

Business Insurance

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\$4

Equitime risk retention group to cover war risk liabilities

Airline RRG seeking clearance for takeoff

By Douglas M. Green

WASHINGTON—United States airlines are a step closer to forming their own and terror liability risk after applying last week to the Federal Reserve, a Vermont-based risk retention group that the airlines plan to capitalize with \$50 million.

Equitime would provide up to \$2 billion in war risk limits, which includes coverage for terrorism losses, at a fraction of the cost of the same coverage in the commercial insurance market, according to airline representa-

tives who contend the traditional market options are unaffordable.

A key hurdle for the RRG, though, will be securing reinsurance: Equitime plans to retain \$300 million of its limit and reinsure the balance with the federal government, which began covering airlines' war risks soon after Sept. 11.

The Department of Transportation, while expressing support for the RRG concept, has emphasized its desire to exit the war risk insurance business and has not yet decided whether it will reinsure Equitime.

Some market participants—notably Ameri-

See **EQUITIME**/ page 30

9/11 losses raise costs, awareness of group life risk

By MICHAEL PRINCE

Corporate benefit managers should brace for higher rates and potential coverage restrictions for their group life insurance programs.

In the wake of last September's terrorist attacks, group life insurers are facing sharply higher reinsurance costs, reduced capacity for catastrophe exposures and exclusions of terrorism risks. While insurers generally have not yet factored these costs into their pricing, they are asking employers to provide more information on covered lives and making changes in underwriting. And higher rates likely are not far off, brokers and insurers say.

"This is the first significant cat exposure the life insurance market has ever experienced," said Nicholas von Moltke, senior vp at Employers Reinsurance Corp. in Overland Park.

See **LIFE RE**/page 27

Fear of claims battles spurs D&O changes

By ROBERTO CENICEROS

Risk managers increasingly are being asked to assure corporate officials that directors and officers liability insurance policies will pay to defend them from shareholder lawsuits if the company also is in bankruptcy.

Their fear is that some bankruptcy courts may freeze D&O coverage as an asset of an insolvent company and refuse to release policy proceeds to cover defense costs. As a consequence, risk managers are exploring ways to revise insurance programs or alter policy wording so that coverage clearly protects corporate officials.

This heightened concern arises because Enron Corp. directors and officers initially were impeded by bankruptcy proceedings from tapping D&O policies to cover legal costs arising from shareholder litigation. In April, nearly four months after they first requested coverage of their legal costs (*BI*, Jan. 28), a bankruptcy judge agreed to allow some of the D&O policy proceeds to flow to lawyers representing Enron's directors.

Delaying the claim was the judge's consideration of shareholder arguments that entity coverage provided under Enron's D&O policy preclud-

ed any money from flowing to the directors, because such a disbursement would reduce corporate assets.

"Enron highlighted for board members the potential for them to be naked, and that has stirred up a lot of anxiety," said Tony Galban, vp and D&O underwriting manager for Chubb Specialty Insurance in Simsbury, Conn.

Risk managers are taking steps to assure, as much as possible, that there is no risk in bankruptcy proceedings that D&O coverage would not be available to directors and officers.

This situation would be particularly troublesome for directors of bankrupt companies, occurring just when they are at greatest risk of being sued for corporate losses stemming from alleged mismanagement.

The possible remedies available to policyholders include reshaping their insurance programs or including D&O policy language that specifically addresses bankruptcy, say insurers, brokers and policyholder attorneys.

The goal is to insulate coverage limits intended for individual officers and directors under a D&O policy from other limits typically contained in

See **D&O**/page 30

Late News

ERISA group blasts OIG release of information

The ERISA Industry Committee is asking Labor Secretary Elaine Chao to investigate what it says



Ms. Chao

was the improper release of confidential employer information by the department's Office of Inspector General.

Recently, Rep. Bernard Sanders, I-Vt., released the names of 13 employers that participated in an OIG audit of 60 cash balance pension plans, citing the OIG as his source. The audit report said that the companies improperly denied millions of dollars in benefits to cash balance plan participants who terminated employment before retirement. The OIG had promised employers participating in the audit that information they provided would be kept confidential.

Senate passes COBRA subsidy provision

The Senate last week passed and sent to a congressional conference committee trade legislation that includes a new federal COBRA health care subsidy provision. Under the legislation, H.R. 3009, employees who lost their jobs due to foreign competition would have to pay only 30% of their COBRA premiums, while the federal government would cover the cost of the remaining 70% of the premiums. Currently, a beneficiary must pay the entire COBRA premium, which is 102% of the group rate. Employers would front the 70% federal subsidy. The legislation, to the concern of business groups, directs the Treasury Department to work out the details on how to reimburse employers.

Panel repeats call for terrorism coverage

The congressional Joint Economic Committee is calling again for a limited federal role in guaranteeing terrorism insurance. In a second report on terror coverage since April, "Economic Perspectives on Terrorism Insurance," the committee

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Spotlight

RISK FINANCING OPTIONS

Begins on page 10



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NEWSPAPER

Inside

IRS rulings clarify auto enrollment

Resolution of tax questions on contributions welcomed by employers. **Page 4**

Government can't eliminate all risk

No one can say for sure that Sept. 11 attacks would have been avoided if the government had heeded early warnings, Editor Paul D. Winston says in Commentary. **Page 6**

Who's inspecting the inspectors?

A government leak of confidential employer names should be investigated, this week's editorial says. **Page 8**

Australian states consider tort reform

A public liability crisis in Australia is prompting proposals for limiting litigation. **Page 25**

NAIC to advise Chinese regulators

U.S. and Chinese insurance regulators have agreed to exchange information. **Page 25**

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REPORTING WEEKLY ON CORPORATE RISK, EMPLOYEE BENEFIT AND MANAGED HEALTH CARE NEWS

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CONTINUED FROM PAGE ONE
underscored the risk that another major terrorist attack could strike when businesses have limited terrorism insurance, forcing them "to bear directly the cost of such an attack." With major businesses facing the threat of bankruptcy in such a scenario, "it does not seem realistic to expect" the federal government to do nothing, says the report. "A federal bailout would almost certainly be demanded, and that federal role, developed in haste and under intense political pressure, might lead to a much larger, more costly and poorly designed role."

E.C. seeks to penalize France over mutuals

The European Commission will ask the European Court of Justice to penalize the French government for failing to comply fully with 1994 European Union directives aimed at creating a single European insurance market. In particular, the European Commission charges that France has failed to adopt the directives' regulatory provisions with regard to about 3,000 French mutual insurers. The Third Life and Non-life Insurance Directives include requirements that insurers must separate their insurance operations from other businesses and maintain adequate reserves. The European Commission said that it would ask the court to fine the French government 240,000 euros (\$213,960) per day until it complies with the directives.



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Health costs rise for small, midsize employers

Late News

The nation's small and midsize employers are being hit with steep price increases for group health insurance coverage, according to a survey of producers by the Council of Insurance Agents & Brokers. The CIAB based its findings on the responses of 60 of its member brokers and agents. Seventy-seven percent of respondents said that,



over the past six months, health insurance premiums increased at renewal by between 10% and 30% on average for midsize employers—which the survey defines as those with between 51 and 500 employees. In addition, 20% of respondents said such clients had been hit with premium increases of between 30% and 50%. Smaller employers—those with 50 or fewer employees—also saw big hikes. Among surveyed brokers and agents, 72% said their small-employer accounts had received increases of between 10% and 30%, while 23% of respondents said small clients had seen premium boosts of between 30% and 50%.

Mold coverage bill passes Calif. Senate

Legislation that would prohibit insurers from excluding mold coverage from property and liability policies was passed by the California Senate last week. The California Insurance code already requires



insurers to cover mold, said Mark Sektnan, American Insurance Assn. vp-western region in Sacramento, but Senate Bill 1763 would also prevent insurers from inserting a sublimit for mold. Instead, insurers would have to offer full policy limits for mold risks, he said. The bill will likely be heard by the Assembly in June.

GE unit to serve XL Winterthur clients

GE Global Asset Protection Services will offer its risk management services to clients of XL Winterthur International under a new agreement between the two companies. Under

the arrangement, GE GAP will provide XL Winterthur customers such services as candidate assessments, loss prevention field visits, risk mitigation, and risk assessment reports. XL Winterthur clients also will have access to GE GAP's Web-based risk management tools. XL Winterthur International, a unit of Hamilton, Bermuda-based XL Capital Ltd., writes property/casualty coverages for large national and multinational companies. GE GAP is part of Overland Park, Kansas-based General Electric Co. unit Employers Reinsurance Corp.

Briefly noted

Sphere Drake Insurance Ltd. plans to appeal an Illinois federal judge's decision that vacates an arbitration panel's 2-1 decision to void six reinsurance contracts that Sphere Drake wrote for All American Life Insurance Co. The arbitration panel voided the coverage—part of the Unicovert workers compensation debacle—because it determined from All American's own position paper that an unauthorized intermediary bound the coverage. But, the federal judge ruled that Ronald A. Jacks, the arbitrator Sphere Drake appointed to the panel, was partial to the reinsurer and had not disclosed some previous work that All American claimed he had performed for Sphere Drake's parent company....**Lloyd's of London** has named Nick Charteris-Black to the newly created position of head of capital provider relationships. He previously was with XL Winterthur International....California Assembly Bill 1985, which would introduce minimum rate requirements for **workers compensation insurance**, passed the state's Assembly last week. The bill will now be heard by the state Senate.

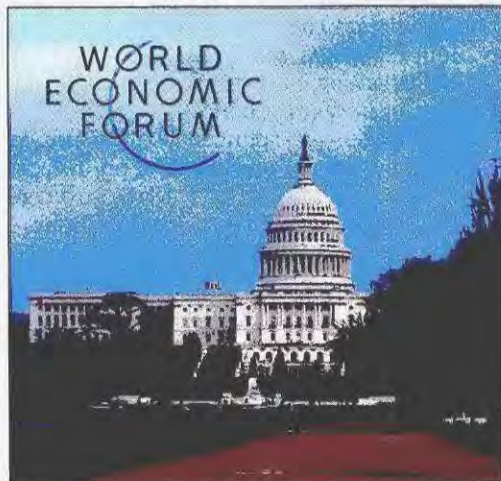
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All the material in the Late News column, as well as other content in this week's issue, is generated from daily news postings that appeared on the Web site in the previous week.

World Economic Forum focuses on the cost of risk

Terrorism threat to grow, panel warns



By MARK A. HOFMANN

WASHINGTON—Terrorism will not vanish as a threat to U.S. interests and is likely to only get worse.

That was a theme stressed by a panel of experts who discussed the broad topic of the cost of risk during the World Economic Forum in Washington last week. The panelists also endorsed the idea that not only should public and private sectors share more information about terrorism and cooperate more in dealing with the problem, but also that the federal government should act as a backstop to private insurance to help pay for future terrorism-related losses.

Government ends up involved with the risk by default, said Grahame Chilton, chief executive of

London-based Benfield Grieg Group P.L.C. He pointed out that Europeans have accepted a mixed government/private system for dealing with terrorism risks through such entities as the U.K.'s Pool Reinsurance Co. Ltd. He also noted that the effort to create such a mechanism in the United States has been stalled in the Senate because of disputes over tort reform. He urged his audience to "try and fight to get the right solution" to the problem of terrorism insurance.

Andreas Beerli, CEO of the Americas division of Swiss Reinsurance Corp. in Armonk, N.Y., pointed out that many countries, including the United Kingdom and Spain, have had considerable experience with terrorism and that the insurance industry in those countries has adapted

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California entities not liable for crime on public property

Court affirms sovereign immunity

By JUDY GREENWALD

SAN FRANCISCO—In a decision being hailed as a major victory for California public entities, the state Supreme Court has ruled that government entities generally cannot be held liable for crimes that occur on public property.

The unanimous May 20 decision in *Dana E. Zelig vs. County of Los Angeles* arose from a lawsuit filed after the death of Eileen Zelig, who was shot to death by her ex-husband in the Central Civil Courthouse in Los Angeles in 1995, in front of their 6-year-old daughter. The family was

there to attend a family court hearing on spousal and child support. Mrs. Zelig had previously obtained a restraining order that prohibited her ex-husband from possessing or carrying firearms. The courthouse had no metal detectors in place at the time.

A lawsuit was filed on behalf of the Zelig's children against the county, the sheriff's department, Mr. Zelig and 10 unnamed public employees, alleging wrongful death and negligence, among other charges.

In a unanimous opinion that overturned an appellate court's de-

cision, the California Supreme Court said, "In this and other jurisdictions, it is well established that public entities generally are not liable for failing to protect individuals against crime."

The decision said state statute provides that public entities may not maintain property in a dangerous condition. "We emphasize however that liability is imposed only when there is some defect in the property itself and a causal connection is established between the defect and the injury." But that was not the case here, said the decision. "Indeed, the risk of injury to Eileen

at the hands of her ex-husband was at least as great outside the courthouse. For example, he could just as readily have shot Eileen as she picked up one of her children from a public or private school."

Girard Fisher, an attorney with Pollak, Vida & Fisher in Los Angeles, said the decision "is probably the most important decision in favor of public entities in a decade, and maybe longer."

It has "resolved a question that's been battling back and forth in government law for the last 50 years" about whether a dangerous condi-

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HARD MARKET VIEWPOINTS

American Re surveyed property/casualty executives on various issues, including:

How much longer will the hard market last?	What are the two biggest threats to duration of the hard market?
69% 1-2 years	75% 'weak resolve' of management
21% 2-3 years	40% 'aggressive competition'

Source: American Re Corp.

Insurers skeptical hard market to last

By DOUGLAS MCLEOD

Most insurance company senior executives believe the current hard market cycle will be over within two years and that "weak resolve" within their ranks to maintain higher rates is the biggest threat to the cycle's duration, a survey by American Re Corp. concludes.

A majority of executives also cites the unavailability of terrorism coverage as the most critical issue facing the insurance industry, but few believe that Congress will act this year to alleviate the problem, the survey found.

American Re, a Munich Reinsurance Co. unit, canvassed 48 insurer chief executives and senior officers earlier this month during an annual forum at the reinsurer's Princeton, N.J., headquarters. The surveyed executives represented companies ranging in size from small single-state insurers to large regional insurers.

The officials answered a variety of questions about industry issues and about their own companies' operations.

Queried about the duration of the hard market—which American Re defined as price increases above the rate of claims cost inflation—69% of those responding said tight conditions will last between one

and two years, and another 8% said they expect a market turn within one year. A minority—21%—said the hard market will last two to three years, while 2% predicted it will continue for more than three years.

Dominic Addesso, president of American Re's direct treaty unit, expressed surprise at the expectation of a relatively quick market turn, "since earlier indications and predictions suggested that the hard market could last as long as three years."

Insurer CEOs also blame themselves in advance for the eventual softening. Asked what two factors pose the biggest threat to the hard market's continuation, 75% cited "weak resolve of industry senior management to achieve adequate returns," American Re found.

In addition, 40% of the respondents see "aggressive competition fueled by new capacity," notably from Bermuda companies, as a key factor in turning the market.

Terrorism, meanwhile, was at the top of the executives' lists of the most important problems facing the industry. Unavailability of terrorism reinsurance and questions about the applicability of terrorism exclusions in primary policies were cited by 65% as a critical issue.

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NCCI issues symposium

NCCI reviews comp problems

By MEG FLETCHER

ORLANDO, Fla.—Although the workers compensation losses from the Sept. 11 attacks were not as bad as was initially thought, they still worsened what was already a tough year for workers comp insurers, according to speakers at the annual symposium sponsored by NCCI Holdings Inc.

As a result, workers comp buyers will likely face greater underwriting scrutiny as their policies renew, speakers said.

"Unfortunately, this year the state of the workers compensation market remains difficult, with preliminary 2001 results reflecting one of the worst years in the market's history," said Chapin Clark, interim president and chief executive offi-

cer of the Boca Raton, Fla.-based NCCI. "The 2001 numbers tell a grim story, with some of the bad news tied to the Sept. 11 attacks on America," he said.

The combined ratio of 121% for the 2001 calendar year was an increase of three percentage points compared with 2000, according to preliminary figures released earlier this month at the NCCI's meeting in Orlando, Fla. That marks the sixth straight year of deteriorating results, which have returned to levels last seen in the early 1990s.

In addition, "potential reserve deficiencies in workers compensation on an ultimate-payout basis could be as much as \$21 billion in 2001,"

the NCCI said. The worsening results are due, in part, to lower investment income, according to the NCCI.

Improvements were seen, though, in the industry's 127% accident-year combined ratio, which is six percentage points lower than the 2000 ratio, according to preliminary statistics. That is due, in part, to insurers charging higher workers comp premiums last year, speakers said.

Particularly noteworthy is that the projected financial impact of the Sept. 11 terrorist attacks on primary insurers' 2001 preliminary results "is substantially less than origi-

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subscribers the ability to quickly access current articles online.

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IRS clarifies auto enrollment tax issues

By JERRY GEISEL

WASHINGTON—The Internal Revenue Service has clarified the tax status of two health care plan designs—both involving employee salary reductions used to pay health care premiums.

The first design, addressed by the IRS in Revenue Ruling 2002-27, involves a health plan that features an automatic enrollment process. Under that plan design, unless an employee objects, he or she is automatically enrolled in the employer's health plan, with the employ-

ee's salary reduced on a pretax basis to pay a portion of the premium. An employee who affirmatively rejects coverage does not have his or her salary reduced.

The question before the IRS was whether an automatic-enrollment plan effectively offers employees a choice between cash and a tax-free benefit. Such a choice must be present for a benefit arrangement to be considered a flexible benefit plan under Section 125 of the tax code. That qualification is important because under Section 125, employees can use pretax dollars to pay for

benefits.

In its ruling, the IRS said that an automatic-enrollment plan does involve a choice between cash and a tax-free benefit. After employees receive the notice about how the automatic enrollment process works, "The employee has an opportunity to choose between cash and a qualified benefit. Therefore, the plan's automatic enrollment is subject to the requirements of Section 125," the IRS said.

Although the IRS' position is not a surprise, it is welcome affirmation of a widely used practice.

"This is welcome ratification of what employers have done for years," said Andy Anderson, a consultant at Hewitt Associates L.L.C. in Lincolnshire, Ill.

"It is good to have the IRS' blessing on this," said Mark Hamelburg, an attorney with Mercer Human Resource Consulting in Washington.

The second type of plan involved in the IRS ruling also involves an automatic enrollment process, but with an unusual twist. Under this design, an employee can reject coverage and take in cash the health

premium contributions, but only if the individual can certify that he or she has coverage from another source.

If an employee cannot prove that he or she has other coverage, the employer enrolls the employee in a single-coverage indemnity plan. Because employees that lack other coverage effectively don't have a choice between cash and a tax-free benefit, the employer's plan—for employee-only coverage—doesn't qualify under Section 125.

But, the IRS said, as long as the employer doesn't ask for more than employee certification of other coverage, such as requesting specific information about that coverage, employees' health care contributions would be considered "deemed Section 125 compensation."

Benefit experts say they aren't sure why a request for additional coverage information would disqualify the contribution's status as deemed Section 125 compensation.

Deemed compensation, while not part of an employee's taxable income, could be counted as compensation for pension calculation purposes, the IRS said.

Specifically, the IRS said, deemed compensation would be considered employee compensation under Section 415(c)(3). That section limits the benefits and contributions that can be provided through plans.

For example, last year, the maximum contribution that could be made to a defined contribution plan was the lesser of 25% of an employee's compensation or \$35,000; while this year, due to the 2001 Economic Growth and Tax Relief Reconciliation Act, the limit was increased to the lesser of 100% of employee compensation or \$40,000.

Counting deemed compensation as employee compensation for Section 415 purposes effectively increases the benefits that can be provided through a pension plan.

Take the case of an employee who earns \$25,000, of which \$2,000 is considered deemed Section 125 compensation, representing his or her health insurance premium contributions. While the employee's taxable income would be \$23,000, his or her income for Section 415 purposes would be \$25,000. As a result, pension contributions of \$25,000—rather than \$23,000—could be made on behalf of that individual. Such a scenario would be most likely to develop if the employee had the resources to make hefty contributions to a plan.

While this issue was more important prior to the EGTRRA change, there are still employees who will benefit, said Kyle Brown, an attorney with Watson Wyatt Worldwide in Washington.

The ruling is retroactive to Jan. 1, 1998.

Errors & Omissions

- The May 6 edition of *BI* carried an incorrect issue number. The correct issue number is No. 18.
- Due to an editing error, a May 20 letter to the editor by Robert H. Myers Jr. incorrectly listed his location. Mr. Myers is based in Washington, though the National Risk Retention Assn.'s administrative offices are in Minneapolis.

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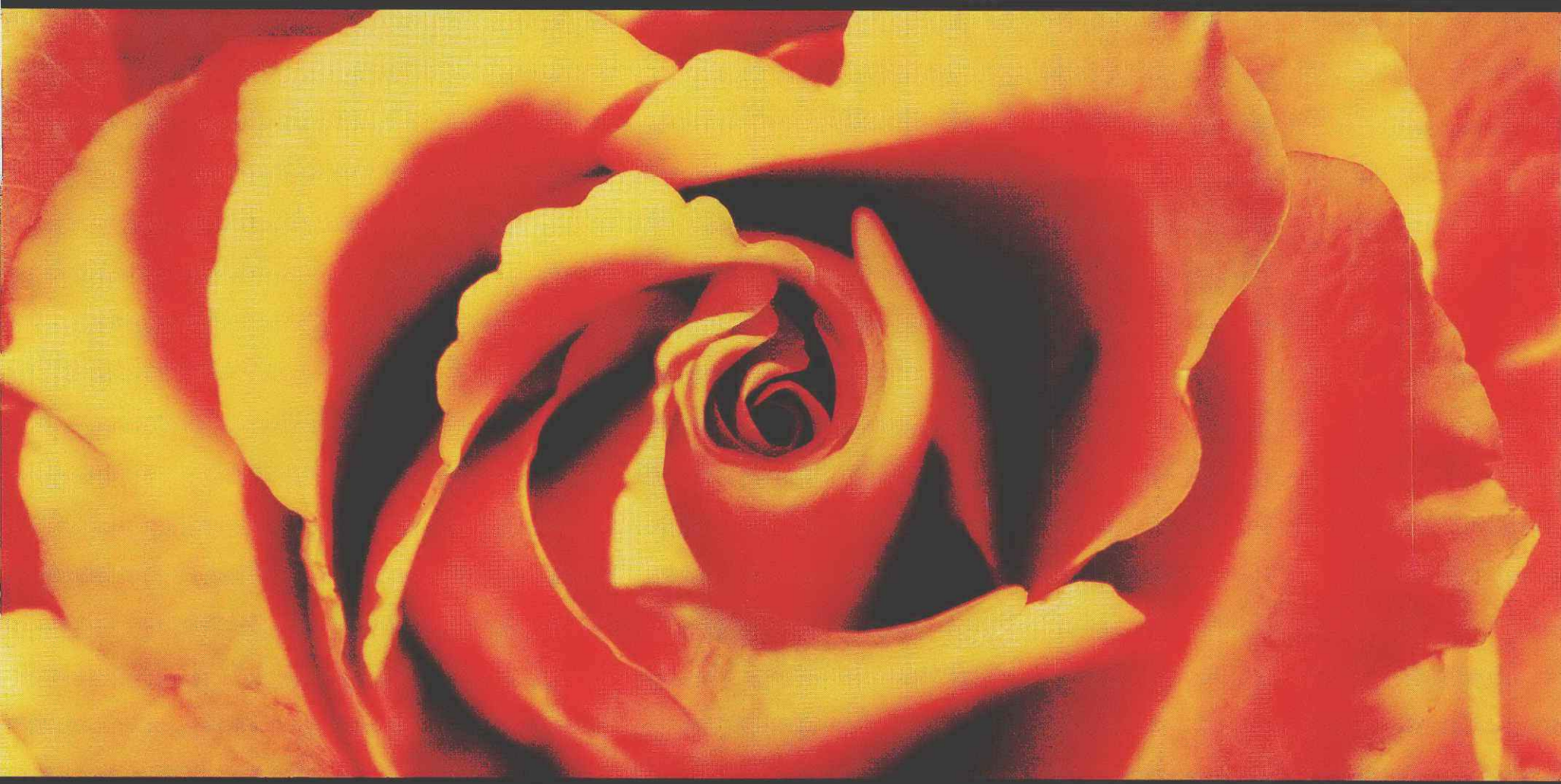


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Insurers: Execs polled

Continued from page 3

Toxic mold and construction defect claims were cited by 46% and general claims cost inflation by 38%.

Most of those surveyed were pessimistic about getting any help from Congress this year on terrorism or for another industry problem—*asbestos liabilities*. While virtually all of the executives, for example, agreed that Congress should create a federal terrorism reinsurance facility to back private insurers, only 27% believe lawmakers will act this year. Most respondents also cited a need for *asbestos liability reform* legislation, but only 13%

believe Congress will act during 2002.

Optional federal chartering of insurers was a relatively low legislative priority for the 48 surveyed executives. Only 23% said action is needed on the issue, and 17% expressed a belief that Congress will do something this year.

Most of the insurer officials say their companies will be more profitable over the next two years, but many also worry about maintaining underwriting discipline.

Thirty-six percent of those surveyed say their companies' combined ratios will improve by more

than five percentage points in the next two years, while another 52% said their combined ratios will improve by up to five points. Another 10% said they expect profitability to remain unchanged, while only 2% expect poorer results.

While nearly three-quarters of the senior managers cited underwriting discipline as a key competitive advantage for their companies, 40% also cited it as one of the crucial areas where their companies need to improve, American Re found.

Copies of the American Re survey results are available from Terese Rosenthal, 609-243-4339, trosenthal@amre.com.

Commentary

Eliminating risk an impossible aim

What did they know and when did they know it?

That refrain is again a focus of politicians, journalists and average citizens who are asking whether preventive action based on available information could have helped avoid the horrific losses from last Sept. 11.

This questioning arises from the disclosure that persons within the U.S. law enforcement and intelligence communities had issued various warnings about terrorist threats in advance of last September that were not acted on or passed along to the Bush administration. With the benefit of hindsight, which always makes things seem so clear, these reports are being touted as evidence that the government negligently disregarded warning signs, allowing the terrorist attacks to proceed unobstructed.

The emergence of these reports has caused politicians in both parties to spar over whether such second-guessing is fair or even patriotic. It has also prompted the Bush administration to now flood the media with warnings about potential but nonspecific terrorist threats—thereby elevating public anxiety—so that no one can again accuse it of failing to warn the public.

Even if the president or senior officials did have those reports prior to Sept. 11, and even if that had resulted in heightened security awareness before then, there is no certainty that the government could have prevented what occurred—or some equally heinous attack elsewhere, by someone else, using different means.

Just as is the case in professional risk management, the government cannot anticipate every threat or prevent every loss arising from the risks that are on its radar screen.

And, as is also the case in professional risk management, second-guessing and finger pointing in government circles always occurs after a big loss, in an effort to place blame.

It is healthy to review the adequacy of government risk management and security measures after any catastrophic event. After all, learning from mistakes is the way to improve the chances of avoiding them in the future.

But we cannot expect to eliminate all threats. That is as true for professional risk managers as it is for the government.

In the corporate world, any risk

manager who tried to eliminate all risks would also wind up stifling opportunities for his or her organization to conduct business and generate revenue. A company would be able to do very little—from hiring, to R&D, to manufacturing, to marketing, to distributing its products or services—if it first sought to avoid all risks that could create a loss.

Knowing this, the professional risk manager tries to create processes and introduce controls to minimize the extent of losses that do arise. The risk manager also raises awareness of risks so that others in the organization recognize their risk tolerance and can make decisions about their own

activities. This effort helps prepare people in an organization to respond appropriately when an unforeseen loss occurs to improve safety and minimize losses.

Similarly, the government walks a fine line between protecting the public from harm and not treading on their freedoms, which can include the right to

take risks. Obviously, no one would choose to incur the kind of harm that occurred Sept. 11, but it would require imposing significant limits on that freedom and other restrictions to minimize the risk of such attacks. While we might be safer from terrorist attacks, people would very likely chafe and revolt against such constraints.

The government also has to balance the public's desire for information about specific threats with the risk of creating a panic by providing too much information. Already, there is growing public opposition to the now-frequent warnings from administration officials about vague, ill-defined terrorist threats.

We have a right to expect that the government will take reasonable steps to protect us from harm and to eliminate known threats to our well-being. And, it should be accountable for the effectiveness of its efforts.

But I don't think we can expect that to mean the government has the duty, let alone the ability, to eliminate all threats.

That is an unreasonable expectation, and the cost of achieving such an end may be one that we don't wish to pay.



Paul D. Winston

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Editorial

Cash balance report raises queries

IS IT TIME to inspect the inspectors? That's a question that should be asked in light of the growing controversy surrounding a report issued by the Labor Department's Office of Inspector General on cash balance pension plans.

The report itself is highly suspect. The OIG reported that employees who terminated employment before retirement age at 13 of 60 companies it examined were denied benefits from cash balance plans to which they were legally entitled. Based on its finding, the OIG estimated that participants in the country's cash balance plans may be underpaid between \$85 million to \$199 million annually (BI, May 13).

The inspector's report triggered, not surprisingly, sensational headlines in daily newspapers on how employers were "shortchanging" workers and how the OIG had "uncovered" these mispayments.

In fact, however, it is very clear after a careful reading of the report that the OIG's assertion that cash balance plan participants were illegally shorted millions of dollars in benefits has little,

if any, basis in fact.

The OIG's finding is largely based on its acceptance of a theory on valuing account balances that was never adopted by regulators. This theory was outlined six years ago by the Internal Revenue Service on how account balances should be valued when an employee terminates employment and takes his or her benefit. The IRS never adopted this theory as regulation, but the OIG used it for its study as if it were the law of the land.

While it's disturbing enough that the OIG research was based on a flawed methodology, what is even more outrageous is that the OIG violated the confidentiality it promised employers participating in the audit. The OIG made the names of companies where the alleged benefit shortfalls occurred available to Rep. Bernard Sanders, I-Vt. Rep. Sanders, one of Congress' most strident cash balance plan critics, promptly released the names, resulting in very negative publicity for those employers.

So far, the OIG has said little about this betrayal of confidentiality except that its release

of the names was appropriate pursuant to a congressional request.

The ERISA Industry Committee has asked the Labor Department for an investigation. Certainly, some tough questions need to be asked, not the least of which is why OIG felt it had the right to release confidential information. It also invites suspicion that the person to whom the names were made available is one who has a known bias against cash balance plans, making one question whether the OIG shares these prejudices.

Whether pension plans are operating by federal rules is something government needs to know and should be examining. Such an examination only is possible through employer cooperation. But that cooperation surely will be lost if employers have no confidence that promises of confidentiality by government investigators aren't worth the paper they are printed on.

That should not be allowed to happen and a prompt examination of the OIG is called for to determine why it happened here.

Risk retention groups to the rescue

THE PLANNED FORMATION of a new risk retention group by U.S. airlines shows how buyers can solve their own coverage problems when confronted with harsh conditions in the traditional insurance market.

A group of U.S. airlines is in the process of forming a risk retention group called Equitime, which will provide them with up to \$2 billion in war risk liability limits at a substantially lower cost compared to their limited options in the traditional insurance market.

The formation of the RRG, which is seeking a Vermont license, also shows how important the federal Risk Retention Act is in eliminating regulatory obstacles to buyers' ability to rely on such groups for their liability insurance needs. Without the Risk Retention Act, which allows RRGs to operate nationwide after meeting the

licensing requirements of one state, Equitime never could have been formed with such speed.

While the Risk Retention Act paved the way for the formation of Equitime, it does not eliminate all the hurdles before it can begin operations. Key to its plan is for the risk retention group to obtain reinsurance from the Federal Aviation Administration. The FAA began providing war risk reinsurance to airlines after the market dried up after Sept. 11.

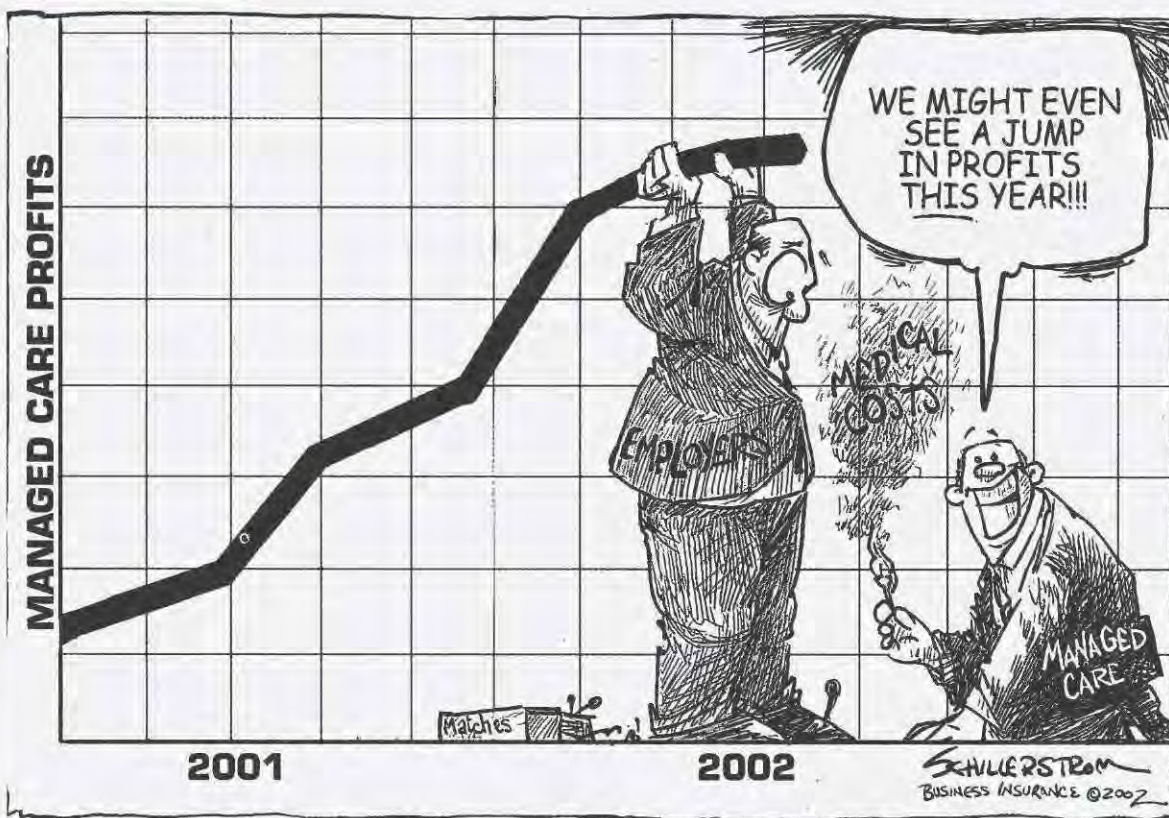
Insurers contend, though, that the government should not provide this sort of assistance to the airlines when a private market exists. But that private market is still unaffordable for most airlines as the cost could drive some of them out of business, given the financial straits they are in. Until the private market offers more competitive coverage, the

government should provide the reinsurance needed to help the facility get off the ground.

Just as federal assistance is required, at least for the moment, for Equitime to meet its organizers' risk financing needs, congressional intervention is needed to expand the Risk Retention Act. In 1986, during the last hard market, Congress expanded the law so groups could cover all liability risks—except workers compensation. That was a significant expansion—initially the groups only could cover product liability exposures—and an appropriate one given market conditions at the time.

We think there is a compelling case to expand the law once again so buyers can cover property risks and gain an alternative to increasingly costly and scarce property coverage in the traditional market.

Schillerstrom



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Risk Financing Options

Spotlight editor: Rodd Zolkos

Interest in captives expanding

Hard market driving buyers to alternatives

By RODD ZOLKOS

Difficult conditions in the traditional insurance market are prompting nearly unprecedented levels of employer interest in captive insurance companies.

The increased activity cuts across types of business and across lines of coverage, according to captive industry experts, as insurance buyers look for alternatives to the hard market.

"We're about as busy as we've been in the last 10 years. There's a ton of activity," said Guy F. Ragosta, managing director at Willis Management (Vermont) Ltd. "People are being hit with such incredible increases in their premiums."

"Typically when conditions like that occur, as they did in the early to mid-'80s, companies look to alternatives," said Jeff Kehler, manager special projects in the captive services division of Liberty Mutual Insurance Co. in Boston. "Captive insurance companies, being not new, are a great alternative for them to look at."

New interest in RRGs / 24

"We certainly are seeing a lot of inquiries," said Nicholas S. Dove, president of Quest Management Services Ltd. in Hamilton, Bermuda. "There's a lot of rent-a-captive programs people are looking at as well."

Mr. Ragosta suggested that while many businesses are looking to the captives as an alternative, it might not be an appropriate alternative for all of them.

"A lot of the people that are looking at captives, I don't know if it fits. There's an education process," he said. "But there's also a lot of real opportunities."

And, according to one consultant, for some, the timing might not be right, at least not in the current renewal cycle. That might suggest the trend toward increased captive formations could continue into the year ahead.

"The clients are confronted with the renewal terms and say, 'Oh my gosh, what are we going to do?' and typically that's too late to get the captive started," said Richard S. Betterley, president of Betterley Risk Consultants Inc. in Sterling, Mass. "But maybe that gets them started for next year."

One factor distinguishing the current hard market from that of the mid-1980s, and one that is shaping the current wave of captive ac-

See **CAPTIVE**/page 24



Capital markets fail to make big inroads

Complexity, costs are still barriers to growth

By DOUGLAS McLEOD

The capital markets have not seen the big increase in risk financing activity that many predicted in the wake of Sept. 11, though the markets are far from fading away as an alternative to traditional reinsurance, brokers and reinsurance observers say.

With commercial reinsurers already tightening terms before the terrorist attacks, many industry officials expected the attacks' huge losses to bring dramatic reductions in reinsurance capacity and increases in rates, spurring new interest in such capital markets alternatives as catastrophe bonds.

It hasn't happened.

The pace of new capital markets deals has picked up somewhat in recent weeks, but a flood of new business has not occurred, and the early part of this year proved especially quiet.

Asked how much activity the capital markets have seen this year, broker-dealer Morton N. Lane replied succinctly, "Not enough."

"There may have been a half dozen (deals), but it's a disappointing number," said Mr. Lane, president of Lane Financial L.L.C. in Kenilworth, Ill.

After Sept. 11, "people thought we would see a boom in securitizations, but that hasn't been the case," agreed James Doona, director with Standard & Poor's Corp. in New York.

One factor is the billions of dollars of new equity capital raised by existing and start-up reinsurers since the terrorist attacks. The new capital has helped hold down rate increases for traditional reinsurance, weakening demand for capital markets alternatives, some observers say.

Hurdles inherent to capital markets products have also contributed to the slowdown. The deals remain relatively complex and time-consuming to structure, because they must appeal to investors who want their risk precisely defined and quantified.

Still, securitizations are going forward, especially in areas where traditional reinsurance capacity remains tight, including retrocessional coverage for earthquake, windstorm and hurricane risks, observers say.

Market participants are also examining other lines of business for securitization—among them workers compensation and aviation coverages—and are developing new structures for transactions, such as splitting a deal into tranches with different levels of risk to appeal to different sets of investors.

"I don't expect a lot of screaming growth, but I don't see it going away, either," Mr. Doona said of capital markets activity.

Big growth is what many market participants anticipated for risk securitizations at the end of last year. Commercial reinsurers had

See **CAPITAL**/page 22

Cat bond market fears more red tape

By MARK A. HOFMANN

A series of regulatory and legislative initiatives could limit the effectiveness of some alternative risk financing options for risk managers and insurers.

Backers of catastrophe bonds that rely on special purpose vehicles regard proposals under consideration by the Financial Accounting Standards Board and the National Assn. of Insurance Commissioners as unwarranted intrusions into the marketplace.

In addition, a wave of federal legislation designed to curb offshore tax shelters for U.S. companies also could hamper use of some alternative risk transfer vehicles.

Special purpose vehicles frequently are used in the risk financing arena to issue catastrophe bonds and securitize other risks. However, looming regulatory initiatives might limit their attractiveness.

The Norwalk, Conn.-based FASB, which sets guidelines for generally accepted accounting principles, plans to consolidate multiple accounting rules for SPVs and similar entities. This project began more than a decade ago but took on new urgency after the collapse of Enron Corp., which used SPVs to shift assets and liabilities off its balance sheets.

Under the proposed FASB rules, companies would be required to keep SPVs and other entities, such as partnerships, on their books unless an independent third party has a stake of at least 10% in the entity. FASB's current standards allow companies to keep such special entities separate from their books if as little as 3% is owned by an independent third party.

Risk-linked securities experts say the proposed change, which could emerge in a formal draft as early as next month, should not be applied to SPVs used to issue cat bonds and other forms of risk financing.

"An SPV is really an element in a structure that is designed to permit the diversification and distribution of risk in the capital market. Risk-linked alternatives permit you to distribute the risk more widely in the capital markets, and we think that is something that should be encouraged," said Michel de Konkoly Thege, vp and associate general counsel of the Bond Markets Assn. in New York, whose members are involved in developing risk-linked securities.

In a risk-linked transaction, a ceding insurer puts a book of risk into an SPV, he explained. The SPV then sells bonds to investors and the cash generated by the proceeds are, in turn, invested in high-quality instruments, which are held by the SPV.

If certain losses or events occur, depending

See **REGULATIONS**/page 20



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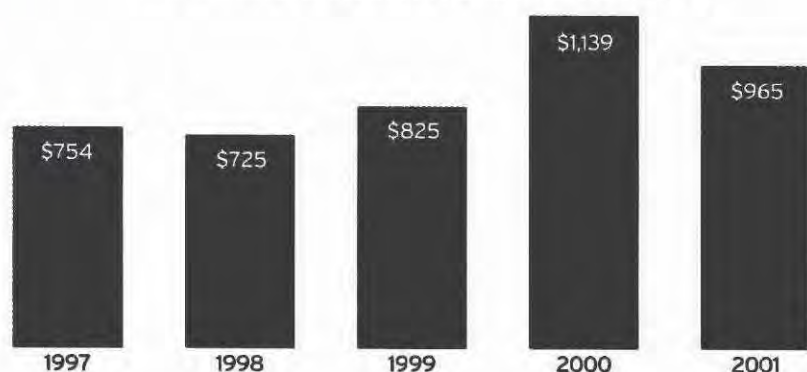
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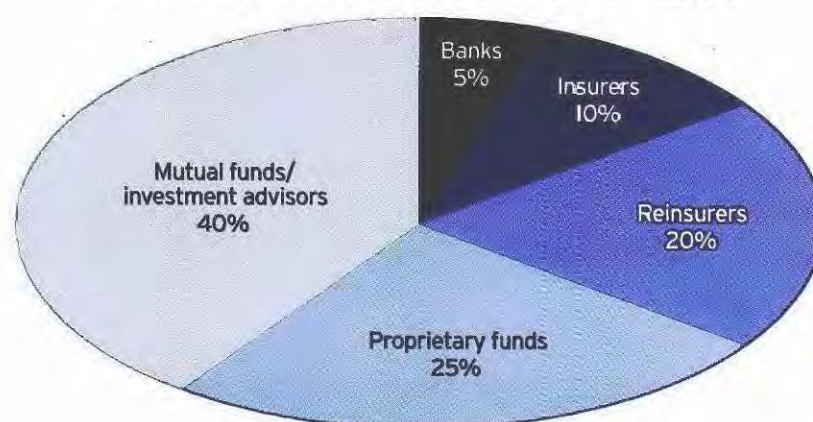
Issue volume 1997-2001

Risk-linked securities issue volume, in millions of dollars



Source: Swiss Re Capital Markets Corp.

Risk securitization investors in 2002



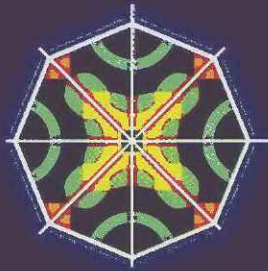
GRAPHIC BY ADAM DOI

Risk securitization specialists

Company Address	Phone/Fax Web site	Number of deals*	Types of risks securitized	Risk securitization employees	Officers
AIR Worldwide Corp. ¹ 101 Huntington Ave. Boston, Mass. 02199	617-267-6645 Fax: 617-267-8284 www.air-worldwide.com	5	Catastrophe	NA	Karen Clark, president/CEO
American Re Securities Corp. 555 College Road E. Princeton, N.J. 08543	609-243-4979 Fax: 609-951-3017	2	Catastrophe	2	Kenneth Bock, president
Aon Capital Markets 200 E. Randolph St. Chicago, Ill. 60601	312-381-5300 Fax: 312-381-0160 www.aon.com	9	Catastrophe, general first-party property, capital access problems	35	Bryon Ehrhart, Garrett P. Shumway, managing directors
Converium Ltd. General-Guisan-Quai 26 Zurich, Switzerland CH-8022	41-1-639-9393 Fax: 41-1-639-9090 www.converium.com	1	Catastrophe, earnings shortfalls, general first-party property, general casualty, capital access problems	8	Dirk Lohmann, CEO
Goldman Sachs & Co. 85 Broad St. New York, N.Y. 10004	212-902-1000 Fax: 212-902-3000 www.gs.com	5	Catastrophe, residual value, credit, capital access problems, life insurance risks, weather	NA	Andrew Kaiser, managing director
Hannover Re Karl-Wiechert-Allee 50 Hannover, 30625 Germany	49-511-5604-0 49-511-5604-1118 www.hannover-re.com	7	Catastrophe, aviation	6	Wilhelm Zeller, chairman
Kemper Insurance Cos. 500 W. Madison St., Suite 1100 Chicago, Ill. 60661-2555	312-559-2100 312-559-8520 www.kemperinsurance.com	8	Catastrophe	7	Donald W. Mosier, vp
LeBoeuf, Lamb, Greene & MacRae L.L.P. 125 W. 55th St. New York, N.Y. 10019	212-424-8000 212-424-8500 www.lgm.com	67	Catastrophe, residual value, credit, capital access problems, funding agreement note issuance program, life insurance and annuity risks	NA	John Schwolsky
MMC Enterprise Risk/ Marsh & McLennan Securities Corp. 1166 Ave. of the Americas New York, N.Y. 10036	212-345-5000 212-345-7316 www.mmcer.com	30 ²	Catastrophe, workers compensation, general first-party property, general casualty, credit, capital access problems	NA	Bob Khanna, president/ CEO-MMC Enterprise Risk; Jamshid Ehsani, president/CEO-Marsh & McLennan Securities Corp.
Swiss Re Capital Markets Corp. 55 E. 52nd St. New York, N.Y. 10055	212-317-5400 212-317-5450 www.swissre.com	4	Catastrophe	10	Dan Ozizmir, senior managing director

* Deals include any of those in which firm's involvement includes consulting, underwriting, modeling or bringing the risk securitization issue to market. ¹Formerly Applied Insurance Research Inc.; acquisition by Insurance Service Office Inc. is pending. ²Bestimate. NA=not available
Source: BI survey

The 2002 Risk Securitization Online Directory is available in the directory area of www.businessinsurance.com. The directory is searchable by company name, number of deals, services provided and types of risks securitized. If your company provides risk securitization services and would like to be listed in the online directory, contact Directory Editor Kevin Edison at 312-649-5279 or kedison@crain.com for a questionnaire.

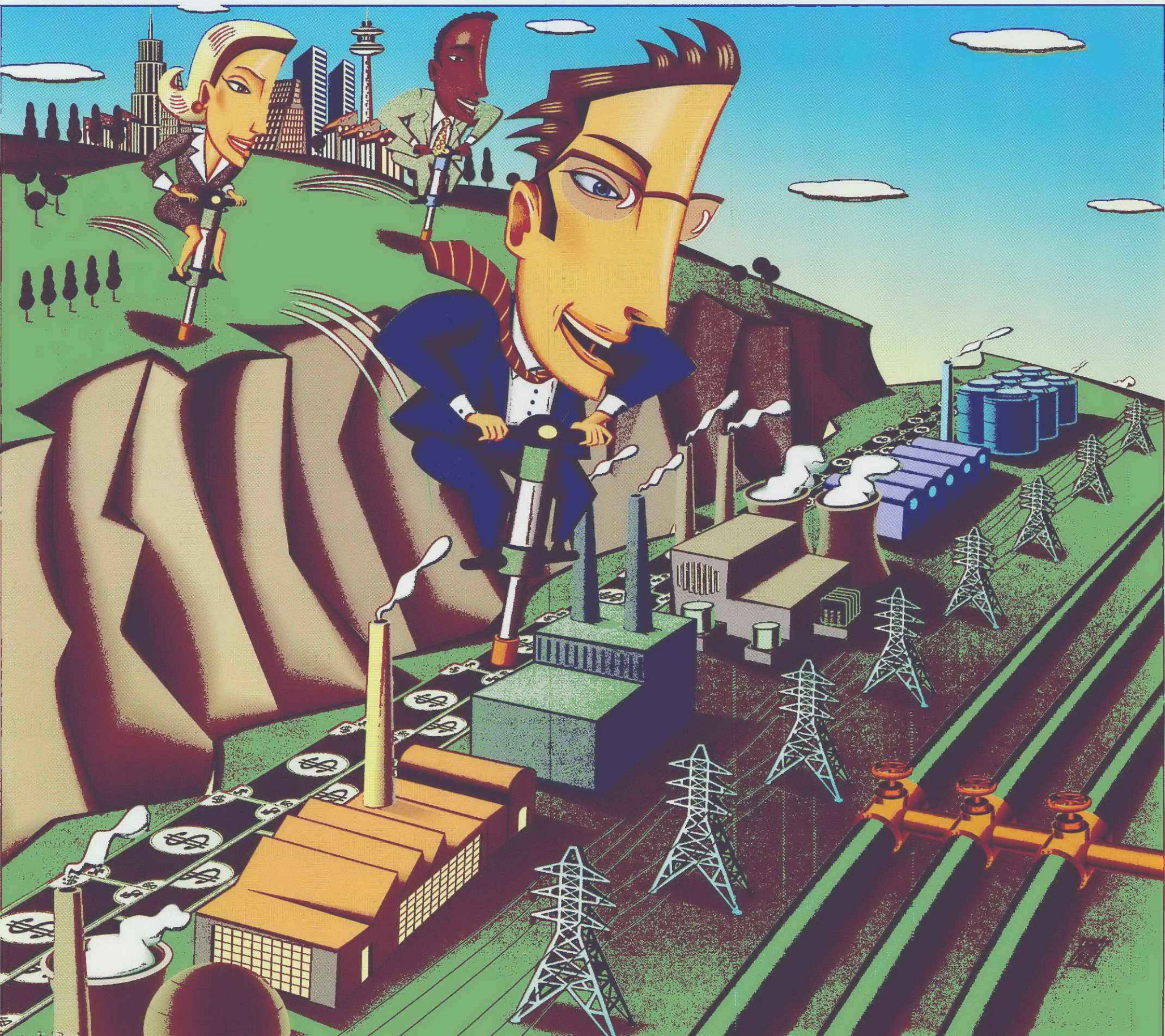


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C R E A T I N G C E R T A I N T Y SM



Fewer integrated risk programs post-Sept. 11

By MICHAEL BRADFORD

It's getting harder for risk managers to find an insurer that is willing to put together an integrated insurance program of the kind that was readily available during the soft market.

When prices were low and insurers were competing for business, underwriters were actively promoting integrated programs. Such programs, which typically are written on a multiyear basis, bundle together various coverages into one integrated package.

Now, in the post-Sept. 11 insur-

ance world, many underwriters aren't as focused on creative coverage offerings as they were when they were looking for new ways to attract business and boost volume.

One reason is that, in some cases reinsurance is not as plentiful for the programs as it once was. In addition, in the wake of the Sept. 11 terrorist attacks, insurers have become more wary of large exposures that could span several lines of coverage.

"A number of major insurers have indicated that they are not going to be doing this very seriously," said Edward Koral, a senior manag-

er at Deloitte & Touche L.L.P. in New York, referring to writing integrated coverage. Mr. Koral, who recently joined the company after leaving Marsh & McLennan Cos. Inc. unit MMC Enterprise Risk, said some insurers had asked Marsh not to emphasize integrated programs to their clients.

Indeed, some insurers, including XL Capital Ltd. and Swiss Re New Markets Corp., declined to be interviewed about integrated risk programs, despite promoting their willingness to write such coverage in recent years.

Others were blunt about their de-

cision not to commit to multiyear deals such as integrated programs.

"We're not writing multiyear insurance commitments any longer," said Greg Flood, chief operating officer at National Union Fire Insurance Co. of Pittsburgh, Pa., a unit of American International Group Inc. Exceptions may be made for "singular-event" coverages, he said, such as liability coverage for directors and officers of a company that was sold.

Mr. Flood said National Union quit writing multiyear deals because locking in premiums takes away the insurer's ability to adjust charges

should costs rise. Doing so "could leave us disastrously insufficient in our funding for future claims," he said.

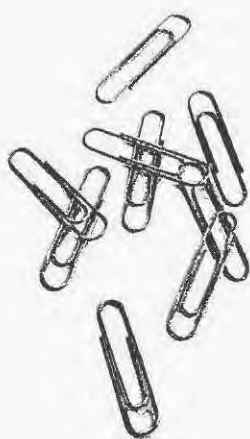
Nevertheless, risk managers continue to show interest in the concept of integrated risk financing. Deloitte's Mr. Koral said buyer interest probably is greater today than it was in the final days of the soft market, now that capacity is so much more expensive for monoline transactions.

"But are insurers willing to offer it?" Mr. Koral asked. Because of restrictions on the amount of reinsurance they can obtain, many insurers are not enthusiastic about offering integrated programs, he said. "Reinsurers are circling the wagons and not providing a lot of capacity in the integrated area."

'Reinsurers are circling the wagons and not providing a lot of capacity in the integrated area.'

Edward Koral
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In the wake of the Sept. 11 attacks, insurers also "are now keenly aware" of the potential for big losses on risks that span several lines, said Charlie Ruoff, senior vp and chief marketing officer with Chicago-based brokerage Acordia Inc. They are taking a "new view" toward the lumping together of property, business interruption, workers compensation and other risks, he said. Mr. Ruoff also noted that reinsurers have become reluctant to offer capacity for the programs.

Integrated programs have "really gone by the wayside dramatically," said Bob Slovin, the Hilton Head, S.C.-based senior vp of commercial marketing for brokerage USI Insurance Services Corp. He agreed that reinsurance costs have likely played a part in insurers' decisions to back off. "It's a reinsurance-driven marketplace."

Not all insurers have cooled on the concept, however. Business is booming for at least one company that continues to put together integrated programs.

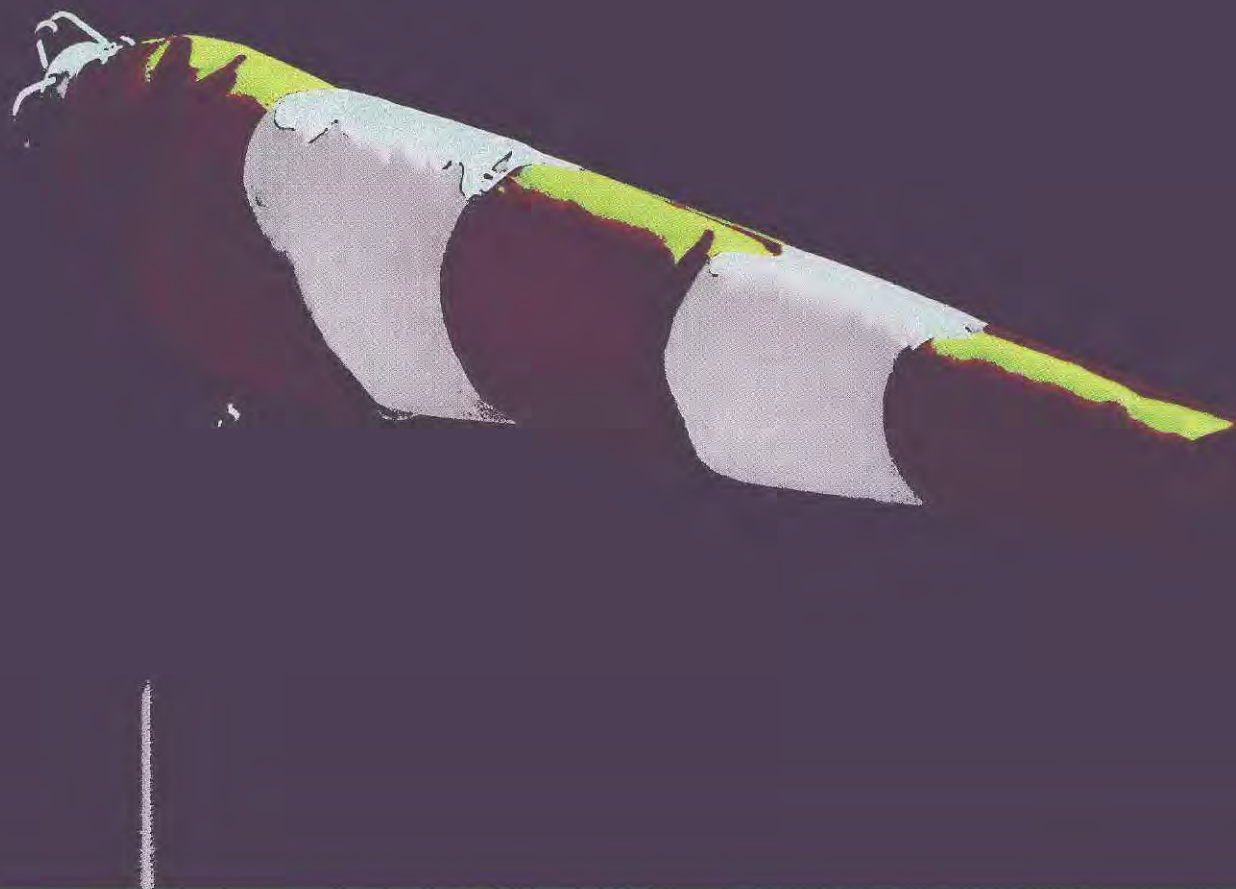
"Our business has never been better," said Randall Clouser, chief executive officer of Zurich Corporate Solutions in New York. "Demand is higher than it's ever been. The economics of integrated risk financing are more compelling in a more rational pricing market than in the soft market."

Zurich Corporate Solutions, a unit of Zurich Financial Services Group, is a "boutique operation" that offers only integrated programs, Mr. Clouser said. He acknowledged that competitors in that area have become scarce.

"I wish there was more competition," Mr. Clouser said, because more capacity for integrated programs would make them "more common in the marketplace."

For policyholders, the value in an integrated program is that they are

See **INTEGRATED**/page 16



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Integrated: Fewer insurers offering programs

Continued from page 14

"taken out of the transactional insurance marketplace," said Mr. Clouser. Risk managers who currently are in the middle of three-year contracts are looking very good in the eyes upper management, he pointed out, because those companies were "totally unaffected" by the recent market hardening.

As for its reinsurance, Zurich Corporate Solutions renewed its treaty April 1. Mr. Clouser said there was some increase in pricing but that the change was not drastic.

Michael McAndless, director of risk management at Agricore Unit-

ed Ltd. in Winnipeg, Manitoba, said that risk managers who want to implement an integrated program will have a much better chance if they present underwriters with a well-organized proposal. "Integrated risk programs don't just fall out of the air," he said, noting that a risk manager needs to conduct a thorough analysis of an organization's exposures before approaching an insurer.

Agricore United recently merged with United Grain Growers Ltd., where Mr. McAndless served as risk manager. An integrated program in place at United Grain and written

Risk managers who want to implement an integrated program will have a much better chance if they present underwriters with a well-organized proposal.

*Michael McAndless
Agricore United Ltd.*

on a three-year term by Swiss Re New Markets renews Dec. 31. Mr. McAndless said he expects the program to renew and that there is a

possibility that integrated programs could be structured in the future to cover the risks Agricore has insured in the traditional market.

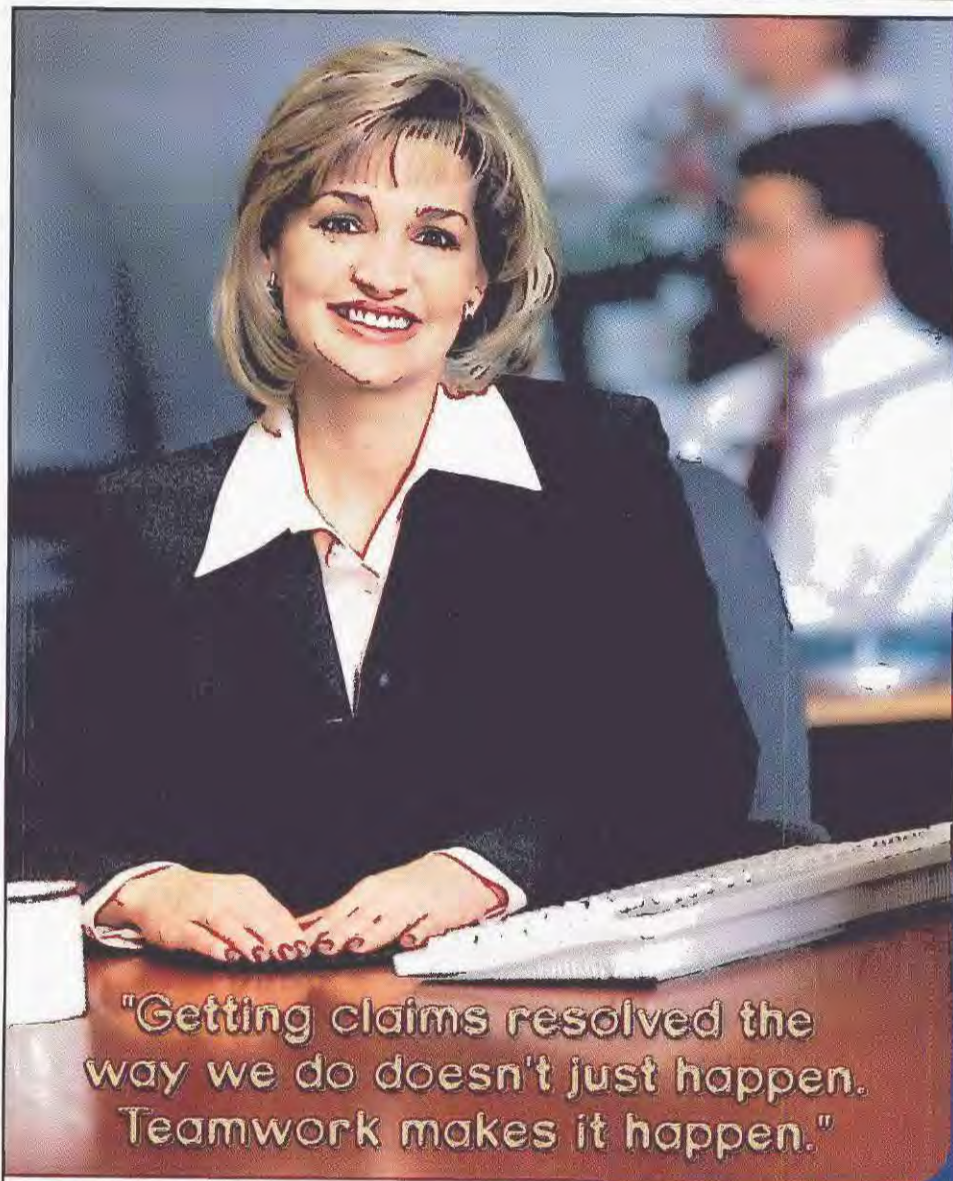
An enterprisewide program written for FMR Corp., better known as Fidelity Investments, is up for a June 30 renewal. "We're cautiously optimistic" about the renewal, said Tom Wronski, senior vp-insurance and risk management at Boston-based Fidelity.

The insurers on the program—American International Group, XL America Inc., Swiss Re New Markets and London market underwriters—are "preparing us like at any other

renewal," Mr. Wronski said, with indications that there could be price hikes.

But even with the current market conditions, "there has been surprisingly little doom and gloom" from insurers, he noted.

Not all risk managers have seen smooth renewals of their integrated programs. Mr. Korall said that while at Marsh, he worked with a client who badly wanted to renew its program but had to abandon the effort because insurers could not offer reasonable pricing. "It did not make any economic sense," he said of the proposed deal.



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CEA decides against using cat bond

By ROBERTO CENICEROS

After weighing whether to transfer a \$738 million catastrophe exposure into the capital markets, factors such as favorable pricing and concerns about public perception of offshore transactions prompted the California Earthquake Authority ultimately to stay with the traditional reinsurance market.

Obtaining capacity through a catastrophe bond placement would have been a significant change for the Sacramento-based CEA, a quasi-governmental insurer that provides earthquake insurance for approximately 830,000 California homeowners. The CEA, which has an annual premium volume of \$433 million, was formed in December 1996 to address a lack of private coverage for earthquake risks in the state. Since its formation, the CEA has obtained reinsurance coverage mainly through the traditional market.

Had the CEA cat bond deal gone ahead, it would have dwarfed a \$450 million transaction for hurricane exposure currently considered the largest catastrophe risk securitization deal, according to a market analysis prepared for the CEA by its broker, Benfield Blanch Inc.

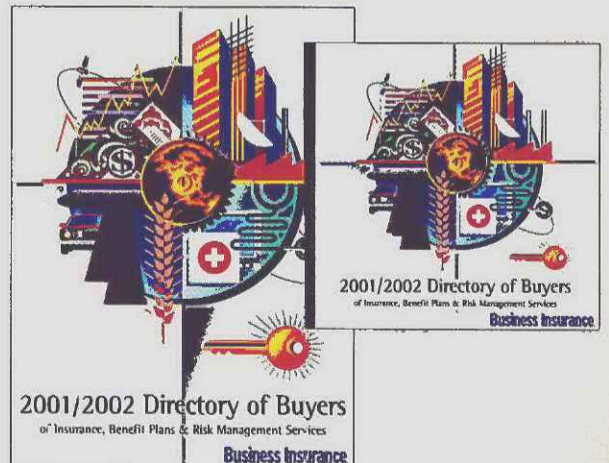
But the proposal was abandoned, in part because the CEA was able to negotiate a satisfactory arrangement in the traditional reinsurance market. In addition, the CEA's board was concerned about public perception of the securitization deal because it would have required the use of an offshore facility similar to entities used by troubled Enron Corp.

In March, the authority put together \$1.34 billion in reinsurance limits from 39 reinsurers, said Tim Richison, CEA chief financial offi-

See CEA/page 18

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CEA: Quake facility remains with traditional market

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cer. The reinsurers, all acting under one contract, provide three layers of coverage for 2003 that help the authority maintain \$7 billion in claims-paying capacity, CEA officials say.

Other layers within the CEA's \$7 billion claims-paying capacity are provided by the authority's own capital, a line of credit, and potential assessments against insurers that sell property coverage in California.

For the \$1.34 billion in reinsurance limits purchased for 2003, the CEA will pay a premium of \$110

million. That represents a 7% rate increase over the amount it paid to buy \$1.9 billion in limits for 2002, Mr. Richison said.

"We got such a great price on reinsurance...that the cost for the catastrophe bonds wasn't going to be any cheaper than reinsurance," Mr. Richison said.

Some of the CEA-related risk did eventually make its way to the capital markets, though. One of the CEA's reinsurers, Swiss Reinsurance Co., retroceded its exposure in a securitized deal structured by Lehman Bros. in New York.

The CEA obtained a 7% renewal

rate increase in part because it gained negotiating leverage by in-

'We got such a great price on reinsurance...that the cost for the catastrophe bonds wasn't going to be any cheaper than reinsurance.'

Tim Richison

California Earthquake Authority

forming reinsurers that it was considering placing some of the coverage in the capital markets, accord-

ing to a source familiar with the authority's reinsurance negotiations.

Reinsurance rates for California earthquake coverage vary greatly, but they currently average between 30% and 40%, said Sean F. Mooney, chief economist and research director for reinsurance brokerage Guy Carpenter & Co. Inc. in New York. Guy Carpenter, which is a unit of Marsh & McLennan Cos. Inc., did not place the CEA's reinsurance.

A reinsurance buyer that gets a 7% rate increase is doing "quite well," Mr. Mooney said. But, he noted, the CEA is considered a "technical risk," meaning reinsurers

feel confident they can accurately price the coverage using catastrophe models. In addition, the authority's risk profile does not change much from year to year, making it easier for reinsurers to price the risk, Mr. Mooney said.

Given those factors and the growing capacity for catastrophe risks, it is hard for reinsurers to push for larger increases from the CEA, Mr. Mooney said.

The authority initially decided to examine capital markets alternatives after a consultant and state auditors determined in 2000 that the association should consider reducing its reliance on reinsurance. Because pricing in the traditional market can be volatile, the CEA was looking to smooth out the peaks and valleys, Mr. Richison said.

But the authority would only look to the capital markets if doing so were economically sound, and "we did not find that reinsurance prices escalated to the point that would have made catastrophe bonds economically advantageous," Mr. Richison said.

Using a securitized program also faced another hurdle: public perception.

A cat bond placement would have required the creation of a special-purpose vehicle. SPVs, which generally are located offshore, transform reinsurance purchased by a ceding insurer into catastrophe bonds sold to investors.

And SPVs recently came into the public eye when Houston-based Enron's troubles emerged last year. At that time, it was widely reported that the company had used offshore SPVs for tax purposes.

That created a perception problem regarding SPVs among CEA's board of directors, who decided that, in light of the Enron situation, the timing was not right for creating an offshore facility, Mr. Richison said.

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Regulations: New limitations on SPVs possible

Continued from page 10

on the level of damage and the layer of coverage, the SPV might liquidate those securities it holds and pay the proceeds to the ceding insurer. If there is no triggering event, the bondholders get their principle back as well as the yield during the period of transaction, explained Mr. de Konkoly Thege. The SPV is essentially a protection for the investor, he said.

"The proposed regulations appear to require independence and 10% equity," said Malcolm P. Wattman, partner in the law firm of Cadwalader, Wickersham & Taft in New

York. "The independence requirement can probably be met. Raising the equity level from 3% to 10%, assuming that non-consolidation is an issue, will present additional expense and make cat bond deals less attractive economically," he said.

"None of this makes sense because, unlike Enron-type transactions, there are no assets being moved off balance sheet or liabilities being disguised," Mr. Wattman said. "The cat bond is merely reinsurance to the sponsor and requiring the sponsor to put the bond debt on its balance sheet would be

misleading from an accounting point of view. Nevertheless, no exceptions appear to be available," he said.

FASB is not alone in attempting to regulate SPVs. The NAIC promulgated a special purpose reinsurance vehicle model act in 2001 to encourage risk securitization deals to be done onshore, where they can be monitored by state regulators. Only Illinois and South Carolina so far have adopted the model law, which does not mandate that such deals be done onshore.

"The purpose was to create a legal structure to do a special purpose

reinsurance vehicle through a U.S. corporation rather than having to go offshore," explained Arnold Dutcher, chief deputy director of the Illinois Insurance Department in Springfield.

Mr. Dutcher said that beyond that concern, the purpose of the model law also is to establish U.S. regulatory approval of such transactions before the deals are consummated and to establish solvency and transactional standards for the deals.

Some risk securitization experts are not swayed by the NAIC efforts in light of federal income tax con-

cerns.

"I am not a supporter of the efforts to do cat bonds domestically. I think the offshore deals work fine. While there is some additional expense and inconvenience associated with being offshore, on the margin I do not believe it is that substantial," said Mr. Wattman.

"The issue with domestic issuers is that the cat bond will almost never qualify for debt treatment for tax purposes, which means that the issuer would be subject to taxation on its income without the ability to deduct the interest on the bonds—which would be treated as dividends for tax purposes," he said.

"That would be a nonstarter. The NAIC effort is nearly worthless unless there is accompanying tax legislation. You can guess what the probability is of Congress passing favorable tax treatment for any sort of SPVs in this climate," said Mr. Wattman.

'The NAIC effort is nearly worthless unless there is accompanying tax legislation. You can guess what the probability is of Congress passing favorable tax treatment for any sort of SPVs in this climate.'

*Malcolm P. Wattman
Cadwalader, Wickersham & Taft*

"If the NAIC wants to bring offshore onshore, our position was that was fine, as long as the accounting and regulatory structure, including tax treatment, is consistent with reinsurance," said Joseph B. Sieverling, vp and director of financial services for the Reinsurance Assn. of America in Washington. Apart from tax treatment, he said the RAA has other concerns about the NAIC proposal for onshore SPVs, including the fact that it would allow as many as 10 cedents to pool their risks in a single vehicle.

Meanwhile, proponents of alternative risk financing are keeping an eye on federal legislation aimed at discouraging U.S. corporations from reincorporating in foreign countries to avoid U.S. income taxes.

Bills have been introduced in the House by Reps. Richard Neal, D-Mass., and Nancy Johnson, R-Conn., and in the Senate by Sens. Max Baucus, D-Mont., and Charles Grassley, R-Iowa, to curb such redomestications but have not moved very far.

"With regard to the corporate inversion legislation that has been introduced, it is our understanding that it is not the intent of any legislator to go after these types of transactions, but we continue to analyze the various legislation to make sure this not the case," said Frank Hampton, senior vp for the Bond Markets Assn. in Washington.

"We are certainly trying to make sure that no unintended consequences come out of this legislation."

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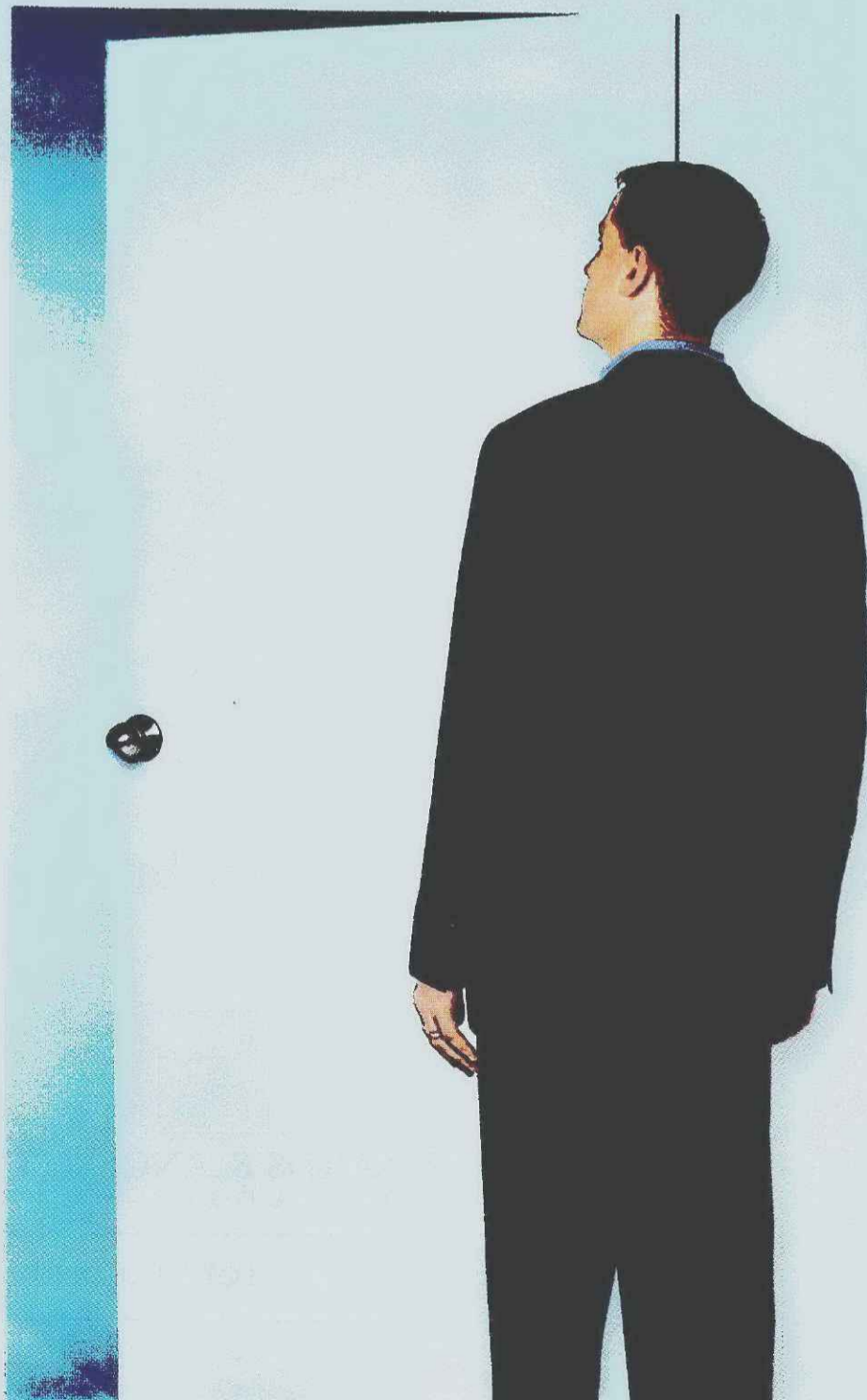
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Capital: No big increase in risk securitization seen

Continued from page 10

already begun to raise rates and restrict coverage even before the Sept. 11 attacks, and retrocessional capacity in particular had diminished dramatically. Soon after the attacks, when industry losses were projected at \$50 billion or more, many reinsurance market observers predicted doubling or tripling of rates and severe shortfalls in capacity.

However, new equity capital poured into the market—with several billion dollars in new money going to existing and start-up reinsurers in Bermuda—and tightening continued in only modest form, with rate hikes averaging in the low double digits, market observers say.

Catastrophe bond pricing does not move in lockstep with commercial reinsurance pricing, and prices in the cat bond market have actually fallen since the terrorist attacks as traditional reinsurance rates have climbed, noted John Kiernan, managing director with Lehman Bros. in New York.

Nevertheless, the expected boom in risk securitizations hasn't followed the hardening commercial market.

"At the beginning of the year, we thought there would be tremendous opportunities" for the capital markets, said Anqi Liu, managing senior financial analyst with A.M.

Best Co. in Oldwick, N.J. But "it's not making a killing at all."

The influx of capital in the traditional market has, in many cases, "at least postponed the need for securitizations," Mr. Lane observed.

Even with commercial reinsurance prices rising, the capital markets alternative "is not as cheap a form of capacity as that available in the traditional market," said Kew-song Lee, a partner with Warburg Pincus L.L.C. in New York. Warburg Pincus last year contributed part of the \$750 million raised by Bermuda-based Arch Capital Group Ltd.

Another factor dampening investor interest in risk-linked securities is that they are relatively difficult to trade, Mr. Lee suggested. "The liquidity of these instruments has not historically been all that great," he said.

Other problems inherent to securitizations have made them less attractive than traditional reinsurance, including the time required to model a deal's underlying risks, obtain a rating and market the issue to investors.

"To do capital markets deals, it takes an incredible amount of senior management time and energy," observed Enda McDonnell, president and chief executive officer of Access Reinsurance Inc., a Westfield, N.J.-based intermediary.

Mr. McDonnell and three other former Willis Re officials formed Access Re earlier this year to specialize in industry loss warranty and other reinsurance products.

Despite these problems, though, a few capital markets deals have been done this year—or are in the works—after a slow start.

'The investor universe is growing slowly but surely' for cat bond issues.

John Kiernan
Lehman Bros.

Lehman last month completed a deal, dubbed Redwood II, securitizing \$200 million in California earthquake risk assumed by Swiss Reinsurance Co. from the California Earthquake Authority, according to Lehman's Mr. Kiernan. Swiss Re in April took over portions of the CEA reinsurance program previously written by Berkshire Hathaway Inc., and has retroceded the business to investors through Redwood II, he explained. The CEA had itself explored securitizing its reinsurance coverage but, ultimately, obtained reinsurance from Swiss Re and other companies in the traditional market (see story, page 16).

San Antonio-based USAA Group Inc. is also working on a new cat bond issue through its Cayman Islands-based Residential Reinsurance Ltd. unit, a USAA spokeswoman confirmed.

"The investor universe is growing slowly but surely" for cat bond issues, Mr. Kiernan said, adding that bonds make the most sense "where there are capacity issues in the traditional market."

So far, the focus has been on such quantifiable exposures as California, Japanese and central U.S. earthquake risk and U.S. and European windstorm exposure, he said.

The ability to quantify exposure is key to a successful securitization, though. Although some market participants are trying, for example, to develop models to quantify terrorism risk—an area where traditional market capacity is virtually non-existent—Mr. Kiernan and others express doubts that the risk can be made predictable enough to attract investors.

Some have likewise raised the idea of securitizing tobacco or other mass product liability risks, but the unpredictability of jury behavior makes these exposures unlikely candidates for the capital markets, Mr. Kiernan added.

More promising ideas include securitizing catastrophic workers

comp exposure—arising, for example, from buildings being destroyed in an earthquake—and aviation risks excluding terrorism, Mr. Kiernan said. He said that "it would not surprise me" to see a workers comp deal done this year.

Market participants are also developing new structures to attract a broader range of investors.

Swiss Re Capital Markets Corp., a Swiss Re unit, recently completed a \$40 million securitization that adopted an approach used by mortgage lenders to package and sell collateralized debt obligations. The Swiss Re deal's pool of underlying risks—industry loss warranties and index-linked insurance contracts for worldwide natural catastrophes—was divided into four tranches with varying levels of cat risk, according to Swiss Re. Investors could thus opt for securities carrying a higher level of risk for a higher return or for those with less risk for a lower return, the reinsurer said.

In general, Swiss Re sees this and other risk-linked securities as part of an array of risk financing options that also could include contingent capital arrangements and finite reinsurance, noted Prakash Shimpi, president and CEO of Swiss Re Financial Services Corp. in New York.

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Market sparks new interest in risk retention groups

By **RODD ZOLKOS**

The hard insurance market is spurring considerable interest in risk retention groups, as entities with comparable risks and similar difficulties finding coverage—such as U.S. airlines seeking war risk insurance or doctors struggling to find medical malpractice coverage—look to the alternative market for solutions.

RRG proponents also hope the hard market will provide an added boost to their efforts to win approval of a proposal to expand the groups' risk financing authority to allow them to write property and other risks, in addition to the commercial casualty coverages they currently provide to their members.

"We're presently in the search for another co-sponsor (for the Senate bill). But to date we've heard of no opposition," Jon Harkavy, vp and general counsel of Risk Services L.L.C., Arlington, Va., said of the effort to expand the federal Risk Retention Act.

The measure would allow RRGs to write anything but workers comp or personal lines, said Mr. Harkavy, who is a member of the National Risk Retention Assn.'s government affairs committee.

According to Gary Osborne, a senior vp at USA Risk Group in Montpelier, Vt., a major attraction of the proposed change is its scope.

"A big plus to me is that it's not just property; it takes away that problem of what's considered liability and what's not," Mr. Osborne said.

"I had a proposal today that I'm trying to figure out if I can get done. It's a bail bond program," he said. "The problem is some states consider it a liability product. Some states consider it a surety product. If we get the amendment, that problem goes away."

Janice M. Abraham, president and

'What we have heard from (RRG members) is what we do so well for them in liability insurance, they very much want us to do in property and fleet auto.'

Janice M. Abraham
United Educators Insurance
Risk Retention Group Inc.

CEO of United Educators Insurance Risk Retention Group Inc. in Chevy Chase, Md., said her group is eager to take advantage of such a change.

United Educators for 15 years has provided stable liability coverage to 1,100 academic institution members, which is a "very unique line of business that we think we understand very well," she said.

"What we have heard from (RRG members) is what we do so well for them in liability insurance, they very much want us to do in property and fleet auto," she said. "So we're very supportive of this. We feel that as a risk retention group, we have proven that we can run a sound business. We understand the risks, we underwrite them appropriately, pay claims appropriately."

As it has for captive insurance companies, the hard traditional market is spurring interest in new RRG formations. Mr. Osborne said about half of the ART proposals he's seeing currently are for RRGs, many of them for groups where coverage is particularly tight—doctors, nursing homes and truckers.

"Those are the three main industries, but we're also getting lots more," he said.

Reinsurance in this market can be a problem for RRGs, just as it is for captive insurers, and its availability can determine whether a new group's formation is feasible.

With the medical groups, for example, "There is some reinsurance available," Mr. Osborne said. "Not a lot, but there is a possibility these will happen."

One of the more dramatic RRG

proposals came earlier this year with the announcement that a group of major U.S. airlines sought to form a Vermont-domiciled group called Equitime to provide war risk coverage.

The Air Transport Assn. member airlines are working with Marsh Inc. to form the RRG, which proposes to offer up to \$1.5 billion in combined limits for passenger and third-party war risk liability. The group would retain a portion of the limit, reinsuring the balance with the federal government.

The proposal was developed after the airlines had difficulty obtaining those coverages in the commercial aviation insurance market following the Sept. 11 terrorist attacks. Although some private coverage has since emerged, airlines have said it is too costly and contains too many exclusions to deter them from form-

ing Equitime.

Ms. Abraham said her own group is looking at both property and liability terrorism coverage issues, as it has become more difficult for United Educators member institutions, particularly large research-oriented universities, to obtain those coverages from insurers since Sept. 11.

"Clearly there's a liability issue as well as a property issue for terrorism," she said. "So we are looking at the large research universities and whether they could be possible targets and possible weapons."

"We're taking that on as an issue to try to understand and try to provide coverage where we think it's prudent or try to find another alternative," Ms. Abraham said. "The property in many ways might be easier for us, because we know these campuses so well."

Captives: Increased activity

Continued from page 10

tivity, is the hard property market, according to Mr. Betterley.

"The '80s hard market was casualty driven, which lends itself quite well to captives and risk retention groups," he said. "This hard market is more across the board, with a property component to it."

Mr. Betterley said it's difficult to put property programs in captives unless the company's property is well spread out among numerous locations.

"The people who have five locations and high value are having a hard time solving their property insurance problems with a captive," he said.

Still, while increased captive use is across the board in terms of types of coverage, the amount of property activity is a distinguishing factor of the current wave of captive use, many say.

"Nobody's done much with property in captives in years," Quest's Mr. Dove said. "And we have seen some inquiries in that area."

"We had a group of property owners looking at forming a group property captive," said Gary Osborne, senior vp at USA Risk Group in Montpelier, Vt. "Normally, you see nothing on property. Right now we've seen six wanting to do property. That's a sea change."

"Property's a big driver," of the current wave of captive activity, Mr. Osborne said, noting that property owners are looking to respond to market conditions forcing them to take higher retentions or structure property programs in layers.

Among those considering forming a captive are several members of the Real Estate Board of New York, a group representing some of the city's largest property owners, who also have extensive holdings elsewhere in the country. That group is considering forming a captive to write their working layer property and casualty coverage. (BI, April 15)

"A number of people have been sending in their information, their

property holdings and experience," Deborah Beck, executive vp of the Real Estate Board, said of the status of that proposal. "It's moving along."

She estimated the group should know in a week to 10 days whether there is sufficient interest to move forward with the captive proposal, which is being developed with Aon Risk Consulting Inc. If formed, the captive would be domiciled offshore.

"We have gotten a number of

'Reinsurers are occupied by their own problems, so it's more difficult for captives to find reinsurance.'

Richard S. Betterley
Betterley Risk Consultants

calls from owners of very large property portfolios around the country saying that they would be interested in participating," Ms. Beck said. "So if we could get the core group in New York, it should go nationally pretty quickly," she said.

Separate from the Real Estate Board members' captive proposal, "There is a group interested in getting together to address some of the terrorism insurance issue," Ms. Beck said. "I think they're just in the exploratory stages and haven't gotten very far."

But, she said, placing terrorism coverage for major properties in a captive appears difficult.

"The need for coverage is so much greater than the amount of capital that can be put at risk without some form of backup," Ms. Beck said.

Mr. Betterley agreed that it would be difficult to use a captive for property terrorism coverage. "That's going to be tough because of the need for big value," he said. "A captive can help with the price, but not the capacity so much."

While captives are an attractive alternative to the hard traditional market, a hard reinsurance market is creating some problems for captives.

"Reinsurers are occupied by their own problems, so it's more difficult for captives to find reinsurance," Mr. Betterley said. "It's true you can pull the reinsurance together, but it's a lot more expensive to do it. It's slow. It's hard work. It takes a lot more time."

"Reinsurance is a problem. They're asking for a lot more data," Mr. Osborne said. "If you're doing workers comp, payroll by class by state isn't enough anymore. There's a big push for concentration details."

And, he added, "There's a real reluctance to offer statutory limits."

"I think there's only two reinsurers that will do statutory," Mr. Osborne said. In the current market, "You have to sort of go in and layer your workers comp coverage," he said.

And the new capacity that has come into the market hasn't been much help to captives, he said, as the reinsurers are demanding high attachment points.

"The new Bermuda money hasn't really helped the alternative risk market because it's up in the stratosphere," Mr. Osborne said. "We're having to find more capital (from) day one because we're having to retain more to do these."

Liberty's Mr. Kehler said he thinks most of those being driven into the captive market now are likely to remain when the traditional market softens. "Companies who look to a captive as an alternative typically stay in the captive long-term," he said.

"Even in the great insurance giveaway, as I call it in the decade of the '90s, there was still positive captive growth," Mr. Kehler said. "As rates tend to flatten over the next few years—and you may even see a backsliding in rates—I think you'll still see growth in the captive market."

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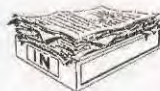
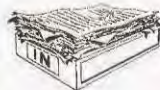
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International

Queensland, NSW consider tort reforms to curb rising cost of liability coverage

By DAMIEN TOMLINSON

BRISBANE, Australia—State governments in Queensland and New South Wales have proposed legislative reforms designed to reduce personal injury litigation and combat rising public and medical liability insurance rates.

The reform proposals both call for caps for damages in personal injury lawsuits, liability immunity to some volunteer and sporting associations and a ban on attorney advertising.

Earlier this year, Australian state government officials gathered at a national summit in Canberra to discuss strategies to stem an affordability crunch for liability insurance (*BI*, April 8). The demise of Sydney-based HIH Insurance Ltd. and the Sept. 11 terrorist attacks have accelerated rate firming in the Australian market, and rate hikes for some risk managers renewing earlier this year have more than tripled.

Queensland Premier Peter Beattie announced the

proposed reforms early this month, saying the liability insurance system is experiencing "urgent problems" and is in danger of collapse. "We've got doctors who are reluctant to operate, we've got not-for-profit organizations which can't hold fetes, and the whole social fabric in some country and provincial cities is starting to be put at risk," he said.

In January, the Queensland government formed an insurance taskforce to consider changes to the state's liability system. The taskforce reported its findings in February with a series of recommendations, which formed the basis of the proposed reforms announced by the premier.

Mr. Beattie noted that the purpose of the proposed reforms was not to stop injured people from receiving compensation. "Our reforms are not designed to limit compensation for people who suffer catastrophic disabilities. My message to people who have been injured is that if you've got a legitimate claim, you'll get a fair go."

See REFORM/next page



PHOTO: ALLSPORT

Queensland Premier Peter Beattie

World Updates

If P&C posts first-quarter loss

Scandinavian insurer If Property & Casualty Insurance Ltd. has posted a 421 million Swedish kronor (\$41.1 million) loss for the first quarter of 2002, largely as a result of reduced investment income. For the first quarter of 2001, If reported a pro forma profit of 43 million Swedish kronor (\$4.2 million). That figure reflects the Stockholm, Sweden-based insurer's merger with the property/casualty business of Sampo Insurance Co. Ltd. in January of this year. If's gross written premiums for the quarter were 14.60 billion Swedish kronor (\$1.42 billion), up 6.4% on a pro forma basis.

French employers must pay asbestos victims

Two French employers have been ordered to compensate a group of workers suffering from asbestos-related illnesses, in what is the first ruling to follow a high court judgement earlier this year that expanded employer liability for workplace injuries and illnesses. The amount of damages was undisclosed. The tribunal ruling follows a Feb. 28, 2002, decision by France's highest court, the Cour de Cassation in Paris, which ruled that employers could be held liable for injuries even though they had complied with existing employment law. The high court ruled that although the French government did not restrict the use of asbestos until 1997, a group of employers were guilty of negligence because they continued to use asbestos after its health hazards became widely known.

U.K. authorities reopen manslaughter probe

The United Kingdom's Crown Prosecution Service has asked the British Transport Police to conduct further inquiries into the October 1999 Paddington rail crash, raising the possibility that a charge of corporate manslaughter could be brought against Railtrack P.L.C., the operator of the U.K. rail network. The Crown Prosecution Service, which had earlier ruled out such a charge, has reopened investigations into the management of signaling at Paddington in light of the 2001 Cullen report on the accident. Lord Cullen's report blamed the crash, which occurred when a train driver passed a red warning signal, in part on a "lamentable failure" by Railtrack to respond to safety warnings before the accident.

See WORLD NEWS/ next page

NAIC to advise on Chinese regulations

By MICHAEL BRADFORD

KANSAS CITY, Mo.—Insurance regulators in the United States are set to offer advice to their counterparts in China, as that country continues to liberalize its insurance market and open it to foreign participants.

The National Assn. of Insurance Commissioners and the China Insurance Regulatory Commission on May 18 signed a memorandum of understanding whereby the two groups will exchange information on regulatory issues.

And under a technical assistance program, the NAIC will provide help to Chinese regulators, who have less experience overseeing free-market insurers, said Lawrence H. Mirel, who is insurance commissioner for the District of Columbia.

"We've been regulating insurance for 150 years, and the Chinese have been at it for just four or five years," he said. "We have a lot of experience, procedures and systems that can really help them."

Mr. Mirel, who helped develop the technical assistance program and who was an NAIC representative at the signing of the agreement at the group's

Kansas City headquarters, said the association will help the Chinese develop model laws and regulations, compile examination handbooks, and collect and analyze data, among other steps.

There may also be exchanges of personnel to help train Chinese regulatory staffers, Mr. Mirel said.

The commissioner said insurance buyers in China will benefit from a tighter regulatory scheme. "Any rules and regulations that govern insurance, which is a long-term product, are going to benefit buyers," he said. "You want to make sure companies are solvent and can pay claims."

Insurers welcomed the agreement. "A cooperative and mutually beneficial relationship between the NAIC and CIRC will strengthen the Chinese insurance market and help Chinese insurance consumers," John Savercool, vp-federal affairs for the Washington-based American Insurance Assn., said in a statement.

Mr. Savercool also said that U.S. insurers operating overseas "are able to compete more effectively in open and well-regulated markets. We support efforts to modernize undeveloped insurance markets around the world."



PHOTO: COURTESY OF THE NAIC

Terri Vaughan, president of the National Assn. of Insurance Commissioners and Iowa's insurance commissioner, signs an agreement with Feng Xiaozeng, vice chairman of the China Insurance Regulatory Commission.

Lloyd's to encourage outside investment

By SARAH VEYSEY

LONDON—Lloyd's of London plans to allow individuals and institutions to invest in Lloyd's without becoming members of the market, Lloyd's Chairman Sax Riley announced.

Currently, corporate capital providers and individual investors—or names—must become members of the Society of Lloyd's to invest in the market. The proposed change aims to make it easier for investors to enter and exit the market, as the nonmember investors would not face claims for open years—or those for which ultimate liabilities have not been calculated—after leaving the market, a Lloyd's spokesman said. Lloyd's members, in contrast, are exposed to all claims for open years.

Mr. Riley said that during discussions on pro-

posed reforms of the Lloyd's market, Lloyd's had decided "to encourage the development of a range of Lloyd's investment schemes by market players, aimed at attracting new capital on a non-membership basis."



Mr. Riley

He said that some investors were interested in providing capital but did not wish to be Lloyd's members.

To enable non-member investors to participate in the market, Lloyd's may accept investments

through special purpose investment companies that would allow investors to buy bond- or equity-based investments, Mr. Riley said.

Speaking at the annual meeting of the Assn. of Lloyd's Members in London on Friday, Mr. Riley said the investment vehicles could be in place by the start of 2003.

The introduction of nonmember investment would help Lloyd's increase its capacity from its current record level of £12.2 billion to the £20 billion (\$17.44 billion to \$28.60 billion) it needs "to play at the table it plays at," Mr. Riley told the meeting's more than 250 attendees.

The Lloyd's reform proposals, put forward by Chairman's Strategy Group, are currently under review by market participants (*BI*, Jan. 28), and a vote on the reforms will take place later this year.

Reform: Australian states to consider tort changes

Continued from previous page

Among the proposed reforms for Queensland are requirements for early claim notification after injury or the appearance of symptoms and the introduction of limits on how long defendants and insurers have to make liability determinations. Under the proposals, exemplary, punitive or aggravated damages, all of which are noncompensatory damages, could not be awarded against insurers, and judges would decide all personal injury cases, instead of juries.

In addition, plaintiff attorneys would no longer be able to advertise so-called "no-win, no-fee" legal representation, in a bid to discourage frivolous lawsuits. In such arrangements, a lawyer agrees that he or she will not receive a fee if a case

is lost. In exchange for assuming this risk, the lawyer is entitled to a bonus on top of standard fees if the case is won.

"While we will restrict no-win, no-fee advertising, we don't plan to abolish the no-win, no-fee process, because that enables a lot of people without money to access the courts," Mr. Beattie said.

Queensland will establish a task force to coordinate the final formulation of the bill, which likely will be introduced to the state's Parliament next month.

The New South Wales Parliament also will soon consider legislation to reduce liability costs.

That proposal, the Civil Liability Bill, would limit damages for pain and suffering and loss of amenity—or diminished quality of life—

awards to \$350,000 Australian (\$192,500). In addition, awards for lost income would be capped at \$2,712 Australian (\$1,492) per week, which is in line with current restrictions for damages in motor vehicle and health care lawsuits. Previously, there were no other statutory caps on damages or loss of income awards.

In addition, punitive damages would be abolished. If a damages award is for less than \$100,000 Australian (\$55,000), attorneys could charge no more than \$5,000 Australian (\$2,750), and attorneys would be required to pay the costs of a lost case if the court determines that there was a high chance of failure.

New South Wales Premier Bob Carr said the legislation, which will

be introduced in Parliament on May 28, would be retroactive to March 20, 2002.

"We are making new laws so communities can have affordable insurance cover," Mr. Carr said. "This should see an end...to 'ambulance chasing' lawyers wasting time and money on speculative lawsuits."

In addition, both New South Wales and Queensland have proposed "Good Samaritan" legislation, aimed at indemnifying volunteers from personal liability for injury. For example, under the proposals, parents coaching children's sports leagues would not be liable if an injury occurs.

Bruce Ferguson, president of the Sydney-based Assn. of Risk & Insurance Managers of Australasia and

risk and insurance manager for Sydney Water Corp., said the proposed reforms in Queensland and New South Wales should help curb rate increases for liability coverage.

However, the introduction of damages caps could lead to poorer risk management, he said.

"I query whether capping general damages will see a relaxation of risk management by companies believing they are protected," Mr. Ferguson said.

And the proposals are unlikely to lead to lower insurance rates, he said.

"Insurance prices currently are more a reflection of a hard insurance market than a profiteering insurance industry. The reforms will benefit most policyholders, but I do not foresee a reduction in rates," Mr. Ferguson said.

Risk managers and insurers earlier this year called for tort reform to curb sharply increasing liability insurance rates (*BI*, Feb. 4).

David Muir, insurance group national head at Sydney-based Deacons Lawyers, said the differing laws in border states Queensland and New South Wales would see litigants trying to raise actions "in the jurisdiction most beneficial to their case".

Currently, none of Australia's states or territories have caps on damages.

Mr. Muir also said the Queensland law would be more beneficial to stabilizing the insurance market, as it aimed to reduce small claims, which were the "death by 1000 cuts" for insurers.

By contrast, in New South Wales, "Mr. Carr has taken aim at reducing the perverse judgments we sometimes see, without taking consideration of the much more prevalent smaller claims which are the real cause of soaring insurance rates," Mr. Muir said.

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(Under an Order for Winding-Up the above-named Company, dated 5th February, 1991.) NOTICE OF INTENTION TO PAY A DIVIDEND NOTICE IS HEREBY GIVEN that Focus Insurance Company Ltd. - In Liquidation ("The Company") intends to declare a first and final dividend on 22 July 2002, under the provisions of Rule 84 of the Companies (Winding-up) Rules 1982.

All known creditors have been sent a notification by Focus Insurance Company Ltd. - in Liquidation of the basis upon which their dividends will be calculated. Creditors who have not received such notification, or who do not agree with the basis of calculation of their dividend should submit a completed Proof of Debt form to the Liquidator of Focus Insurance Company Ltd. - in Liquidation, PricewaterhouseCoopers, Dorchester House, 7 Church Street, Hamilton HM 11, Bermuda on or before 5:00 pm (Bermuda time) 12 July 2002. Failure to notify the Liquidator in writing of your disagreement with the basis of calculation, by submitting a Proof of Debt form, on or before 12 July, 2002, will result in your exclusion from participation in payment of the dividend to be declared.

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World Updates

Continued from previous page
Briefly noted

Lloyd's of London insurer Cox Insurance Holdings P.L.C. raised about £66 million (\$96.2 million) in an April 26 offering of ordinary shares. Cox said that it sold about 90% of the 177.8 million shares offered, at 41 pence (60 cents) per share. Cox earlier had said it planned to raise about £70 million following an announcement in March that it would exit commercial property and reinsurance to focus on personal lines....Zurich, Switzerland-based Swiss Reinsurance Co. has been granted approval to open a service company in India. Swiss Re said it planned to offer risk management and product-design consulting to Indian insurers and financial institutions through the company, Swiss Re Services India Private Ltd.

Products & Services

St. Paul offers coverage for investment advisers

ST. PAUL, Minn.—The St. Paul Cos. Inc. is offering a new professional liability insurance policy for investment advisers. St. Paul SelectOne for Investment Advisers includes coverage for directors and officers, employment practices, fiduciary liability, mutual fund professional liability and private investment fund general partnership liability. Only investment advisers who are registered with the Securities and Exchange Commission are eligible for the coverage.



Limits can be written to \$25 million, above deductibles that will range from \$25,000 to \$500,000 depending on the size of the account.

John Kearns, president of St. Paul's Financial & Professional Services unit in St. Paul, Minn., said in a statement that the coverage is designed to meet all the professional liability needs of investment advisers. "This type of approach will reduce the potential for coverage gaps and keep the costs down for our policyholders," he said.

More information is available from Eileen Purcell at 617-371-0294 or purcell@stpaul.com.

Aetna to launch plans for small businesses

HARTFORD, Conn.—Aetna Inc. in July will begin offering a new suite of health benefits aimed at small businesses in five states.

The new standardized product line will be available to employers with fewer than 50 eligible

employees in California, Florida, New York, Pennsylvania and Texas. Additional markets will be added throughout the year, according to Hartford, Conn.-based Aetna.

The plans can include up to a dozen health plans per state as well as dental, life and short-term disability products. Members will be able to manage their benefits online through Aetna's Navigator service.

"The 2.5 million small-business employers in this country have a unique set of needs when it comes to providing health benefits to their employees," said William Roth, senior vp of the Aetna Small Business Group.

He said the new product line "is designed to offer streamlined plan options, simplified enrollment and customer service, and one-stop shopping."

Employers can get more information on the plans from Jeff Crippen, head of sales for the Aetna Small Business Group, at 860-273-4140.

Liberty Mutual booklet outlines comp strategies

BOSTON—Liberty Mutual Insurance Co. is offering a booklet that lists some proven strategies for

reducing workers compensation costs.

The 16-page booklet provides short case studies that describe a client's workers compensation problem and discuss how it was corrected. For example, one strategy discussed is the early reporting of claims. The accompanying case study explains that an industrial company had found that the reporting times for its disability claims were much higher than the industry norm. Streamlining the reporting process reduced the company's average cost per claim by \$6,741.

Other strategies addressed include identifying where accidents are likely to occur, putting proactive claims management strategies in place and using provider networks and medical bill reviews.

Copies of the booklet are available from Boston-based Liberty Mutual by calling 800-454-2378, ext. 81.

Marsh offers services for gaming industry

ATLANTIC CITY, N.J.—Marsh Inc. has established a new practice to provide insurance and risk management services to the



gaming industry.

The New York-based brokerage has named Steven J. Batzer, senior vp, to head the new practice, which is based in Atlantic City, N.J.

Hotel casinos, particularly those in coastal areas, face some unique challenges, according to Mr. Batzer. "With the market in the condition it is in now, capacity and pricing are both major issues" for property coverages on locations that, in some cases, face not only such "normal" risks as fire exposures, but also windstorm and hurricane threats, he said.

Dockside casinos also face the unique exposure of being both a land-based and marine risk, Mr. Batzer pointed out.

More information the new practice and the risk management services offered is available from the Marsh office in Atlantic City at 609-641-8880.

Life: Reinsurers hike cat prices, tighten terms

Continued from page 1

Kan. Consequently, he said, the marketplace is operating in uncharted terrain.

The Sept. 11 attacks caused an estimated \$2.70 billion in life insurance losses, according to Robert Hartwig, chief economist for the Insurance Information Institute in New York.

As a result of those losses, many life reinsurers have curbed their underwriting of catastrophe coverage. This pullback is occurring just as many group insurers are looking to retain less of this risk.

"A lot of the reinsurance capacity that had been the norm really dried up and went away," said Rob McGinnis, executive vp and chief operating officer of group operations for CNA Insurance Cos. in Chicago.

Much of the capacity for life catastrophe reinsurance is written outside the United States, as non-U.S. companies dominate the life reinsurance market overall.

'A lot of the (life catastrophe) reinsurance capacity that had been the norm really dried up and went away' after the Sept. 11 terrorist attacks.

Rob McGinnis
CNA Insurance Cos.

Partly because of the more limited supply of catastrophe reinsurance coverage for life risks, and because of the increased exposure, prices for group life reinsurance are skyrocketing.

Rates are up from five to 10 times the expiring rates for group life reinsurance, according to Pamela Saunders, chief executive officer of Disability Consulting Group L.L.C. in Portland, Maine, a reinsurance underwriting manager.

"It's very clear that rates are going up," said Frolly Boyd, senior vp, group insurance at Aetna Inc. in Hartford, a leading group life insurer. While Aetna has not yet received a quote for its catastrophe coverage renewals, she has heard that some contracts are renewing at seven to 13 times "what they were, with terror exclusions."

Besides reinsurance rates going up, for the first time the catastrophe reinsurance contracts exclude deaths from terrorist acts. This includes any death from a bioterror-

ist act, such as an anthrax attack, in addition to deaths from other terrorist attacks involving nuclear or chemical weapons.

"Bioterrorism seems to be in every contract," Ms. Saunders said.

In addition, she noted that cat life policies now include caps on the amount of coverage for deaths arising from a single event, such as \$10 million to \$25 million per event.

Mr. McGinnis noted that, in the past, coverage of up to \$200 million per occurrence was available. "Now, you may have \$10 million or zero," he said.

Group life insurers are not yet passing on their higher reinsurance costs and retentions to employers. However, one requirement of reinsurers—demands for more information about concentrations of covered lives—is already trickling down to employers.

Before Sept. 11, this was not a concern, as reinsurers priced their coverage based on actuarial estimates of mortality. But the terrorist attacks showed that many deaths can occur unconnected to the mortality tables, said Mr. von Moltke of Employers Re.

To better evaluate their risk, reinsurers want to know where the covered lives sit during the day, he explained. This applies not only to whether they are located in "highly concentrated areas," such as business districts of cities, but also what individual buildings they are in, he said.

As a result, new rates are being established that combine the mortality risk "plus the rate for this concentration of risk," Mr. von Moltke said. Those risks with a large concentration of personnel

face a higher rate for coverage, he said. And those that don't provide the information also can be hit with higher rates.

"They will be charged as if they have a high-exposed risk," he said.

Because of these changes, employers are likely to see higher rates for group life coverage in the future.

With reinsurer losses from Sept. 11 and their rates going up, "eventually the consumer will pay the price for that," said Richard Travers, managing partner of Travers, O'keefe, a benefit consultant and broker in New York.

The increased cat costs "have to be built into pricing" of group life insurance, said Ethel Brightwell, a vp with Employers Re in Overland Park, Kan.

Until those costs are passed along to buyers, group life insurers are being squeezed by higher reinsurance costs and are retaining terrorism risks without coverage.

"This gap is where we don't have coverage and the exposure is all but unlimited," said Mr. McGinnis of CNA.

To address this concern, about a dozen large group life insurers have joined forces to lobby state and federal lawmakers for a federal reinsurance pool for life insurers, similar to what has been proposed for property/casualty insurers, said Aetna's Ms. Boyd. So far, though, those efforts have yet to produce any legislative proposals.

For now, group life insurers are also unable to pass along to employers the same terrorism exclusions they are receiving from rein-

LARGEST WRITERS OF NORTH AMERICAN LIFE REINSURANCE

Ranked by 1999 net premiums written

1. Swiss Re
2. Reinsurance Group of America
3. Employers Re
4. Transamerica Re
5. ING Re

Source: A.M. Best Co.

urers.

This hinges on whether state regulators will permit group life insurers to exclude terrorism from their policies, Ms. Boyd said. Such a plan faces an uphill struggle, as the National Assn. of Insurance Commissioners issued a statement in March saying the exclusions are uncalled for in life policies.

"It is the sense of the NAIC membership that terrorism exclusions are not necessary for individual life and health products and are generally not necessary to maintain a competitive market for group life and health products. They also may violate state law," NAIC President and Iowa Insurance Commissioner Terri Vaughan said in a statement.

Ms. Boyd acknowledged that any exclusions will come about slowly.

"This may be a state-by-state issue," she said.

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NCCI issues symposium

Observers perplexed by U.S. inaction on terror cover

By MEG FLETCHER

ORLANDO, Fla.—The U.S. Senate's failure to adopt a proposed federal backstop for insurer losses from future terrorist attacks is frustrating many representatives of the workers compensation industry.

Insurers are "guardedly hopeful" that there may be progress soon on such a measure, NCCI Interim President and Chief Executive Officer Chapin Clark said at the NCCI's annual meeting in Orlando earlier this month.

Privately, though, several attendees at the meeting questioned

whether federal relief for insurers would ever become a reality. The measure currently is stalled in the Senate over efforts to couple it with tort reform.

Many key industry representatives find the lack of progress particularly galling because there is broad-based support for a federal relief program from insurers, brokers, agents, regulators, employers and labor unions, as well as within the Bush administration.

Mike Pickens, vp of the National Assn. of Insurance Commissioners

and insurance commissioner of Arkansas, told the group: "I've supported the federal backstop and have never seen it as a handout."

The best approach for providing federal protection to insurers is most likely a federal excess-of-loss reinsurance arrangement, said J. David Cummins, professor of insurance and risk management at the Wharton School at the University of Pennsylvania in Philadelphia, who spoke at the conference. Federal officials also could facilitate the development of

a market for securitizing and transferring terrorism risk, he suggested.

Mr. Cummins said that even without immediate legislative action, there is an "implicit federal guarantee" for authorities to provide help to insurers if losses from future events reached \$70 billion to \$100 billion, because they would have no other choice if they wanted to prevent the collapse of the private insurance industry.

But, in an interview, New York Insurance Superintendent Gregory V. Serio asked, "How does one book an implicit backstop?" It is not a firm commitment that the insur-

ance industry can rely on to conduct business, he said.

As a consequence, the industry is facing "a crisis of uncertainty," Mr. Serio said.

Meanwhile, the New York regulator praised the insurance community response to the Sept. 11 attack on the World Trade Center. Currently, insurers have paid more than \$17 billion in claims, he reported. In addition, only 221 complaints were made out of the 31,000 claims that have been filed to date, and many of those complaints had to do with trip cancellation insurance, he added.

NCCI: Comp problems reviewed

Continued from page 3

nally expected," the NCCI said in a statement. "The vast majority of losses were ceded to reinsurers and will not appear in the workers compensation line on a net-of-reinsurance basis," the statement notes.

The NCCI currently estimates ultimate Sept. 11 workers comp losses at \$1.3 billion to \$2 billion. It also estimates primary insurers' losses net of reinsurance at between \$300 million and \$1.2 billion, which would result in a 1% to 4% impact on the 2001 accident-year combined ratio.

Those statistics reflect current estimates that the attacks resulted in 3,084 deaths and around 4,000 injuries—considerably fewer than the

more than 6,000 deaths others originally estimated, according to Ron Retterath, a consulting actuary with the NCCI. Other factors also lowered the ultimate exposure of the workers comp system, including that 5% of the fatalities—mostly airplane travelers—were not work-related and 15% of the workers comp losses, including those for firefighters and police personnel, were self-insured. In addition, about 20% of the fatalities were single persons, and the New York comp system payout in each of those cases is \$50,000.

The NCCI expects additional claims, however, due to stress and respiratory ailments, the organization said in a statement.

But even though the direct losses likely will be lower than previously expected, the larger impact of the Sept. 11 attacks on the workers comp system has created a "drastic" situation, especially if a similar catastrophe occurs, Mr. Clark said.

"Primary workers compensation insurers must cover terrorism risk, but reinsurers can exclude it. Therefore, primary workers compensation writers have accepted concentrated financial risk with no way to spread it," he said. Before Sept. 11, "catastrophe reinsurance was available and inexpensive, all based on a belief that workers comp carried only a theoretical risk of unlimited loss and that the unthinkable could never occur. But it did occur."



In addition, current workers comp rates and loss costs contain no provision for terrorism-related catastrophes. Earlier this year, the NCCI sought a 4% increase in loss costs or rates for terrorism exposures in 34 states (*BI*, Feb. 18), but state regulators have not approved the filing. Regulators, in rejecting the filing, cited several concerns, including the appropriateness of applying the charge nationwide.

"Given the current level of underfunded exposure, another terrorist event on the scale of Sept. 11 could easily overstress capacity and drive numerous insurers into insolvency. This would, in turn, place intolerable pressures on the structure of insolvency mechanisms—pressures that would expose otherwise solvent workers compensation insurers to the very real threat of financial ruin," Mr. Clark said.

"Since insurers writing workers compensation must also participate in the sharing of potentially catastrophic residual market losses, they may have unlimited financial liability from this mechanism with no ability to underwrite or limit their risk selection as they can in the voluntary market," he said.

In effort to prevent catastrophic losses, workers comp insurers and reinsurers are demanding "an extraordinary amount of data," said Franklin W. Nutter, president of the Reinsurance Assn. of America in Washington. For example, underwriters now are requiring additional information on building location, operations and type of construction.

The deteriorating private market for workers comp risks has helped fuel growth in states' residual markets. Those state-mandated programs, which serve as workers comp insurers of last resort, grew by 74% to \$615 million in total premiums in 2001. Also, growth is continuing in the first quarter of 2002, as the number of newly assigned policies increased by 22% and premiums increased by 63%, compared with the first quarter of 2001.

Meanwhile, the cost of workers comp claims is up, including an 11% increase in the severity of medical claims in 2001.

Workers comp experts, however, continue to be encouraged by a decline in the frequency of lost-time claims, including a 4% decline in 2001, according to the NCCI.

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NCCI issues symposium

Meeting attracts 580

ORLANDO, Fla.—About 580 people attended NCCI Holdings Inc.'s annual issues symposium earlier this month in Orlando, Fla.

They heard a wide range of speakers—including NCCI executives, reinsurers, economists and investment analysts—discuss current market issues and workers compensation insurers' 2001 financial results during the meeting, which was held May 8-10 at the Hyatt Regency Grand Cypress Resort.

In addition, the organization's membership elected two new board members and re-elected 12 others. The two new members are David H. Long, chief operating officer for national mar-

kets at Boston-based Liberty Mutual Insurance Co., and Susan Rivera, president of ACE INA Holdings Inc.

The Boca Raton, Fla.-based NCCI plans to hold its next conference April 23 and 24, 2003, at the same location.

For additional information, contact the NCCI at 800-622-4123 or visit www.ncci.com.

The NCCI offers data-based products and services that enable workers compensation insurers and others in the industry to perform a variety of functions, including establishing loss costs, calculating experience rating modification factors and managing residual market mechanisms.





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Equitime: Airline RRG awaits clearance for takeoff

Continued from page 1

can International Group Inc., leader of a consortium offering war risk coverage—are urging the DOT to phase out its coverage of the airlines and not to provide any ongoing support to the RRG.

Equitime proponents, however, argue that federal reinsurance would not amount to a subsidy, since the RRG would pay for the coverage, and that the government's role would end in as little as two years as Equitime's surplus grows and commercial reinsurers return to the market.

"If the DOT wants a key part of the economic infrastructure healthy, the DOT and the government have to start looking at the financial crisis we are in," said Chris Duncan, vp-finance and chief risk officer for Delta Air Lines Inc. in Atlanta.

Noting that U.S. airlines collectively lost \$7 billion in 2001 and stand to lose another \$2 billion to \$3 billion this year, Mr. Duncan warned that the estimated \$1 billion industrywide cost of commercial market war risk coverage "could accelerate the insolvency of certain airlines."

Equitime's backers say that they are not sure when to expect a DOT decision on reinsurance, but that they hope to have the RRG up and

running by July 1.

Members of the Washington-based Air Transport Assn. of America and broker Marsh Inc. began developing the Equitime concept after aviation insurers drastically cut back war risk liability coverage in the wake of the Sept. 11 terrorist attacks. While major airlines typically had \$1.5 billion or more in war risk limits for both passenger and third-party liability before Sept. 11, insurers canceled the coverage after the attacks and reissued policies with a \$50 million sublimit for third-party risks.

The federal government then stepped in to provide coverage in excess of \$50 million under a program that the DOT has renewed every 60 days since last fall. The government has made it clear, though, that it wants private insurers to take over the coverage burden, and its latest extension of the program, on May 19, was for only 30 days. The Federal Aviation Administration, which administers the program, is also considering raising its \$7.50 per departure premium for the coverage and shifting to a per passenger charge, government and insurance industry sources say.

Two main commercial market options exist for third-party war risk insurance—the AIG-led consortium and a consortium led by German

insurer Allianz A.G. Holding and Berkshire Hathaway Inc.—but U.S. airlines view the coverage as inadequate and too expensive, and the DOT has continued its own program despite their availability.

The airlines' answer is Equitime, which would be open to the ATA's 22 U.S. members, the roughly 50 members of the Washington-based

'If the DOT wants a key part of the economic infrastructure healthy, the DOT and the government have to start looking at the financial crisis we are in.'

Chris Duncan
Delta Air Lines Inc.

Regional Airline Assn. and "critical subcontractors," such as ground handlers, refuelers, caterers and airport security companies.

Nine major airlines will become Class A shareholders of Equitime by contributing \$5 million each in start-up capital. They are Alaska Airlines, America West Airlines, American Airlines, Continental Airlines, Delta, Northwest Airlines, Southwest Airlines, United Airlines and U.S. Airways, said Scott Russell,

a Marsh managing director in Minneapolis and head of the broker's U.S. airline practice.

A second group of Class B shareholders, mostly smaller airlines, would contribute at least \$250,000 each, while Class C shareholders—mostly airline subcontractors—would contribute at least \$10,000, Mr. Russell said.

Equitime's initial gross written premium volume is projected to be \$450 million, and this, combined with its start-up capital, would allow it to sustain a loss of its full \$300 million retention immediately after opening its doors, Mr. Russell noted.

The RRG's premium rates would depend on the limits being purchased and other factors, but would amount to about 65 cents per boarding passenger for major airlines, a fraction of the cost of traditional market alternatives, he said.

The AIG consortium, for example, has charged \$1.85 per passenger for third-party limits totaling \$950 million excess of \$50 million. Coupled with the \$1.25 per passenger that aviation markets collect for passenger war risk coverage with its \$50 million third-party sublimit, this adds up to \$3.10 per passenger for war risk coverage.

John A. Myers, president and chief executive officer of AIG Avia-

tion Inc. in Atlanta, said the consortium's rates had dropped sharply and that AIG recently offered to write a \$1 billion limit for British Airways at a rate of \$1.00 per passenger.

AIG also maintains that government war risk backing amounts to an unfair subsidy for the airlines when commercial insurance is available.

"If you're playing with somebody else's capital," Equitime's 65 cent rate may be adequate, Mr. Myers said, referring to government reinsurance. But "if you are playing with your own capital, then (65 cents) sounds too low to me."

The RRG's backers, though, counter that commercial pricing not only is unaffordable but also that the terms of coverage—such as its \$1 billion limit, compared with Equitime's \$2 billion—are unacceptable to major airlines.

In any case, Equitime's growth will allow the government to withdraw as a reinsurer within as little as two or three years, backers say, and will prevent the DOT having to step in again as an emergency war risk insurer if another terrorist attack triggers commercial market cancellations.

"That's not anti-competitive, that's entrepreneurial," Mr. Duncan said.

D&O: Directors fear claims fight

Continued from page 1

D&O forms. The other limits pertain to reimbursement of a corporation for its costs of defending corporate leaders and to protection of the entity against securities litigation brought against the corporation itself.

The issue can arise because the corporate entity not only purchases the D&O policy but is a named insured. Such was the case in the Enron D&O dispute.

If a policyholder has insulated the coverage limits available for directors and officers, a bankruptcy judge is less likely to rule that a policy's entire limits belong to the bankruptcy estate.

One option is to address the issue through so-called D&O policy "Side A" coverage, said Steven Anderson, vice chairman of the FINPRO division of New York based Marsh Inc. Side A provisions specifically dedicate coverage limits for the defense of directors and officers.

Side A coverage typically is purchased in an excess policy that sits above a master D&O program. The master program, in contrast, often provides a single coverage limit for individual officers and directors, reimbursement of a corporation and entity protection against securities claims.

"So if you run into an Enron scenario, you would want the excess Side A coverage to drop down to become primary for defense purposes," Mr. Anderson advised. Some excess policies have long contained language stating that their Side A coverage will become the primary

layer and respond if the primary insurer does not pay a claim, he said.

But not all Side A policies respond that way, so purchasers should look carefully at the breadth of their coverage, Mr. Anderson advised.

Some excess D&O policies drop down and respond only when primary coverage limits have been exhausted, said Michael A. Rossi, a policyholder attorney for Insurance Law Group in Glendale, Calif. Risk managers, therefore, should specifically ask that the excess policy trigger be changed to include a bankruptcy filing, not just the exhaustion of primary limits, Mr. Rossi advised.

An alternative, he said, is to purchase primary D&O coverage with separate Side A limits.

Another option for risk managers is to require clauses in D&O policies in which an insurer agrees that if bankruptcy occurs, the insurer will allocate a certain percentage of a policy's limits for the defense of board members and will give them priority over the rights of the entity. At the same time, the entity agrees that it will waive certain rights to a policy during bankruptcy.

There is, however, an absence of case law determining how courts would rule on such language, insurers and policyholder attorneys agree. Even if such language is present in a policy, a bankruptcy judge could still rule that policy proceeds belong to the estate and not to individual officers and directors.

An option that D&O insurers advocate is to entirely remove entity

coverage from a policy. Insurers contend that most current coverage complications stem from inclusion of entity coverage in D&O policies. This practice, which insurers say was sought by risk managers, arose in the mid-1990s in response to shareholder lawsuits against corporations.

One risk manager who asked not to be identified said he would consider removing the entity coverage from his policy during renewal.

The risk manager recently created a memo detailing the D&O policy defense available for his company's board members. He was asked to do so by his company's corporate council after a board member grew concerned about available D&O coverage in light of the Enron bankruptcy scenario.

The risk manager reported in his memo that a D&O policy purchased from National Union Fire Insurance Co. of Pittsburgh, Pa., a unit of American International Group Inc., provides an "order of payment provision," giving directors and officers priority over the corporation.

The policy also contains a provision under which the corporation waives certain rights in bankruptcy so that funds would flow to directors and officers, the risk manager said.

But because there is no certainty that some state courts would uphold the provisions, the risk manager said he will consider removing the entity coverage from his D&O policy.

National Union in February 2000

began including the bankruptcy waiver language in its D&O policies because of an overall increase in bankruptcy filings, said John Keogh, president of National Union in New York. And Enron's bankruptcy has increased demand for such coverage considerations, he added.

Insurers rewording their policies to specifically address bankruptcy, however, could potentially use that change to deny coverage, said Ed

Joyce, a partner in the New York office of Heller Ehrman White & McAuliffe L.L.P. Insurers now could argue before a bankruptcy judge that coverage limits available under policies that do not contain such language should be the property of the estate.

In that way, insurers are spared from paying on a claim while the issue is tied up in bankruptcy proceedings. "I can just see that argument happening," Mr. Joyce said.

Zelig: Entity not liable

Continued from page 3

tion on a public property must stem from a physical defect as opposed to "being simply dangerous," said Mr. Fisher, who filed an amicus brief in the case on behalf of 115 California cities and the California State Assn. of Counties. He predicted the decision will lead to a reduction in the number of verdicts against public entities in California.

"I think probably public entities throughout the state breathed a big sigh of relief with the Supreme Court decision. It was a big case," said Stephen Shane Stark, county counsel for Santa Barbara County. Had the appellate court decision been upheld, it would have significantly expanded counties' potential liability by imposing a duty to provide protection not just in courthouses "but also possibly in other areas as well."

Tom Vance, risk manager for the city of Anaheim, Calif., said the decision will hopefully lead to more summary judgments dismissing charges against public entities in

cases where they are sued because an incident "just happens to occur on our property."

However, LeAnna Gutierrez, staff attorney at the Los Angeles-based California Women's Law Center, said the court should not have lumped the courthouse in with beaches and other public places when it ruled the state did not have to take special measures to protect Ms. Zelig.

Women are "repeatedly forced to go to court" on family law matters where they must confront their abusers, she said. "The state really needs to recognize that domestic violence is unique," and either provide these women with special protection or permit them to handle these legal matters remotely, said Ms. Gutierrez.

Dana E. Zelig, a minor, etc., et al., plaintiffs and appellants, vs. County of Los Angeles et al., defendants and respondents, Supreme Court of California, No. S081791

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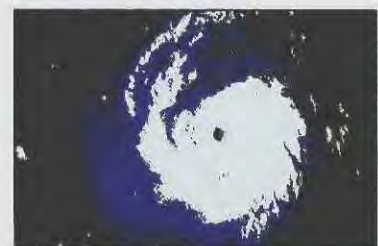


PHOTO: NOAA

Normal hurricane activity likely in 2002: NOAA

The 2002 Atlantic hurricane season will be marked by normal to slightly above normal activity, according to the National Oceanic and Atmospheric Administration. The NOAA forecast calls for nine to 13 tropical storms. Six to eight of those will become hurricanes, and two or three of the hurricanes will be strong enough to develop into major hurricanes. A "normal" Atlantic hurricane season sees 10 tropical storms, six of which become hurricanes, two of which are considered major hurricanes, according to NOAA.

U.K. rate hikes may not last, S&P says

Commercial property/casualty insurers in the United Kingdom have successfully implemented steep rate increases since the Sept. 11 terrorist attacks, but the clout of the larger brokers may prevent insurers from maintaining the hikes, according to Standard & Poor's Corp. The price increases should improve the historically poor profitability of U.K. commercial insurers in 2002, according to S&P, which has affirmed its "stable" outlook for the U.K. nonlife insurance industry. However, S&P noted that insurers may not be able to maintain the hikes in the longer term. "Whether the market can sustain the price increases remains to be seen, however, as commercial lines brokers remain a

powerful force in the sector and have historically been able to keep rates low for their clients," Simon Marshall, an associate director at S&P in London, said in a statement.

Comp costs down in 2000 relative to wages: Study

For the eighth consecutive year, workers compensation benefit payments and employer costs declined relative to covered wages in 2000, according to a report by the National Assn. of Social Insurance. The dollar amount of benefits and costs actually rose in 2000, but that increase was outpaced by higher wages. Total workers compensation benefit payments for 2000 were \$45.9 billion, a 6.5% increase over payments for 1999, while total employer costs for the year were \$56.0 billion, a 2.9% increase over 1999.



PHOTO: KRI

Major League Baseball, Marsh settle dispute

Major League Baseball and Marsh & McLennan Cos. Inc. have settled a lawsuit alleging the broker failed to obtain adequate insurance coverage for the organization, a spokesman for Marsh said. The settlement was reached earlier this month before an appellate court reinstated the suit that was dismissed by a trial court in August 2001, the spokesman said. Terms of the settlement were not

announced. The suit arises from a lawsuit brought by a group of investors claiming that an executive associated with MLB in 1992 defamed them when the investors' attempt to purchase a professional baseball franchise was rejected. New York-based MLB settled the investors' lawsuit for an undisclosed amount. When MLB sought coverage for the settlement it discovered that defamation risks were excluded under its policy issued by Hartford Fire Insurance Co. The insurer, which had previously provided defamation coverage, had notified Marsh of the exclusion, but the broker did not notify baseball executives of the reduction in coverage or find replacement coverage, according to court papers. MLB then sued Marsh to recover its losses related to the investors' lawsuit.

Supreme Court to rule on vicarious liability

The U.S. Supreme Court agreed last week to decide whether real estate company officers can be held liable when their employees violate federal anti-discrimination laws. The case, *David Meyer vs. Emma Mary Holley, et al.*, involves the federal Fair Housing Act of 1968. Ms. Holley, who is African-American, and her husband, who is white, allege that a real estate agent employed by Triad Realty in Twentynine Palms, Calif., illegally discriminated against them when he canceled an offer they had made on a house and allegedly used racial epithets. They sued Triad Realty and the agency's owner, Mr. Meyer, for the agent's action. Although a federal district court granted summary judgment for Triad Realty and Mr. Meyer, a three-judge panel of the 9th U.S. Circuit Court of Appeals in San Francisco reversed the lower court's decision.

9th Circuit overturns coverage denial

Death caused by autoerotic asphyxiation is covered under an employer's group accidental injury and death policy, the 9th U.S. Circuit Court of Appeals ruled in a partial departure from other courts. In

Jorita Padfield vs. AIG Life Insurance Co. a three-judge panel of the 9th Circuit in Pasadena, Calif., unanimously ruled that a death caused by autoerotic asphyxiation is not a suicide. The majority also held that the death was not a self-inflicted injury, therefore making the claim eligible for coverage. Autoerotic asphyxiation is the practice of limiting oxygen flow to the brain, often with a noose, to heighten sexual pleasure.

Clark/Bardes forms new consulting practice

Clark/Bardes Consulting has formed a unit to focus on retirement plan design and compensation consulting. Bruce Benesh, former global head of Arthur Andersen L.L.P.'s human capital group, will be president of the Clark/Bardes unit, which will be based in New York. Mr. Benesh is one of 10 former Andersen staff to recently move to Clark/Bardes.

Marsh forms intellectual property practice

Marsh Inc. has established an intellectual asset management practice to provide consulting and related services to businesses seeking to manage risks related to

intellectual property. Joby A. Hughes, former president of Houston-based Litigation Risk Management Inc., is joining Marsh to head up the practice. Donald Birdsong, a managing director of New York-based Marsh and head of its risk consulting practice, said in a statement that the new operation is "highly complementary" to Marsh's existing intellectual property brokerage services.

Smith to succeed Mathis as Kempers chairman, CEO

William D. Smith will become chairman and chief executive officer of Kemper Insurance Cos. next year, replacing David B. Mathis, who is retiring. Mr. Smith, who currently is president and chief operating officer of the Long Grove, Ill.-based insurer, will become CEO on Jan. 1, 2003. He will then take on the additional title of chairman upon Mr. Mathis' retirement in April.



Mr. Smith

Online Poll [5/20 - 5/24]

Should the government subsidize COBRA premiums for workers who lost their jobs because of foreign competition?

Yes 25%

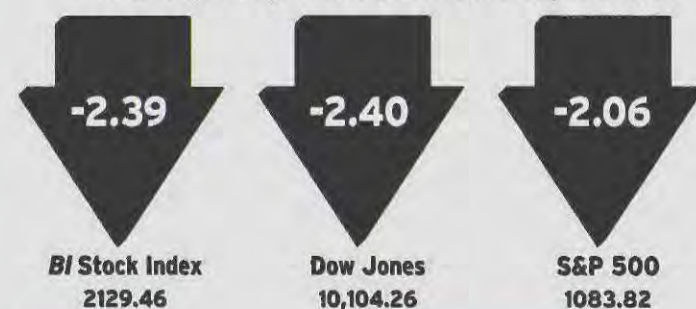
No 75%

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BI Stock Index [5/20 - 5/24]

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Percentage change of BI Stock Index vs. key indicators



Largest gains

Seibels Bruce Group
Tokio Marine & Fire
ACE Ltd.
AFLAC Inc.
Ohio Casualty Corp.

19.15%
7.84%
5.67%
4.16%
3.10%

Largest losses

Fremont General Corp. -20.86%
Unico American Corp. 18.10%
NYMagic Inc. 11.43%
Baldwin & Lyons Inc. -11.00%
PMA Capital Corp. -10.30%

Weekly change by market segment

Brokers 56.67%
Insurers/Reinsurers 33.76%
Managed Care Organizations 29.50%

Source: CNET Investor (investor.cnet.com)

WEF: Terrorism risk examined

Continued from page 2
to it. But the new terrorism, exemplified by the Sept. 11 attacks on the World Trade Center and the Pentagon and the coordinated hijacking of four jets, represents a new, previously underestimated threat.

"We have to expect that the next" terrorist act could happen anywhere in the world and perhaps involve simultaneous events at multiple locations, he warned.

And that action could be quite horrific, noted J.M. McConnell, a vp with Booz Allen Hamilton in McLean, Va., and former head of the National Security Agency. "Information is the capital of this century," and it's vulnerable to attack, he said. "It's a matter of time" before terrorists figure out a way to combine a cyber attack with a chemical, biological or nuclear at-

tack, predicted Mr. McConnell. He added that his greatest fear is that terrorists will detonate a so-called "dirty" nuclear device in Washington "sooner rather than later."

'I think (bioterrorism) has got to be the big risk.'

Grahame Chilton
Benfield Grieg Group P.L.C.

In an interview after his formal presentation, Mr. Chilton expressed concern about the bioterrorism threat, as well. "I think bio's got to be the big risk" because it could spread rapidly, he said.

During a question and answer period, the panel's other speaker predicted that property/casualty insurance prices will probably stabilize in

a year or so.

But Roger Egan, president and chief executive officer of Marsh & McLennan's North American operations in New York, added that insurance prices would likely stabilize at a level higher than those of a year ago. He also said that certain lines of coverage, such as professional liability coverage for Big Five accounting firms and terrorism insurance, would remain problems.

William G. Little, president and CEO of Chicago-based Quam-Nichols Co., moderated the discussion, which took place at the U.S. Chamber of Commerce in Washington.

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