to raise their prices significantly, an insurance tax expert predicts.

As a result, "large commercial clients will have a bigger incentive to self-insure," noted Dennis Van Mieghem, a partner with Peat, Marwick, Mitchell & Co. in Chicago.

The Treasury proposal would prevent insurers from setting aside tax-free reserves for the amount of the ultimate loss they expect to pay. Instead, insurers would be permitted to establish "qualified reserve accounts" by line of business, with the loss reserves discounted for the company's aftertax yield on investments.

Mr. Van Mieghem quoted A.M. Best Co. Vp Robert A. Bailey, who recently predicted that such a change in the tax law would increase insurers' taxes the equivalent of 8% of earned premiums each year.

Premium increases needed to compensate for this lost income were estimated by Mr. Bailey at 32% for medical malpractice, 24% for general liability and 15% for workers compensation.

## RBH sues A&A in California over non-compete agreement

By MEG FLETCHER

LOS ANGELES—Rollins Burdick Hunter Co. and its California subsidiary are suing fellow broker Alexander & Alexander Services Inc., charging a former RBH of California executive violated a non-compete agreement with RBH.

The RBH lawsuit, which was filed last month in Los Angeles Superior Court, follows a similar lawsuit filed last fall in Boston by A&A's Massachusetts office against RBH of Massachusetts (BI, April 22).

However, the suits differ in that RBH's California lawsuit seeks only monetary damages.

In addition to seeking monetary damages, A&A's Massachusetts subsidiary successfully obtained a preliminary injunction, later modified by an appellate court, that bars employees at RBH of Massachusetts from handling accounts of some current and former A&A clients.

RBH of Massachusetts responded to the A&A suit by filing a \$9 million countersuit, accusing A&A of violating the state's antitrust law and of "maliciously and intentionally" interfering with its contractual relationships.

**A&A will fight the lawsuit because it has a 'good and valid' defense, Mr. Gill says.**

In the West Coast suit, RBH and subsidiary Rollins Burdick Hunter of Southern California Inc. seek compensatory damages for alleged breach of agreement and fraudulent conversion as well as punitive damages.

Named as defendants are Alexander & Alexander Services Inc. and its national and California brokerage subsidiaries; A&A corporate officials; and two A&A of California employees who previously worked for RBH, Donald S. Huff and Ellsworth Jesse Royer.

According to the suit, Mr. Huff sold his business to RBH in 1976 and later became president and a member of the board of RBH of Southern California.

Mr. Huff left RBH and joined A&A in February 1985, taking with him some of the accounts that he had previously sold to RBH, in violation of a non-compete agreement signed by Mr. Huff when he sold his business to RBH, the complaint states.

The suit also alleges that Mr. Royer, who had worked at RBH with Mr. Huff, and the A&A officials assisted Mr. Huff "to achieve his unlawful and improper objectives."

Mr. Royer also left RBH and joined A&A in February, according to the suit.

RBH's suit requests compensatory damages of at least \$500,000 and punitive damages of at least \$5 million.

The suit also asks for interest, costs and the establishment of a constructive trust into which commissions and fees paid from Mr. Huff's disputed clients should be placed until the court resolves the litigation.

An RBH official cited current market conditions as the reason why it did not seek an injunction barring A&A and its employees from serving former RBH clients.

"Today, institutional buyers of insurance are facing unprecedented problems in finding necessary coverages because of dramatically shrinking capacity and

rapidly increasing premium rates," said Raymond I. Skilling, executive vp and chief counsel for Combined International Corp. in Chicago, RBH's parent company.

"Especially in this environment, unimpeded access to all available markets through all brokerage houses is vital to insurance buyers and to the public at large," Mr. Skilling explained.

A&A says it plans to "vigorously" defend the West Coast suit because it has a "good and valid" defense, according to Benjamin P. Gill Jr., vp and general counsel for Alexander & Alexander Inc. in Baltimore.

Neither Mr. Gill nor Mr. Skilling would comment on whether RBH's California suit was triggered by for the A&A suit filed in Boston.

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# Struggle to control Michigan state fund continues

By CAROL CAIN

LANSING, Mich.—The 9-year-old controversy over who is responsible for administering Michigan's workers compensation fund is surfacing once again.

Legislation intended to clearly define the state's responsibility for

administering the Accident Fund of Michigan has been introduced in the state Senate.

The issue being debated is whether the fund is an independent entity or a state agency under the aegis of the state insurance commissioner—as was suggested in an opinion issued by the state attorney general in 1976.

The fund, originally created 73 years ago to serve the residual market, now provides workers compensation insurance for more than 16,000 Michigan employers. It is the state's fourth-largest underwriter of workers compensation insurance and competes with some 253 commercial insurers.

The fund, which currently has a 3% to 4% share of the state market, had written premiums of \$25 million at year-end 1984. Administrators of the Accident Fund of Michigan and its advisory board have contended it has acted independently from the state and that the fund has been self-supporting since its inception in 1912.

However, Attorney General Frank J. Kelley issued an opinion in 1976 stating the fund is a state agency subject to control by the insurance commissioner, and that its workers should be classified as state employees. Shortly after that opinion was issued, Thomas Jones, then insurance commissioner, ordered the fund to discontinue its supplemental pension plan and turn over its assets to the state.

The two sides have filed several lawsuits in both state and federal courts in the dispute over control of the fund (*BI*, Feb. 6, 1984).

Sen. Rudy Nichols, R-Waterford, recently introduced two bills similar to legislation he introduced last year that cleared the Senate but died in the House Insurance Com-

**Fund manager Floyd Luginbill said state control of the fund would pose a conflict of interest.**

mittee at the end of the legislative session.

One of this year's measures, S.B. 297, is designed to amend existing statutes to make it clear that the fund is an independent entity.

The other bill—S.B. 298—would repeal a requirement that the fund administer the state's self-insured workers compensation plan.

The bills, which were introduced May 15, have been assigned to the Senate Labor Committee and are awaiting hearings.

"The conflict centers around a difference in philosophy between the state government and us (legislators)," Sen. Nichols said. "The state claims it has a responsibility to use the fund as a competitive tool, but the government can't be in the insurance business while promoting free enterprise and a healthy business climate in the state."

Floyd Luginbill, manager of the fund, emphasized that state control of the fund would pose a conflict of interest. "The commissioner of insurance can't serve as a competitor and regulator simultaneously. We can't serve the best interests of our policyholders and injured workers if we must bend to the will of the

state."

To make its stance on the issue known, the fund's advisory board in March hired an outside marketing and communications firm—Stone, August & Co. of Birmingham, Mich., which has designed a packet of information and full-page newspaper ads relating to the controversy.

Meanwhile, an Ingham County Circuit Court judge recently refused to grant a motion for summary judgment in a lawsuit filed last summer by the Attorney General's office on behalf of the state against the accident fund's advisory board.

That suit, which seeks to establish the fund as a state agency, charges that the advisory board is interfering with the statutory responsibilities of the insurance commissioner and other state officials over the fund.

Ingham County Judge Carolyn Stell noted, however, in her opinion May 14 that the insurance commissioner has certain administrative authority over the fund as stipulated in statutes.

Responses to this ruling are expected to be filed soon.

Insurance Commissioner Nancy Baerwaldt was unsure last week what the state's next step would be. "The (judge's) opinion is so new and the timeline is so fresh," she noted.

Meanwhile, a consent order issued last July 24 by Judge Stell that said the advisory board is responsible for the fund's operations is still in effect.

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## Murder charge dismissed

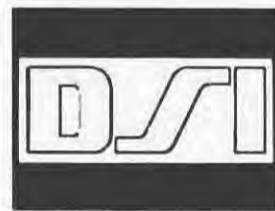
MAYWOOD, Ill.—The former vp of a defunct suburban Chicago corporation no longer is facing murder and reckless conduct charges, but three other company administrators are still on trial for an employee's work-related death.

A Cook County circuit judge dismissed criminal charges against Gerald Pett, vp and manager of Film Recovery Systems Inc. on May 14, when the prosecution rested its case. At that time, defense attorneys had routinely filed motions for a directed verdict for all

four defendants.

But Judge Ronald J.P. Banks, without elaborating, only dismissed the charges against Mr. Pett, who was described by his attorney as the national sales coordinator for FRS. The defunct corporation, as well as its marketing company, Metallic Marketing, also are on trial on charges of involuntary manslaughter (*BI*, April 22).

The case involves a 61-year-old FRS employee whose death in February 1983 allegedly was caused by cyanide poisoning.



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# Doyle named president of Cameron & Colby

**Lawrence S. Doyle**, vp and director of The Hartford Insurance Group's international property/casualty operations, has been named president and chief operating officer of Cameron & Colby, the Boston-based underwriting management affiliate.

Mr. Doyle succeeds **Chester A. Abbey**, who has been named vice chairman of Cameron & Colby and the companies that it manages, including First State Insurance Co.

Mr. Doyle retains his duties as general manager of the company's European casualty operations and as president of Hartford Fire International Ltd., Hartford's international property/casualty and reinsurance subsidiary established in October 1984.

#### Other excess/surplus changes:

**Landon V. Alexander** named vp in charge of the excess and specialty lines program at United States Fidelity & Guaranty Insurance Co. in Baltimore. He had been senior vp in charge of marketing at Cravens, Dargan & Co.

**Ray Barnes** joined Sherwood Insurance Services Inc. in San Francisco as vp-casualty.

**Swett & Crawford Group** in Los Angeles has made the following appointments: **James A. Bradley** named executive vp; **Everett J. Souza** named senior vp and chief financial officer.

**B. Thomas Johns** named vp in charge of the excess and surplus lines casualty department at Industrial Underwriters Inc., an affiliate of Industrial Indemnity Co. in San Francisco. He joined IUI in 1984.

**Troy Duane Law** named senior vp at Crump London Underwriters, a unit of The Crump Cos. Inc. Mr. Law, head of the Memphis, Tenn.-based excess and specialty lines insurance brokerage, joined Crump in 1969.

**Sanford Dorf** promoted to senior vp and director of operations, at Professional Underwriters Insurance Agency Inc., a managing general agency and excess/surplus lines broker. He will handle all operations at the company's Miami and Orlando, Fla., offices.

**Arthur E. Judson** named executive vp for Stewart Smith Mid America Inc. in Chicago. He joined Stewart Smith Michigan Inc. in Detroit in 1982, and most recently was vp and director.

**John George** named vp at Castle Underwriters Inc. in Morristown, N.J., a unit of Warwick Group. Mr. George previously was the company's general manager.

**Michael L. Pautler** named vp at Guaranty National Insurance Co. in Englewood, Colo. Mr. Pautler joined Guaranty National in 1981.

**Glenda Matthews** named vp-casualty department at RISC Inc., underwriting managers and specialty brokers, in Dallas. Ms. Matthews, who joined the firm in 1975, had been assistant vp.

#### Insurers

**Donald J. Birmingham** named president of American Continental Insurance Co. in Kansas City, Mo. He joined the company in 1980 and had been senior vp.

**Marc Darby** named district manager at Protection Mutual Insurance Co. in Montreal. Mr. Darby previously served as risk and insurance manager for Montreal-based Steamship Lines Inc. and was president of the Risk & Insurance Management Society during 1983-84.

**John B. Fitzgerald Jr.** named

## comings & goings: industry

president of CIGNA Bond Services Inc., a unit of CIGNA Corp. in Philadelphia. Mr. Fitzgerald most recently served as vp of INA Reinsurance Co., another CIGNA unit.

**Gordon H. Howie** named regional vp of the Westchester Fire Insurance Co. in Denver, a unit of Crum & Forster's U.S. Insurance Group. Mr. Howie most recently served as division manager at SAFECO Insurance Co.



Mr. Howie

**Donald C. Kintzing** joins Reliance Insurance Co. as regional vp in charge of the Northeast Region. He'll work in Reliance's Northeast Service Center in King of Prussia, Pa. He had been senior vp at Marketpac International, a marketing unit of American International Group Inc.

**Rose E. Frattali** elected chief executive officer of Watertown, N.Y.-based New York Casualty Insurance Co., a unit of Phoenix Mutual Life Insurance Co. Ms. Frattali, co-founder of New York Casualty, has been president since 1984.

**Bradford W. Mitchell** elected chairman of the board and chief executive officer of The Harleysville Insurance Cos. in Harleysville, Pa. Mr. Mitchell also will continue as president and chief executive officer of parent company Harleysville Mutual Insurance Co., and chief executive officer of its subsidiaries. He joined the company as president in 1976. Also, **John J. Keenan** elected president and chief operating officer at Harleysville Life Insurance Co.

Three senior vps have been promoted at The Travelers Corp. in Hartford, Conn., and will serve in the corporation's new National Accounts Group. Promoted to senior vp were **Christian T. Paul**, who will supervise employee benefits products and the supporting customer service activities; **Thomas E. Keating**, who will head group pension business; and **Charles J.**

**Clarke**, who will head the group's property-casualty business.

**Peter B. Hawes** named chief executive officer of Monterey, Calif.-based Design Professionals Financial Corp. and its principal subsidiary, Design Professionals Insurance Co. Mr. Hawes, who joined DPIC in 1982, has served as president of both DPIC and DPFC since 1984. Also, **Lee E. Redding** named vp and chief underwriting officer at Design Professionals. Mr. Redding most recently served as vp-casualty underwriting at Baccala & Shoop Insurance Services in Columbus, Ohio.



Mr. Hawes

**Patrick D. Burns** named president and chief executive officer of Confederation Life Insurance Co. in Toronto. Mr. Burns, who has served as Confederation Life's president since 1982, succeeds **John A. Rhind** as chief executive officer. Mr. Rhind will continue as chairman the board.

#### Reinsurance

**James E. Roberts** and **David C. Smith** have been promoted to senior vps at North Star Reinsurance Corp. in Stamford, Conn. Mr. Roberts joined North Star Re in 1979 and most recently served as vp. Mr. Smith joined the company in 1982 and most recently was vp.

**Dennis Corby** joins G.L. Hodson & Son Inc.'s Los Angeles office as vp.

#### Other suppliers

**Steve R. Webber** named principal consultant at Risk Analysis & Management Corp. in Atlanta. Mr. Webber, who joined the company in January, previously was director of risk management for Jefferson County in Birmingham, Ala.

**Warren J. Winer** promoted to president and chief operating offi-

cer at Powers, Carpenter & Hall in St. Louis, an employee benefit consulting subsidiary of Corroon & Black Corp. Mr. Winer joined PCH in 1980 and most recently was se-

nior vp and director of its pension division. Also at PCH, **Robert W. Powers** named chairman. Mr. Powers, founder of PCH, will continue as chief executive officer. ■

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# Lloyd's chairman to pay visit to United States this week

By STACY SHAPIRO

LONDON—Lloyd's of London Chairman Peter Miller will visit the United States this week.

On Wednesday, Mr. Miller will address the National Assn. of Insurance Brokers conference in Sea Island, Ga. On June 4, he will speak to the American Assn. of Managing General Agents in San Francisco. And, on June 10, he will address the National Assn. of Insurance Commissioners in Kansas City, Mo.

Mr. Miller also will visit Kentucky, where he will be honored at a dinner given by Gov. Martha Layne Collins.

And, the Lloyd's chairman will visit Houston, where he will host a reception and meet with representatives of the National Aeronautics & Space Administration.

### Howden changes

Alexander Howden Group P.L.C. has spun off its well-known jewelers block and bullion division to form a separate Lloyd's insurance brokerage called Halford Shead & Co. Ltd.

The company will be managed by co-chairmen John Evans and Brian Hough.

Also, a new Howden subsidiary will provide engineering advice to brokers, insurers and risk managers, particularly in the oil and energy fields in the United States.

Independent Engineering Service Ltd. will provide risk analysis and loss control studies of property risks, a Howden spokesman said.

### london line

The new company is headed by Chairman John Thorpe, who established the oil and risk control division of Lloyd's broker Sedgwick Ltd. before joining Howden.

### Sturge may list stock

Lloyd's of London underwriting agency Sturge Holdings P.L.C. is preparing to be listed on the London Stock Exchange.

Sturge has received permission from Lloyd's to list the company after Sturge amended its articles of association. Under the amendment, the Committee of Lloyd's must approve those holding more than 10% of Sturge's stock.

Sturge also wants to increase its authorized share capital to 7.25 million pounds (\$9.4 million) from 5 million pounds (\$6.5 million) and the issued share capital to 5.51 million pounds (\$7.1 million) from 3.74 million pounds (\$4.8 million).

### Lloyd's visits China

Lloyd's of London Chairman Peter Miller says a delegation from Lloyd's had "fruitful discussions" with Chinese officials during a recent visit to China.

"The object was to get business," Mr. Miller said of the April 18-May 2 trip made at the invitation of the state-owned People's Insurance Co. of China. "The discussions were fruitful."

For example, talks were held on changes that the PICC has requested in the wording of London's hull and cargo war risk clauses. The changes would allow Lloyd's and London underwriters to write some of the \$70 million to \$100 million of premium Chinese hull and cargo risks produce, Mr. Miller said.

Also, Lloyd's wants to write reinsurance on Chinese risks, Mr. Miller said. "The new wealth the Chinese are creating will need to be insured and reinsured," he said.

Also, Lloyd's has offered nine scholarships over the next three years to their PICC colleagues to study in London for eight months.

Already, Lloyd's brokers are making strides into China: Sedgwick Ltd. was appointed by the PICC as its adviser and leading reinsurance broker for coverage for a nuclear power station project at Daya Bay in Guangdong Province.

The construction of China's first commercial-scale nuclear power station will cost about \$3.5 billion, said David Brewer, a director of Sedgwick Ltd. and one of the members of Lloyd's delegation to China.

Discussions of project coverage are in the early stages, Mr. Brewer said.

### Tax appeal

Lloyd's of London underwriting members are waiting for hearings on their appeals of tax reassessments made by the Inland Revenue for the 1976 account year.

The Inland Revenue advised members last year that some reinsurance payments on 1976 accounts were not considered reinsurance by the tax agency and therefore were not deductible. The members considered the "rollover" transactions as catastrophe reinsurance, but the Inland Revenue contends they are transfers of syndicate reserves to offshore funds.

This decision followed a two-year investigation of Lloyd's by a special Inland Revenue team.

Members have been asked to pay from 70 pounds to 80 pounds (\$90 to \$103) up to 2,000 pounds (\$2,580) in extra taxes, said a member of the Assn. of Lloyd's Members. "They are not enormous, but there may be a flock of assessments next year for the year 1977," he said.

Lloyd's underwriting agents are recommending that the members appeal the assessments, he said. In fact, a group of underwriting agents—including Sturge Holdings P.L.C. and Merrett Holdings P.L.C.—has been formed by Peter Daniels, managing director of Lambery Underwriting Agencies Ltd., to gather professional advice.

### New look for magazine

Lloyd's Log, the international magazine of Lloyd's of London, has had a face lift.

The bi-monthly magazine now will cover issues that affect the market, rather than internal workings of Lloyd's. For example, the current issue focuses on China.

An editorial in Lloyd's Log asks, "Why are we relaunching Lloyd's Log? The answer lies in the changing nature of Lloyd's itself. Lloyd's in the 1980s touches on the daily life of businesses and individuals all over the globe to an unprecedented degree."

A new monthly Lloyd's of London Newsletter will cover news and events about workings in the marketplace.

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## Ohio lawsuit

Continued from page 2

than through the workers compensation system, because the statute of limitations for filing a work comp claim had expired, Mr. Moore's clerk said.

Workers compensation claims in Ohio must be filed within two years of the date of injury. Occupational disease claims must be filed within two years of the date the disease was contracted or within six months after diagnosis of the disease.

Celanese's Hilliard plant began operations in 1968 and closed in 1981.

Celanese is headquartered in New York and manufactures and sells a diverse line of chemicals, fibers and specialty products throughout the world.

The company has 60 plants, with some 31,000 employees in the United States and 14 other countries. The company was incorporated in 1918, and it had annual

sales of \$3.3 billion at year-end 1984.

In addition to Celanese Corp., two of its subsidiaries—Celanese Piping System Division and Celanese Plastic Co.—are named as defendants, along with Harry Holthausen, who was plant manager at the Hilliard facility.

Other defendants, which the lawsuit alleges supplied PVC and other chemicals to Celanese, include Monsanto Co. of St. Louis; BFGoodrich Co. of Akron, Ohio; Union Carbide Corp. of Danbury, Conn.; Uniroyal Inc. of Middletown, Conn.; Dow Chemical Co. of Midland, Mich.; E.I. DuPont de Nemours & Co. Inc. of Wilmington, Del.; Chevron Corp. of San Francisco; Eastern Chemical Products Inc.; Shell Chemical Co.; and Compre.

Another lawsuit on behalf of 10 to 20 former employees who allegedly died from exposure to PVC and VCMs was expected to be filed by this week, Mr. Moore's clerk

said.

That wrongful death case, against the same defendants, was expected to seek between \$250 million and \$500 million in damages, he said.

Celanese Corp. had \$250 million in umbrella liability coverage in 1981, the year the Hilliard plant closed, according to Rosalind A. Miller, Celanese's assistant risk manager. This coverage was part of a blanket program for Celanese's domestic operations, Ms. Miller said.

She would not identify the companies that wrote the coverage.

In the early 1970s, the corporation's primary general liability coverage was underwritten by Commercial Union Insurance Co. of Boston. The Commercial Union coverage had an aggregate limit of \$1 million and no deductible, according to Ms. Miller.

In the mid-1970s, the primary policy was written by The Home Insurance Co. of New York. The

Home policy had the same limits and also had no deductibles. And, from the late 1970s until the Hilliard plant closed in 1981, the primary coverage was written by Northwestern National Insurance Co. of Milwaukee, she said. It also had \$1 million limit and no deductibles.

The corporation's umbrella coverage had limits of \$50 million in the mid-1960s, but gradually was increased to \$250 million by 1981, Ms. Miller said.

"As the market capacity increased, we increased our limits."

Ms. Miller says its current limits are less than \$250 million, but would not comment further.

For its workers compensation program, Celanese purchased coverage from the Ohio State Insurance Fund, a monopolistic state fund, until June 1, 1978. After that date, the corporation self-insured its workers compensation program in Ohio.

Many employers throughout

Ohio were unaware of the billion-dollar lawsuit when contacted by *Business Insurance*. However, many said it seems that just about every employer is facing a Blankenship-type lawsuit.

One plaintiff's attorney, however, said employers shouldn't be overly concerned because cases in which intentional injury on the part of employers can be proved should be rare.

"I believe that the business community is unreasonably concerned about the Blankenship case. That case in its essence held that an employer cannot intentionally injure an employee and at the same time have the benefits of the workers compensation defense," said Jim Murray, a Sandusky, Ohio, attorney who is co-counsel for plaintiffs in the suits against Celanese.

"Hopefully, there will not be that many cases in which there will be the facts to support a verdict showing intentional injury of employees," he said.

## Rescue attempt set for lost probe

Continued from page 2

Hughes has not so far filed a claim for the Syncom loss, Mr. Merrett said. "No claim has been presented," he said, although he added that Hughes did notify underwriters that the satellite is unusable in its current orbit.

The Syncom satellite is the third in a four-satellite series leased to the U.S. Navy. All the satellites were insured by Hughes two years ago through Marsh & McLennan and Bowring Space Projects in London.

Syncom III had a total of \$85 million in satellite launch coverage. The leading U.S. underwriter, Intec, underwrote about \$25 million, and London underwriters, led by Merrett and Lloyd's Ariel syndicate, insured about \$35 million. The rest was placed in other U.S. and foreign markets.

Hughes began negotiations in early May with NASA to recover the satellite, Mr. Pipkin said. He said the probe will not be returned to Earth, like the two satellites salvaged by the November shuttle crew. NASA has decided that would be too dangerous, because of the fuel Syncom uses.

Instead, the astronauts on the August mission first will maneuver the satellite into the shuttle's bay. They will then repair and redeploy it.

After the astronauts redeploy the repaired satellite, Hughes technicians will maneuver it by remote control from the earth until it is in a position where the sun can heat up the satellite's fuel, which may be frozen. Then, Hughes will try to maneuver the satellite into a proper orbit.

"As far as what Hughes can do to reorient the satellite, that is Hughes' call. We are not looking into that," Mr. Pipkin said.

NASA may charge Hughes more than \$1 million for the repair mission, Mr. Pipkin said, much less than the \$17 million to \$18 million cost of a shuttle launch.

The same mission will launch three other commercial satellites, including the fourth in the Syncom series.

Meanwhile, underwriters are still trying to sell the two satellites that were salvaged last year, Mr. Merrett said.

"Negotiations are advancing slowly (on the sale)," Mr. Merrett said, but he would not identify any potential customers for the used satellites or reveal how much they might be willing to pay.

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**Sub-total . . . . . 22,627**

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##### Commercial Consumers

**Sub-total . . . . . 24,652**

Insurance agents and brokers . . . . . 9,524  
Insurance companies . . . . . 5,867  
Financial institutions . . . . . 556  
Actuaries, attorneys, adjusters, appraisers and consultants . . . . . 3,265  
Others allied to the field . . . . . 1,143

**TOTAL . . . . . 45,007**

\* Source: Business/Occupational breakdown of qualified circulation, Nov. 5, 1984 issue, as submitted to BPA for Dec. 1984, BPA Publisher's Statement.

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## FSA's criticized

Continued from page 1  
Accounts."

Congress ordered the department to conduct the study last year and report findings by April 1. Although the report still has not been delivered to Congress, *Business Insurance* was able to obtain a draft copy of the study.

The draft already has raised a storm of controversy among those familiar with its findings.

Benefit consultants say that the study is seriously flawed and that it ignores their own findings that FSAs are actually an important health care cost-containment weapon.

"The conclusions fly in the face of common sense and the experience of our clients," said Lance Tane, manager of the flexible compensation team at The Wyatt Co. in Washington.

Employees currently are allowed to spend funds in an FSA on health expenses that are not covered under a group health insurance plan, such as premium contributions, deductibles and copayments; on vision and dental care costs; on dependent care costs; and on legal expenses.

Under a typical FSA plan, an employee will agree to have his or her pretax salary reduced by a certain amount. This salary reduction will be placed into an account and used to pay for uncovered benefit expenses; the employee is not taxed on the amount that is placed in the FSA.

In addition, some employers also make contributions to FSAs.

At the end of the year, the employee typically could cash out the balance remaining in the FSA and pay tax on that amount, or roll over the balances into a savings plan.

However, effective July 1, employees will have to forfeit balances that remain in the FSA at the end of the year. This "use it or lose it" requirement was proposed last year by the Internal Revenue Service (*BI*, May 7, 1984) and enacted by Congress when it passed the Deficit Reduction Act of 1984 (*BI*, July 2, 1984).

Employers argue that FSAs reduce health care costs, since allowing employees to pay for uncovered health care expenses with pretax dollars makes it easier for companies to convince workers to accept cost-containment features like higher deductibles and coinsurance levels.

The HHS study, however, says that FSAs boost health care expenditures and reduce federal revenues because they inflate the demand for health care services and allow uncovered benefit expenses to be paid for with pretax—instead of aftertax—dollars.

The study is based on a complex model set up by researchers and draws heavily upon a study by the Rand Corp. that found use of health care services decreases if employees pay a higher share of

the costs.

The model looks at three prototype health plans:

- The richest, Plan A, is more generous than 90% of all health plans. Plan A requires no deductible but requires 15% employee copayments, up to an out-of-pocket limit of \$150 annually.

- The average plan, known as Plan B, imposes a \$150 deductible, 15% copayments and a maximum out-of-pocket expense of \$500.

- The least generous plan, Plan C, also has a \$150 deductible and 15% coinsurance, but places no limit on the employee's out-of-pocket expense.

The HHS model also assumes that an employee who is covered under each of the three plans makes premium contributions of \$256 a year.

The study found health expenditures under all three plans rose when FSAs were established to pay uncovered medical expenses.

Health care expenditures in-

creased 4% to 5.6% when FSAs were introduced in which employees could collect unused balances at the end of the year, while expenditures rose 4.1% to 6.1% with the introduction of an FSA with a "use it or lose it" feature.

Health expenditures rise because employees are more likely to use health care services if they can spend pretax dollars to pay their share of the costs, according to the study.

"A pair of \$50 eyeglasses may, in essence, really only cost the employee \$32 if pretax dollars are used to pay for the glasses instead of aftertax dollars," a consultant explained.

Using pretax dollars is a change "equivalent to a price decrease," the study said.

The study also concluded that FSAs have a great effect on the amount of tax revenue collected by the government.

The study does not clearly state the aggregate revenue loss created

by FSAs. However, it indicates that one use of an FSA—allowing employees to pay their health care premiums on a pretax basis—could cost the federal government \$5 billion a year.

These revenue losses would result because out-of-pocket benefit expenses that had been paid by employees with aftertax dollars now would be paid with pretax dollars, thus lowering employees' taxable income, the study suggests.

Consultants generally do not dispute the accuracy of the HHS model.

But they say the model misses a fundamental point: When employers establish an FSA program, their health care plans are also changed to require more employee cost sharing, which can reduce health care expenditures.

"Introducing FSAs are a gold-plated opportunity to introduce higher deductibles and coinsurance," said William Chip, counsel for the Employers Council on

Flexible Compensation in Washington.

The study's findings "discount the historic role of FSAs in facilitating the shift to more cost sharing. If you look back at almost all FSAs, you'll find they have played a major impact in going from first-dollar coverage to more cost sharing," said Dale Gifford, a partner with benefit consultant Hewitt Associates.

"The study is looking at worst-case situations," said Edward J. Davey, vp-technical analysis at Johnson & Higgins in New York. "On the whole, when FSAs are introduced it is in conjunction with plan changes."

When employees pay a greater share of health care costs, health plan utilization decreases, Mr. Chip notes.

More health care cost sharing, which is more likely through an FSA, results in cost savings and lower group insurance premiums for employers, Mr. Chip said. ■

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- *The BI Directory* features an index of companies ranked by number of employees. Also included is a geographical index, arranged by state.

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## Defense cover

Continued from page 2

After Judge Giles' 1981 ruling, another federal district judge in Philadelphia held in *AC&S vs. Aetna Casualty & Surety Co.* that AC&S's primary insurers have an unlimited duty to defend (*BI*, Dec. 12, 1983).

The AC&S decision is currently on appeal to the 3rd U.S. Circuit Court of Appeals in Philadelphia; a decision is expected soon.

Some say that Judge Giles' most recent decision could have an impact on the 3rd Circuit's decision in the AC&S case.

In the Pittsburgh Corning case, Pittsburgh Corning and Commercial Union contended that Travelers had an unlimited and unending duty to defend under policies written between 1962 and 1966, even after the limits of the Travelers policies were exhausted.

Pittsburgh Corning said that the language in the Travelers policies regarding defense costs was ambiguous and, thus, should be interpreted in favor of the policyholder.

In addition, Pittsburgh Corning argued that, at the very least, Travelers should have to defend those lawsuits that were pending when its limits were exhausted.

But, Travelers contended that once its policy limits had been exhausted, it didn't have to continue defending Pittsburgh Corning.

In his opinion handed down earlier this month, Judge Giles said his

1981 ruling did not clarify Travelers' duty to defend nor allocate defense expenses between Travelers and Commercial Union.

"This court has not held, contrary to the contentions of Pittsburgh Corning and Commercial Union, that Travelers has an unending duty to defend," Judge Giles said.

"More specifically, there has been no determination that after the exhaustion of aggregate policy limits, Travelers has a duty to defend non-pending litigation or future claims arising from asbestos exposures which occurred during the policy period."

Judge Giles said that where aggregate limits have been exhausted, the policyholder is on notice that there is no valid and collectible insurance pertaining to new claims.

Under these circumstances, there is no continuing duty to defend, Judge Giles said.

"The insured's position that Travelers is responsible for the defense of claims arising from asbestos exposure during the period of coverage but asserted after the exhaustion of aggregate limits is untenable," Judge Giles added.

"By making this argument, the insured, Pittsburgh Corning, does not seek protection under the terms of a subsisting policy but rather seeks a continuation of policy protections simply because a policy has once been issued."

But, while the duty to defend once undertaken is independent of any subsequent obligation to

indemnify, there is a duty to defend if there is or may be a contractual obligation to indemnify, he added.

"Thus, Travelers' duty to defend extends to all claims which were in litigation at the time of exhaustion of its aggregate limits of liability," the court said.

"The costs of that defense cannot be passed onto Commercial Union under the terms of its policies since the obligation to defend pending lawsuits was part of the Travelers' insurance coverage of the insured. Travelers' duty to defend, however, does not extend beyond that point to other claims asserted against the insured."

Judge Giles added that Travelers' own internal memoranda indicate that it is reasonable to interpret the policy language as obligating Travelers to defend pending cases.

Last week, attorneys for insurers and policyholders were divided over the impact of the decision, saying that none of the parties got everything it wanted.

"Judge Giles split the baby," said one industry attorney who asked not to be identified.

However, according to one attorney, the decision is a major setback for Pittsburgh Corning.

"It is extraordinarily important," said Barry R. Ostrager, with the New York firm of Simpson Thatcher & Bartlett, which represents Travelers in the litigation with Pittsburgh Corning.

Because Travelers does not have an unending duty to defend, Pitts-

burgh Corning's excess insurers will have to defend about 15,000 pending cases filed after 1981, plus the approximately 500 a month that are still being filed against the company, he explained.

And because defense costs are included in the policy limits of many excess policies, Pittsburgh Corning's substantial costs for asbestos litigation could be expended much more quickly, he added.

Travelers also contends that under an interpretation by Judge Giles in 1981 of how Pittsburgh Corning must be defended and indemnified, it would only have to pay 5/13 of the costs for the 7,600 cases, he says.

Travelers General Counsel George McKeon said, "This certainly is a significant improvement over the interpretation widely given to Judge Giles' first decision in 1981."

However, he noted it is not in accord with Travelers' appeal in the AC&S case in which the insurer argues that duty to defend ends upon exhaustion of limits—the same argument the insurer made in the Pittsburgh Corning case.

The insurer has not yet decided if it will appeal, Mr. McKeon said. An attorney for Pittsburgh Corning added: "We are studying the opin-

ion. "No decisions have been made."

"In light of the fact that Travelers vigorously opposed the result reached by the court, I'm frankly surprised about the interpretation Travelers is now giving the result," said James J. Restivo, with the Pittsburgh law firm of Reed Smith Shaw & McClay.

"The order clearly obligates Travelers to pay all defense costs on all cases pending at the time of the exhaustion."

James Griffith, an attorney for CU with the Philadelphia firm of Griffith & Burr, also said the decision is favorable to his client.

As a result of the decision, CU will be able to recover from Travelers the money it has spent defending Pittsburgh Corning for the 7,600 cases pending in 1981, Mr. Griffith said.

As a result, CU stands to recover between \$30 million and \$55 million from Travelers, Mr. Griffith said. Attorneys for Travelers said they had not yet calculated how much money, if any, Travelers must pay to CU.

In addition to this case, Pittsburgh Corning has filed a declaratory judgment suit against Travelers on the issue of coverage; that case is still pending.

## Restraining order

Continued from page 2

Orient with an arbitration notice, the same day Ranger says it first realized reinsurance may not have been valid since Jan. 1.

A hearing is scheduled in Santa Ana tomorrow on Ranger's request for a preliminary injunction to replace the temporary restraining order. The court has rejected Orient's attempts to dissolve the temporary restraining order.

"Any agent would resent indirect methods of termination earlier than the six-month notice," says Orient's attorney, David Daar of Miller & Daar in Beverly Hills. "The issue is: Can underwriting controls be used to accomplish the termination," of the agreement.

Ranger believes Orient is complying now with the temporary re-

straining order, says Jonathan Bank, Ranger's attorney in the Los Angeles office of Buchalter, Nemer, Fields, Chrystie & Younger.

The Laguna Hills, Calif.-based MGA has said it would be put out of business if it can't write for Ranger, Ranger Vp Charles A. Taylor Jr. reveals in an affidavit.

Ranger counters that it limited Orient's underwriting and later imposed an underwriting suspension after the adequacy of reinsurance arranged by Orient was found questionable.

Orient arranged for Union Indemnity Insurance Co. of New York to reinsure risks written for Ranger from November 1983, the beginning of Ranger's MGA contract with Orient.

In November 1984, Ranger says,

Union was facing financial difficulties and was unable to increase the required letters of credit. So, Ranger limited Orient's underwriting authority in March.

Later, Mr. Taylor says in his affidavit, Union's owner, Frank B. Hall & Co. Inc., informed him May 10 that Union had terminated its participation in the reinsurance program as of Jan. 1, and that it previously notified Orient of this.

Hall announced in October Union was for sale (*BI*, Oct. 22).

"If Union is able to establish that it is no longer a reinsurer of Ranger, Ranger will be exposed to 100% of the liability under policies issued by Orient," Mr. Taylor says. He estimates Orient wrote \$9.2 million in premiums in Ranger's name from Jan. 1 through May 9.

Orient wrote liability coverage for Ranger of up to \$1 million for alarm installers, security guards and commercial truckers.

Under a quota-share reinsurance arrangement, Ranger retained 10% of these risks and ceded 90% to Union. Orient received a flat commission of 25% of net premiums written annually. Ranger received a 34% ceding commission.

In its effort to dissolve the restraining order, Orient has suggested that Remco Insurance Co., its affiliate, replace Union as Ranger's reinsurer.

But both Ranger and the Delaware Insurance Department object.

Remco President L.W.F. Cornelius in Harrisburg, Pa., told a Delaware department official May 17 that Remco would notify the department before entering any agreement to reinsure Ranger, and that no agreement would be made without Remco obtaining more reinsurance for Remco.

But the Insurance Department later learned that Remco had submitted a reinsurance treaty to Ranger May 13. A department hearing was called for last Friday for Remco to show why its certificate of authority should not be revoked.

The department contends that Remco—with a 1984 surplus of about \$2.4 million—cannot absorb reinsurance premiums of about \$9.3 million from Ranger, let alone withstand what Orient can write under contract until November.

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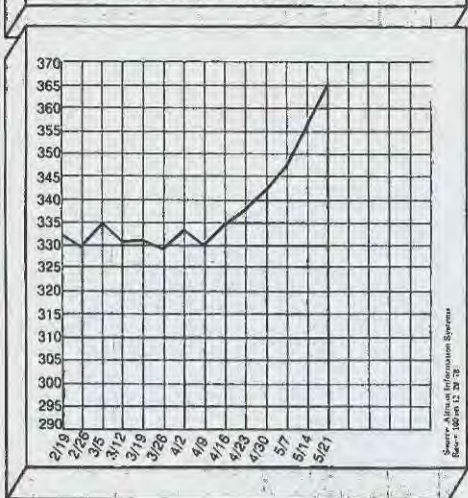
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BI Insurance Index



# Property/casualty insurers utilizing differing strategy

By MYRON M. PICOULT  
Special to Business Insurance

**T**HE MOST NOTEWORTHY trend among property/casualty insurers during the first quarter was the dichotomy in unit growth, defined as the number of policies in force. Some companies were aggressively seeking unit growth, while others continued to reduce the size of their books.

This has the earmarks of "A Tale of Two Cities," and can't be positive for both groups.

The dichotomy in unit-growth objectives is more a function of the perceptions of rate adequacy than surplus at this juncture, given the success many underwriters have had in selling stock or convertible issues plus the improvement in the bond market. The latter has apparently made some company managements feel healthier and wealthier.



Mr. Picoult

The aggressive camps articulate a continuation of the exponential rate of increase in commercial rates, albeit at a moderated pace. The more conservative cadre feels that rates are still somewhat inadequate and that a more aggressive growth posture will be warranted in the second half of 1985.

Comments from company managements during first-quarter analyst meetings indicated at the low point of the pricing cycle—about the fourth quarter of 1983—rates on "bread-and-butter standard commercial risks" were about 60% to 65% of the Insurance Services Office's manual rate.

Based on rate increases secured to date, several companies are now writing current business at a combined ratio of 107% to 110%. With investment yields hovering near the double-digit mark, underwriters are in a position to fully deduct their underwriting losses and, if they write at a 3-to-1 premium-

to-surplus ratio, they would be earning 20% on equity.

While we recognize the need for many property/casualty companies to pay the piper for past sins, pools and captives become an increasingly attractive haven for the more-mundane risks in the face of continued efforts to sustain the exponential rise in commercial rates. If enough buyers tap these risk-funding alternatives, it could quickly curtail the size of rate increases.

The strategy to keep one's powder dry until rates are more adequate is logically correct. It remains to be seen if prudence will outweigh market-share pressures. The picture of a cadre of companies at the starting gate anxious to recapture market position is somewhat reminiscent of the classic scenario of three skiers decked out in their skis and poles trying to get through a revolving door at the same time. No one gets through!

Our data base has been expanded slightly to now include 19 of the major publicly held (direct or indirect) property/casualty insurers, which account for about 47% of the total premium volume of the stock segment of the industry. As of this writing, the data was complete except for results from The Home Insurance Group. Our survey revealed for the three months ending March 31, 1985:

- Net written premiums, on average, rose 16.8% from the comparable figure the year before. Excluding Kemper Group because of a pooling change effective last July, the average gain in premiums jumped 19.1%. This was an extremely strong increase and reflective of the rise in commercial rates to date.

- Ten companies were above the average and eight were below. The sharpest increase in premium volume was achieved by CNA Insurance Cos. with a 37.8% gain. Several other companies, including American International Group Inc., Chubb Corp. and Transamerica Insurance Co. were clustered around the 30% mark. Single-digit growth was registered by American General Corp., The St. Paul Cos. and Crum & Forster Inc.

- Pretax net investment income increased 11.9%, reflective of both enhanced cash flow and continued emphasis on taxable investment instruments. Eleven underwriters were above the average and seven were below. Two companies, Hartford Insurance Group and Kemper Group, reported declines in pretax investment income for the quarter.

- The aggregate combined ratio, after policyholder dividends, actually declined to

117.3% from 118.8%, despite an 88% rise in catastrophe losses. The loss ratio deteriorated slightly to 87% to 86.3%. All of the improvement was centered in the expense ratio, reflective of the strong rate of premium growth and past and current cost-cutting measures.

Ten companies exceeded the average combined ratio and eight were below. Once again, only GEICO Corp. was able to post a combined ratio below the 100% mark, though 11 companies improved their combined ratios. Crum & Forster posted the highest combined ratio of the group.

- Statistics on premium-to-surplus and reserve-to-surplus ratios are incomplete. However, when comparing data on the 14 companies for which information is complete, the premium-to-surplus ratio edged up to 2.74-to-1 from 2.72-to-1 at the end of the year, while the reserve-to-surplus ratio receded slightly to 3.3-to-1 from 3.32-to-1.

- Aggregate loss reserves appear to have increased 12.8%, indicating that some companies are beginning to address their reserve deficiencies. We still have a long way to go on this point. Much to our surprise, paid losses were up only 2.1%.

- Finally, property/casualty earnings slipped about 4%, while consolidated results expanded almost 22%. In many instances, group results continued to be extremely strong. This will slow as the year progresses.

The bottom line to all of this is clearly that the industry's fundamentals are improving. However, we reiterate that an awful lot has been discounted in a very short period of time. Investors with meaningful gains might do well to secure some profits before making the down payment on their Rolls Royce. ■

## A&A/Reed Stenhouse

Shareholders of Alexander & Alexander Services Inc. approved the brokerage firm's proposed acquisition of Reed Stenhouse Cos. Ltd. of Toronto on May 17. Reed Stenhouse shareholders voted in favor of the acquisition on May 15.

The two international insurance brokerage firms expect to finalize the proposed acquisition sometime this summer, after regulators review and authorize the transaction.

## Emett & Chandler stock sale

Chicago-based Old Republic International Corp. sold 178,632 common shares of Emett & Chandler Cos. stock for \$16 a share on the open market in April. The shares represent 11.5% of the Los Angeles-based insurance brokerage's common stock.

## Frank B. Hall

New York-based Reliance Group Holdings Inc. has acquired 1.85 million common shares and \$25 million of subordinated debt of insurance brokerage firm Frank B. Hall & Co. at a cost of \$62 million. In addition, Reliance Chairman Saul P. Steinberg has joined Hall's board pursuant to an oral arrangement with the broker.

The transaction boosts Reliance's holdings in Hall to 20.5% from a previous 9%. Reliance Group Holdings is the parent company of Reliance Insurance Co.

## Gallagher dividend

Arthur J. Gallagher & Co. has declared a quarterly cash dividend of 7 cents per share on the company's common stock, payable July 15 to shareholders of record as of June 30.

## Crump stock split

The board of The Crump Cos. Inc. has approved a 2-1 common stock split. If approved by shareholders, the new shares will be issued to shareholders of record Sept. 30.

In addition, the Crump board declared a dividend of 11 cents per share of common stock, payable July 9 to shareholders of record June 28.

Also, Crump Chairman Sidney A. Stewart Jr. said he expects the board to increase the annualized dividend rate by 14% on the shares outstanding after the stock split. ■

Myron M. Picoult is senior vp and senior insurance analyst with Oppenheimer & Co. in New York. He is the past president of the Assn. of Insurance & Financial Analysts and a member of the New York Society of Security Analysts. His column appears the fourth Monday of every month.

### British Issues

21 May Companies	Price pence	P/E	Div. pence	Yield %	1 Week High—Low
Comm Union	224	N/M	16.9	7.5	232—218
Genl Accident	598	101.4	28.6	4.8	615—598
Gdn Royal Exch	698	20.2	37.1	5.3	715—698
Royal	633	N/M	33.9	5.3	645—630
Sun Alliance	465	22.4	21.1	4.8	480—465

Brokers	Price	P/E	Div.	Yield	1 Week High—Low
CE Heath	612	10.0	30.0	4.9	612—580
Hogg Robinson	280	16.0	11.6	4.1	289—280
JH Minet	202	13.9	8.9	4.0	218—202
Sedg Grp	380	16.7	14.3	3.8	385—380
Stew Wrightson	593	15.6	25.7	4.3	603—593
Willis Faber	683	23.4	18.6	2.7	695—673

Source: Philip Olsen/Alan Clifton, Insurance Industry Specialists Kiteat & Aitken Stockbrokers, London

# BI Industry Stock Report

May 21, 1985 5/15/85 thru 5/21/85

Brokers	Price	% Chg.	P/E	\$ Div.	% Yld.	High	Low	Vol.(000)	
Alexander & Alexander Svcs	NYSE	29.00	0.0	0.0	1.00	3.4	29.38	28.75	228.4
Baldwin & Lyons Inc	OTC	65.00	-4.4	11.8	0.80	1.2	71.00*	65.00	2.7
Corroon & Black Corp	NYSE	47.00	3.6	0.0	1.00	2.1	47.25	44.88	144.6
Crump E H Cos Inc	OTC	30.75	5.1	23.1	0.44	1.4	30.75*	29.25	26.9
Emett & Chandler Cos Inc	OTC	20.00	1.3	95.2	0.00	0.0	20.00	19.75	3.2
Gallagher Arthur J & Co	OTC	42.75	0.0	25.6	0.28	0.7	42.75	42.75	4.1
Hall Frank B & Co Inc	NYSE	26.00	2.5	0.0	1.00	3.8	26.00	25.25	316.6
Marsh & McLennan Cos Inc	NYSE	68.00	3.8	42.0	2.40	3.5	68.00*	65.25	608.6
Poe & Assoc Inc	OTC	8.00	0.0	0.0	0.00	0.0	8.00	8.00	0.5
Reed Stenhouse Cos Ltd	OTC	21.75	1.2	28.2	0.60	2.8	22.00	21.75	84.7
AGENTS/BROKERS	AVERAGE		55.5		2.1				

Conglomerates & Holding Cos.	Price	% Chg.	P/E	\$ Div.	% Yld.	High	Low	Vol.(000)	
American Express(Fireman's Fd)	NYSE	45.25	0.8	15.5	1.28	2.8	45.75*	45.25	4,602.9
Anderson (Layton/Ranger/PanAm)	NYSE	38.38	3.7	19.8	1.32	3.4	39.13	36.75	26.2
Arso Inc	NYSE	7.75	5.1	0.0	0.00	0.0	7.75	7.13	566.9
Berkley W R Co-p	OTC	15.50	0.8	0.0	0.32	2.1	15.50	15.25	25.5
CIGNA Corp	NYSE	57.13	5.8	816.1	2.60	4.6	57.13*	53.38	1,562.3
City Investing Co. (Home Ins.)	NYSE	34.50	-5.5	3.3	0.00	0.0	36.75	34.50*	1,960.9
CNA Finl Corp (CNA)	NYSE	50.50	6.3	19.4	0.00	0.0	51.13*	49.00	274.9
General Re Corp	NYSE	83.88	0.6	52.4	1.56	1.9	84.38	83.50	422.0
ITT (Hartford Group)	NYSE	34.25	1.1	10.7	1.00	2.9	34.63	34.00	3,636.1
Optimum Hldg Corp	OTC	0.50	0.0	0.0	0.00	0.0	0.50	0.50	8.9
Sears Roebuck & Co. (Allstate)	NYSE	36.50	5.0	9.1	1.76	4.8	36.50*	34.88	4,310.1
Teledyne Inc (Argonaut)	NYSE	246.75	2.2	5.3	0.00	0.0	246.75	241.25	228.1
Transamerica Corp (Occidental & Fred S. James)	NYSE	30.75	2.1	15.1	1.64	5.3	30.88*	30.25	627.1
CONGLOMERATES/HOLDING COS.	AVERAGE		10.4		1.7				

Insurers	Price	% Chg.	P/E	\$ Div.	% Yld.	High	Low	Vol.(000)	
Aetna Life & Cas Co	NYSE	45.88	2.2	23.3	2.64	5.8	46.00*	45.13	1,575.5
American General Corp	NYSE	34.88	5.7	11.3	1.00	2.9	35.25*	33.13	2,088.5
Ameri Heritage Life Invst Co	NYSE	30.63	-2.4	9.2	1.20	3.9	31.25	30.63	3.1
American Indty Finl Corp	OTC	20.75	6.4	0.0	1.12	5.4	20.75*	19.88	28.7
American Intl Group Inc	NYSE	85.88	1.3	25.4	0.44	0.5	87.13*	83.00	556.2
Aneco Reins Ltd	OTC	1.50	0.0	0.0	0.00	0.0	1.50	1.50	1.6

Price	% Chg.	P/E	\$ Div.	% Yld.	High	Low	Vol.(000)		
Avecco Corp	NYSE	28.25	-0.9	13.1	0.60	2.1	28.75*	28.25	15.9
Business Mens Assurn Co Amer	OTC	54.25	0.5	7.5	2.08	3.8	54.25	53.75	98.9
Chubb Corp	NYSE	68.88	-2.3	17.3	2.20	3.2	70.25	68.88	223.8
Combined Intl Corp	NYSE	47.88	-0.3	9.3	2.16	4.5	48.50*	47.25	108.5
Continental Corp	NYSE	47.38	6.5	24.2	2.60	5.5	47.50*	45.63	641.5
Crown Life Ins Co	OTC	137.00	0.4	8.3	5.00	3.6	137.00	137.00	0.5
Durham Corp	OTC	40.25	1.9	7.8	1.28	3.2	40.50	39.50	26.2
Farmers Group Inc	OTC	65.25	2.4	11.9	1.76	2.7	65.50*	64.38	672.9
Freemont Gen Corp	OTC	29.00	0.0	0.0	0.48	1.7	29.25	29.00	119.2
Great West Life Assurn Co	OTC	366.00	0.0	9.4	14.00	3.8	366.00	366.00	0.5
Hanover Ins Co	OTC	42.50	5.3	72.0	0.56	1.3	43.00*	41.00	190.6
Hartford Steam Boiler Inspntr	OTC	44.50	1.7	39.7	1.50	3.4	44.50*	43.75	38.5
Kans City Life Ins	OTC	77.00	-0.6	8.8	2.88	3.7	77.00	76.00	9.2
Kemper Corp	OTC	60.38	6.6	35.1	1.80	3.0	60.50*	56.88	245.5
Liberty Corp S C	NYSE	30.88	2.1	14.4	0.72	2.3	30.88	30.00	9.7
Lincoln Natl Corp Ind	NYSE	45.38	7.7	11.9	1.84	4.1	45.75*	42.13	407.0
Mission Ins Group Inc	NYSE	8.13	-1.5	0.0	0.00	0.0	8.38	8.13	120.5
Monumental Corp	OTC	32.50	2.4	23.9	1.30	4.0	32.50*	31.75	15.9
Northwestern Natl Life Ins	OTC	31.00	-4.2	7.4	0.80	2.6	32.50	30.88	334.3
Ohio Cas Corp	OTC	60.50	1.7	22.4	2.80	4.6	61.25*	58.88	145.4
Old Rep Intl Corp	OTC	33.25	4.2	8.0	0.74	2.2	33.38*	31.75	117.7
Orion Cap Corp	NYSE	25.75	4.0	0.0	0.76	3.0	25.75*	24.38	101.2
Protective Corp	OTC	23.00	-1.1	7.8	0.66	2.9	23.00	23.00	248.9
Provident Life & Acc Ins Co	OTC	25.00	0.0	6.8	0.88	3.5	25.00	24.75	365.8
St Paul Cos Inc	OTC	69.00	-1.6	0.0	3.00	4.3	70.13	69.00	475.7
SAFECO Corp	OTC	43.25	2.1	15.4	1.60	3.7	43.63*	42.13	414.3
Sri Corp	OTC	18.88	6.3	32.0	0.68	3.6	18.88	18.00	230.8
Seibels Bruce Group Inc	OTC	21.88	1.7	0.0	0.80	3.7	21.88	21.50	157.3
Statesman Group Inc	OTC	5.50	-2.2	0.0	0.15	2.7	5.88	5.50	48.9
Tokio Marine & Fire Ins Co	OTC	177.00	5.3	30.6	0.00	0.0	177.00	166.00	7.5
Torchmark Corp	NYSE	51.63	1.0	11.4	1.00	1.9	51.63*	50.75	366.9
Travelers Corp	NYSE	47.88	4.1	11.6	2.04	4.3	48.00*	46.50	1,096.5
United Fire & Cas Co	OTC	22.00	0.0	0.0	0.80	3.6	22.00	22.00	0.1
United States Fid & Gty Co	NYSE	36.50	4.7	39.2	2.20	6.0	37.25*	36.13	1,318.6
USLife Corp	NYSE	39.50	0.6	9.0	1.04	2.6	40.00	39.00	252.7
Washington Natl Corp	NYSE	26.63	1.4	7.8	1.08	4.1	26.63	25.75	73.3
Zenith Natl Ins Corp	OTC	14.50	3.6	0.0	0.68	4.7	14.50	14.00	22.8
INSURANCE COMPANIES	AVERAGE		16.4		3.2				

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