

Business Insurance

Reporting Weekly on Corporate Risk, Employee Benefit and Managed Health Care News / \$4

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IBM to increase number of workers allowed to choose pension plan

ARMONK, N.Y.—Under intense employee and political pressure, IBM Corp. last week said it will more than double the number of workers who can stay in its traditional pension plan or move into the company's new cash balance pension plan.

About 65,000 employees who were at least 40 years old on June 30 and had 10 years of service can choose between the two plans. Previously, only about 30,000 employees who were within five years of retirement eligibility could make the choice.

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Floyd's bark worse than bite

By AMANDA MILLIGAN,
MARK A. HOFMANN
and SALLY ROBERTS

Fearful of a storm rivaling the potency and destruction of Hurricane Hugo in 1989 and Hurricane Andrew in 1992, risk managers with operations in the predicted path of Hurricane Floyd prepared for the worst and hoped for the best.

Depending on the storm's track, initial damage predictions before landfall by some forecasters had ranged between \$3 billion and \$12 billion.

Steve Goldstein, senior vp of the Insurance Information Institute in New York, said the computer models used by the III initially projected potential losses from the hurricane to be in the range of \$3 billion to \$4 billion. As of late Friday, however, the III was suggesting insured losses could be turned out to be far lower.

Mr. Goldstein pointed out that much of the damage that occurred in the Mid-Atlantic region stemmed from flooding, which is not generally covered by private insurance.

"It's not the storm of the century. It might not even be the storm of the year," Mr. Goldstein said.

EQECAT Inc. estimated late last week

that Hurricane Floyd caused between \$1.5 billion and \$2.5 billion in private-sector property damage.

"We were very fortunate that this storm's power reduced from its earlier levels of 140 miles per hour—and higher—as it neared landfall," said Mike Vallejos, senior vp for the subsidiary of San Francisco-based EQE International. The fact that the hurricane avoided a direct hit on Florida reduced damage potential significantly, Mr. Vallejos said.

Using its catastrophe modeling software, E.W. Blanch Co. Inc. estimates that Hurricane Floyd will cost the insurance industry between \$1 billion and \$1.5 billion in wind-storm damage in Florida, the Carolinas and the Northeast, said William Ashley, executive vp-risk analysis technology division in Minneapolis.

After assessing damage to their properties, many risk managers said they believe they were spared the full wrath of Hurricane Floyd. At one point, the storm was 600 miles wide and classified as a Category 4 hurricane on the Saffir-Simpson scale of strength, which extends up to Category 5.

"Fortunately, the storm didn't do the damage we anticipated," said Iris Owen, director of risk management for Pizza Inn. The

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API/WIDE WORLD PHOTOS; NOAA

Insured losses from Hurricane Floyd are expected to be light, as much of its impact will be felt from flood damage, most of which is not covered by private insurance.

Online frontier brings new risks

By JUDY GREENWALD

Companies that do business over the Internet are boldly going where no one has gone before.

But while cyberspace is exciting territory, it is hardly free of risks. So-called e-commerce companies face a panoply of risks—some entirely new, and others that take on added importance when compared with the risk profiles of traditional companies.

In response, insurers, brokers and consultants are struggling to help these rapidly evolving companies deal with the liabilities they may encounter as they forge ahead.

The biggest challenge is

the risks traditional insurance does not address, said Steven J. Peterson, senior risk management specialist for Dodgeville, Wis.-based Lands' End Inc., whose \$61 million in Internet business last year, while only a small portion of its \$1.3 billion in total revenues, was triple 1997's total. "There's no precedent," he said, pointing to the rapid rate of change in the business.

Broadly speaking, e-commerce companies fall into two categories: Relatively new "dot com" companies whose existence is based online, and "brick and mortar" companies that have ventured onto the Internet to try and augment their regular business activities.

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Online shopping accounts for a growing portion of Lands' End's revenues and risk management.

Rendez-Vous

Rates at bottom, reinsurers hope

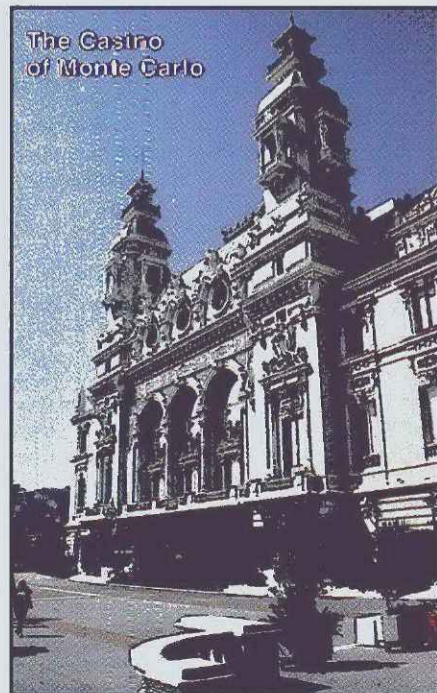
By PAUL D. WINSTON
and GAVIN SOUTER

MONTE CARLO, Monaco—Reinsurer executives agree that the era of declining rates is at last coming to an end, though they are far less unanimous as to when—and by how much—rates will begin to rise.

The global reinsurance industry still is awash in capital, and several executives and analysts say that a significant withdrawal of that capital would be needed before the reinsurance market truly hardens. More than one person suggested such a catalyst could come in the form of a multibillion dollar hurricane, unaware that only a week later Hurricane Floyd would be bearing down on the East Coast of the United States.

Several reinsurance companies are not waiting for external forces to alter market conditions, however. A handful of market leaders have unveiled formal plans to cut unprofitable business, re-

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Updates

IBM extends pension choice

Continued from previous page

IBM had been the target of intense criticism from older employees who said the new plan was much less generous than the old plan and could cost them hundreds of thousands of dollars in pension benefits. The old plan offers full, unreduced benefits after 30 years of service, a feature the cash balance plan lacks.

IBM's change in policy comes as the company is to testify this week before a Senate committee examining whether cash balance plans discriminate against older employees.

Separately, IBM will pay \$15.5 million to settle a suit charging that it unfairly deprived about 340 retirees of pension benefits when it enhanced its plan shortly after enrolling them in an early retirement program.

The settlement follows a ruling by the 6th U.S. Circuit Court of Appeals that IBM had a duty under the Employee Retirement Income Security Act of 1974 to inform affected employees of the planned pension change. The 9th U.S. Circuit Court of Appeals recently reached a similar conclusion in a case involving Exxon Corp. (BI, Sept. 6).

IRS slows cash balance OKs

WASHINGTON—The Internal Revenue Service is slowing down—and may even temporarily stop—approval of cash balance pension plans.

Carol Gold, director of the IRS' Employee Plans Division, last week directed IRS regional offices reviewing employer requests for cash balance plan determination letters to seek technical advice from the IRS national office. A determination letter is a kind of IRS seal of approval employers typically seek when they set up a new pension program.

Ms. Gold's memorandum is an about-face for the IRS. Previously, regional offices were free to act on cash balance plan requests without review from Washington.

It isn't known how long this new IRS procedure, which benefit experts say could amount to a de facto moratorium on cash balance determination letters, will last.

The IRS' position on the plans, which critics say discriminate against older employees, could become better known this week when IRS chief counsel Stuart Brown testifies at a Senate Health, Education, Labor and Pensions Committee hearing on cash balance plans.

Pam Scott, a principal with PwC Kwasha in Teaneck, N.J., said the IRS' action could be the result of the intense political pressure it has received from members of Congress and negative media coverage of cash balance plan conversions.

"This has become a political issue of significance," said Frank McArdele, a consultant with Hewitt Associates L.L.C. in Washington.

Separately, the Equal Employment Opportunity Commission last week said it will launch an investigation of the plans to determine whether they violate age discrimination laws.

House to move on care bills

WASHINGTON—The House of Representatives likely will begin debating patient protection legislation during the first week in October.

House Speaker J. Dennis Hastert, R-Ill., wrote in a statement last week that there will be a "fair process" to consider a patient protection bill introduced by Reps. Charles Norwood, R-Ga., and John Dingell, D-Mich., a second bill sponsored by Reps. Tom Coburn, R-Okla., and John Shadegg, R-Ariz., and possibly other alternatives.

The Norwood-Dingell bill, which the managed care industry and employer groups fiercely oppose, would allow patients to sue health care plans for damages, including punitive damages, allowed under state law in coverage disputes. Employers, in certain situations, also could be sued.

The Coburn-Shadegg bill would allow patients to sue plans—after internal and external review processes have been exhausted—for unlimited economic damages. Limited non-economic and punitive damage awards would be allowed. In limited situations, employers also could be sued in coverage disputes (BI, Sept. 13).

In July, the Senate approved a bill that would not increase the liability of managed care plans in coverage disputes (BI, July 19). The Clinton administration, though, says the Senate bill is inadequate and would be vetoed.

Rep. Hastert has not yet endorsed a particular bill.

Alliance, NAI to talk merger

WASHINGTON—The Alliance of American Insurers and the National Assn. of Independent Insurers will begin talks regarding a possible merger of the two property/casualty insurer trade groups.

The NAI's board of governors approved the discussions last Thursday at a meeting in Washington, less than a month after the Alliance's board had done the same.

In a joint statement, Alliance President Rodger Lawson and NAI President Jack Ramirez said: "The principal reason for considering the creation of a new organization is to provide a more powerful voice on public policy issues impacting the property and casualty industry." The statement added, however, that "we cannot predict with certainty that the discussions will produce an agreement."

The Alliance and NAI decided a feasibility study of a possible merger more than 10 years ago but decided not to merge at the time.

The NAI is based in Des Plaines, Ill., and the Alliance is based in Downers Grove, Ill.

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Errors & omissions

• PXRE Reinsurance Co. was not included in the Aug. 30 Directory of International Reinsurers. A complete listing appears on page 41.

RRGs to fight Oregon

State regulators narrowly interpreting federal ruling

By JERRY GEISEL

SALEM, Ore.—Oregon insurance regulators' refusal to broadly accept a court ruling that they illegally prevented a risk retention group from issuing policies to members could force other RRGs to fight the same legal battle again and again, RRG advocates say.

Oregon insurance regulators said the federal Risk Retention Act protects their right to require that automobile dealers and distributors selling service warranty policies prove financial responsibility by purchasing reimbursement policies from "authorized" insurers and not from RRGs.

But U.S. Magistrate Judge Jan-

ice Stewart said the federal law did not give regulators any such right.

While a state can specify an acceptable means for a business to demonstrate financial responsibility, those "means" cannot "discriminate against all RRGs as a class," she ruled. Any interpretation of the law that prohibits an auto dealer or distributor from proving financial responsibility through the purchase of a reimbursement insurance policy from any RRG violates the federal Risk Retention Act, Judge Stewart ruled.

As part of her order, Judge Stewart barred Mike Greenfield, director of the Oregon Department of Consumer and Business

Affairs, from refusing to accept policies issued by National Warranty Insurance Co., RRG (a Risk Retention Group), as proof of financial responsibility.

Oregon regulators are appealing Judge Stewart's ruling to the 9th U.S. Circuit Court of Appeals, which last week heard oral arguments in the case. The state regulators say the ruling applies only to NWIC and not to other RRGs that write the same coverages.

"The suit was filed by one plaintiff. It was not a class action. The ruling applies" to NWIC, said Katherine Georges, an assistant attorney general at the Oregon Department of Justice, which is

See Oregon on page 50

Major disruptions seen

Typhoon hits Hong Kong

HONG KONG—The biggest typhoon to hit Hong Kong in 16 years has killed one person, injured 493 and caused major disruptions to the province's financial markets, schools, roads, airports and shipping.

Typhoon York, with wind speeds of 87 mph, struck Hong Kong about 7 a.m. Thursday. It is the biggest storm in Hong Kong since Typhoon Ellen in September 1983.

A spokesperson for the Hong Kong Federation of Insurers said there were not yet any estimates of insured damage resulting from Typhoon York. She said it is likely that the majority of losses stemming from the typhoon will be from business interruption.

Official reports from the Hong Kong government, formally known as the Hong Kong special administrative region of the People's Republic of China, indicate that damage was mainly confined to smashed windows in skyscrapers, broken scaffolding and signage and associated debris. More than 90 roads were closed due to fallen trees.

The government reports, issued Friday, said Hong Kong banks, financial markets, schools and government offices were closed all day Thursday but reopened on Friday.

A Chinese river cargo vessel, Tsang Hon 9039, sank in waters just off Hong Kong at about 11 a.m. Thursday, with all five crew members rescued by a government helicopter. Shipping and ferry services out of Hong Kong were suspended all day Thursday.

Service at Hong Kong's Chek Lap Kok airport was heavily disrupted by the typhoon. The government said a total of 468 flights were affected between 10

p.m. Wednesday and 11 p.m. Thursday, with 97 incoming and 80 outgoing flights canceled, 134 incoming and 151 outgoing flights delayed, and six incoming flights diverted.

Last month, a China Airlines aircraft crash-landed at Chek Lap Kok while attempting to land during Typhoon Sam, which had winds speeds of up to 76 mph (BI, Aug. 30).

—By Matthew MacDermott



PHOTO: AFP

Typhoon York, the strongest storm to hit Hong Kong since 1983, caused widespread business interruption.

Reinsurance intermediaries directory nears

Business Insurance will publish its annual directory of reinsurance intermediaries in the Nov. 1 issue, which will also feature a Spotlight report on current trends and issues in the reinsurance industry.

Companies must report gross revenues to be listed in the directory; intermediaries must derive

at least \$500,000 of their revenue from reinsurance brokerage to be included.

The directory includes both U.S.- and non-U.S.-based reinsurance brokers

Business Insurance publishes the directory as an editorial service; there is no charge to be listed. If your company meets the cri-

teria for inclusion but has not yet received the questionnaire, please request one from Directory Editor Kevin Edison at 312-649-5279. Questionnaires also may be printed from the BI Web site at www.businessinsurance.com/magazine/directories.html.

Questionnaires must be returned by Oct. 1.

Inside

• Opposition by state insurance regulators to risk retention groups not only violates the federal Risk Retention Act but also wastes both time and money on unnecessary litigation, one of this week's editorials says. **PAGE 8**

• Nearly a century before Hurricane Floyd, there was "Isaac's Storm." Mark A. Hofmann reviews Erik Larson's book about the 1900 hurricane that killed more than 6,000 in Galveston, Texas. **PAGE 36**

• The Lutheran Church, Missouri Synod, has used \$315 million in excess pension assets to set up a cash balance plan alongside its traditional pension plan. **PAGE 41**

• The directors of GIO Australia Holdings Ltd. are facing a class-action lawsuit from shareholders angered by what they allege is the insurance company's non-disclosure of large reinsurance losses. **PAGE 53**

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U.S. pact doesn't apply to U.K. workers: Panel

By AMANDA MILLIGAN

Multinational corporations may have a new legal hurdle to overcome if a U.K. employment tribunal's recent finding about maternity benefits withstands legal challenges.

The tribunal ruled that Elk Grove Village, Ill.-based United Airlines Inc. must follow U.K. maternity provisions for pregnant flight attendants domiciled or based in the United Kingdom.

Because the decision has yet to be released to the public in written form, however, U.S. and U.K. attorneys can only speculate about the impact it will have on employment practices and benefits packages at multinational corporations.

Frank Colosi, director of people services for United, said the airline currently has 50 pregnant flight

attendants domiciled in the United Kingdom. United will consider whether to appeal after it reviews the tribunal's findings, he said.

United's maternity policy is "longstanding," he said. "Everything we have today is policy or practice or contractually provided for between negotiations or discussions with the Assn. of Flight Attendants."

The AFA is a U.S.-based labor union representing 46,000 flight attendants at 26 international airlines.

In a statement on its Web site, the AFA said it would work with United to make changes in the maternity policy, and Kevin Creighan, AFA president based in London, maintains that "United can't thumb its nose at British law. It has to obey the law like every other company operating in the United Kingdom."

An AFA spokesman said the

United case is the first involving a major air carrier whose employees belong to the AFA. Employees of other major airlines, including American Airlines and Delta Air Lines, are not represented by the AFA, he said.

Mr. Colosi said that several tribunal hearings, taking place from 1994 to as recently as last month, have determined that British law doesn't apply to these employees. He conceded, however, that one flight attendant will be compensated for United's erroneous decision not to offer her alternative work while pregnant.

"We don't believe the U.K. law applies," said Mr. Colosi, who administers and negotiates collective bargaining agreements for the airline. "They are U.S. employees, and they have signed a pre-employment agreement that commits them to be recognized as U.S. employees, and represented by a U.S. labor union, and pay, work, rules

See **United** on page 58



Judge rules for policyholder

Owens Corning awarded almost \$13 million in settling D&O case

By DOUGLAS McLEOD

TOLEDO, Ohio—National Union Fire Insurance Co. of Pittsburgh, Pa., must pay \$12.8 million to Owens Corning to cover the costs of shareholder litigation against the asbestos producer's directors and officers, a federal judge has ruled.

U.S. District Judge David A. Katz this month awarded Toledo-based Owens Corning interest and court costs related to its 1995 settlement of the shareholder suit under a D&O policy it had with National Union, an American International Group Inc. unit. National Union also was ordered to pay attorneys' fees and interest.

Lawyers for the insurer and AIG officials could not be reached for comment on whether National Union will appeal.

In 1991, Owens Corning shareholders filed a securities class-action complaint against the company and six of its directors and officers in an Ohio federal court. The suit, *Gaetana Lavallo et al. vs. Owens Corning Fiberglas Corp.*, charged that company officials had misled investors about the impact of asbestos claims on Owens Corning's financial position, court records show.

Four years later, in September 1995, Owens Corning reached a settlement with the shareholders,

agreeing to pay the class just under \$10 million. The company then sought reimbursement from National Union, which denied the claim. In December 1995, Owens Corning sued the insurer in federal court in Toledo, seeking a ruling that the claim was covered under its D&O policy.

The trial court initially rejected the claim, agreeing with National Union that a policy exclusion of claims arising from or related to asbestos property damage barred recovery by Owens Corning, according to one of Owens Corning's lawyers, Steven R. Smith of Connelly, Soutar & Jackson in Toledo.

Last October, however, a panel of the 6th U.S. Circuit Court of Appeals reversed that ruling, finding that the claim instead re-

See **D&O** on page 62



Many workers cash out savings

57% do not roll over 401(k) balances when moving: Survey

By LEE FLETCHER

When packing up their belongings to take to a new employer, the majority of 401(k) plan participants are not bringing retirement savings along, instead cashing out of their previous plans, according to Hewitt Associates L.L.C.

A recent Hewitt study found

that 57% of employees leaving their companies are choosing cash payments from their savings plans instead of rolling over the balances to their new employers' plans or into individual retirement accounts.

In 1993, when Hewitt conducted a similar survey, the percentage was 64%, but the decrease in

workers cashing out their savings still is not enough, according to Mike McCarthy, a Hewitt 401(k) consultant in Lincolnshire, Ill.

"People see it not so much as money that they need to keep for retirement, but more as a sudden windfall or an opportunity for an access to money that they didn't have before. Maybe they want to go out and buy something, in some cases maybe they want to pay off some credit card debt," he explained.

"They just don't think, even in smaller amounts, it's really going to matter as much in retirement, when really it does make a big difference," he said.

Employers can improve their efforts to educate workers about saving for retirement, Mr. McCarthy suggested.

"Employers can be proactive, really from the moment that people start working for them. They need to have people put money aside for retirement," he said. And when workers have opportunities to spend their savings, employers should encourage them

See **Rollovers** on page 48

Taking the money and running

Workers leaving 401(k) plans often do not roll over their funds into a new employer's qualified plan.



Source: Hewitt Associates L.L.C. 401(k) Distribution Rollover Analysis

GRAPHIC BY JOHN HALL

California bills take aim at HMOs

Governor expected to OK measures

By JOANNE WOJCIK

SACRAMENTO, Calif.—Health care premiums could climb in California following passage of a batch of bills that would permit lawsuits against HMOs and require external review of coverage denials, among other things.

If the bills are signed by the governor, as is expected, California would become the third state to permit lawsuits against health maintenance organizations.

HMOs are challenging a similar 1997 Texas law, and lawmakers in Georgia earlier this year approved an HMO liability measure, according to the Washington-based Health Insurance Assn. of America.

Much of California's managed care reform legislation was passed in the waning hours of the 1999 legislative session, after more than a month of closed-door negotiations between liberal Democratic lawmakers and the

more moderate Democratic governor, who sought a balance between cost and expanded patient rights.

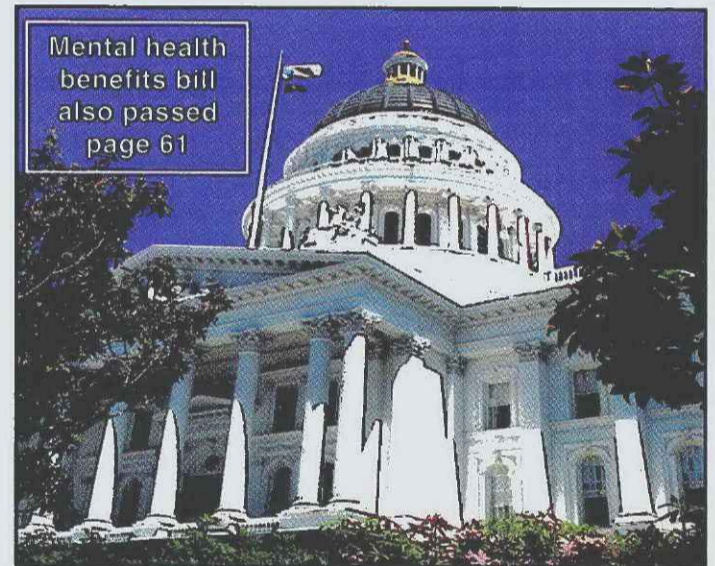
As a result of those negotiations, Democratic Gov. Gray Davis is expected to sign the group of bills, called the Managed Health Care Insurance Accountability Act of 1999. The governor has until mid-October to act on the legislation, which will automatically become law unless he vetoes it.

The Act would, beginning on Jan. 1, 2001:

- Give Californians the right to sue their insured health plans if a delay or denial of coverage for a particular treatment results in significant financial or physical harm.

The statute would not apply to self-insured health plans, which are protected from such suits under the federal Employee Retirement Income Security Act.

See **California** on page 61



California comp bill down, but not out

By ROBERTO CENICEROS

SACRAMENTO, Calif.—Although Gov. Gray Davis will veto a bill that would have increased workers compensation benefits by \$2 billion, opponents of the bill expect the issue to return when legislators reconvene in January.

Trying to forge a moderate road between labor organization and employer wishes, the Democratic governor recently proposed a \$407 million annual workers comp benefits boost for workers in California.

That proposed amount was acceptable to employers, said Steve Wilder, vp-risk management for The Walt Disney Co.

The proposal is a testimony to the governor's efforts to govern from the middle, said Mark Webb, vp-state affairs in Sacramento for the American Insurance Assn. Labor and attorneys for workers comp applicants—some of the gover-

nor's biggest supporters—let it be known that they are irate about the governor's proposal, Mr. Webb added.

Just before adjourning on Sept. 10, legislators sent S.B. 320—which employers and insurers oppose—to the governor's desk. Early in the legislative session, S.B. 320 sought \$1.7 billion in workers comp benefits increases (*BI*, May 3).

In its current form, though, the bill seeks to gradually boost benefits yearly, culminating in an additional \$2 billion in annual benefits by 2005, according to an analysis by the San Francisco-based Workers' Compensation Insurance Rating Bureau of California.

The governor's administration has put S.B. 320's price tag at \$1 billion annually. The governor said he will veto the legislation because it is too costly for businesses and does

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Market

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rate their remaining books and scale back volume as necessary.

A constriction in retrocessional capacity following the collapse of several Australian reinsurers is expected to raise prices for that coverage, though some companies may forego retro coverage rather than pay higher rates.

Firmer pricing also is expected at year end for workers compensation, aviation and marine insurance risks, reinsurance executives say.

Deteriorating profits, mounting catastrophe losses and the uncertainty posed by the Year 2000 computer bug also are factors that likely will influence reinsurance renewals.

Several forces may conspire to prevent prices from rising as much as the

market would like, however, including continued high capital in the market, new and existing reinsurers continuing to compete for top-line growth, and the potential availability of alternatives, such as risk securitization products.

Those were among the issues discussed at the 43rd annual Rendez-Vous de Septembre, held in Monte Carlo, Monaco, Sept. 6-10. The Rendez-Vous is the traditional beginning of year-end reinsurance renewal negotiations. Each year in the first full week of September, the tiny but affluent Mediterranean principality is visited by reinsurers, brokers, cedents, consultants and other service providers, each trying to gauge the market's mood before more formal negotiations commence later in the year.

"Last year, we said rates must go

up. This year they actually might," said William J. Adamson, chief executive officer of the CNA Re unit of Chicago-based CNA Financial Corp. "I'm reasonably optimistic the winds of change are there," he said.

"If you listen to what's being said, there's some conviction that terms have to improve for reinsurers," Mr. Adamson said.

But while there is more resolve among reinsurers to raise rates, competition will continue from some quarters, Mr. Adamson said.

"You still hear of someone swooping in when another company pushes back," he said.

Dennis Zettervall, CEO of HartRe Co. L.L.C., a unit of The Hartford Financial Services Group Inc., said, "There is agreement that the market is sick, and there seems to be agreement on the remedy, which is that rates

needs to go up, but the question is whether the patient will take the medicine."

Reinsurers had suffered numerous small losses that cut into their profits, he said. And "Capital providers are saying, 'I need to make a good return; what are you doing with my capital?'" Mr. Zettervall said.

The bottom has definitely been reached, but an upward trend in rates may not be seen until 2000, said Benito Pagnanelli, deputy general manager of Assicurazioni Generali S.p.A. of Trieste, Italy.

Henry C.V. Keeling, president and CEO of X.L. MidOcean Reinsurance Ltd. in Hamilton, Bermuda, said, "I'm feeling quietly optimistic."

Last year in Monte Carlo, few people were talking about the likelihood of rate increases, but this year more reinsurance executives are expecting

to see some increases, he said.

"I don't know whether that will lead to any increases in prices, but it should mean that rates will stop going down," Mr. Keeling said.

The reduction in retrocessional capacity, mainly in Australia, should, at the very least, have an impact on the marine reinsurance markets, where several primary insurers previously have been dependent on the availability of cheap retrocessional coverage, he said.

"What reinsurance rates need at year-end is a dose of Viagra," quipped Steven J. Bensinger, president of Chartwell Re Corp. of Stamford, Conn. The Trenwick Group is acquiring Chartwell Re.

"The hard market is not here yet," but there are two key indications of possible change, said Hans D. Rohlf, managing director and chief underwriting officer-North America for Hannover Reinsurance Co. of Hannover, Germany.

One sign, he said, is that "it's been many years since I've had so many calls from brokers asking us to revise our more cautious and conservative underwriting approach."

The second indicator, Mr. Rohlf said, is that attendants at previous Rendez-Vous meetings would ask, "How much will prices go down?" "Now, there is a recognition that pricing is flat, and perhaps the question is if (rates) will go up," he said.

"There are many puzzle pieces coming together that could eventually complete a picture of a market turn," he said.

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BI adds new district manager

NEW YORK—*Business Insurance* has made an addition to its New York advertising sales staff.

Bob Murray has joined the magazine as district manager. Mr. Murray, 38, is responsible for



Mr. Murray

accounts in Ohio, New Jersey, New York's Long Island and selected accounts in New York City. "Bob brings to *BI* a strong background in finance, which will be useful as the insurance and finance industries move closer together," said Martin J. Ross III, *Business Insurance's* associate publisher and advertising director.

Before joining *Business Insurance*, he served as the senior treasury officer at Hanil Bank in New York, an agency of the South Korean financial institution.

Previously, Mr. Murray was the senior treasury officer in New York for the Australian State Bank of New South Wales Ltd.

At both banks, he was responsible for correspondent banking relationships, marketing commercial paper programs and managing the institutions' balance sheets.

Mr. Murray has a bachelor of science degree in accounting from St. John's University in Jamaica, N.Y.

Mr. Murray can be reached at 212-210-0136.



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What can we do to help you?

Market

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Ingredients for change

Any change in the market will depend on a change in the reinsurance industry's capital, several executives said.

"While I don't believe rates are falling any more, I don't see significant increases without a loss or a significant removal of capacity," said Donald S. Watson, a director of Standard & Poor's Corp. in New York. But "Companies are more willing to walk away" from inadequate rates, he noted.

"Poor technical results in the reinsurance market will translate into poor financial results," said Max Taylor, chairman of Lloyd's.

"Yet there's still too much capital in the market. So there's this dynamic tension between unattractive results and declining rates," Mr. Taylor said.

CNA Re's Mr. Adamson said he doesn't think it will be capital depletion that turns the market but rather investors demanding higher returns. Insurance stocks are under pressure, and companies no longer can help profits by writing more business, he said.

"We are trying to be as smart and prudent as we can be, but a market turn is not going to be driven by us; it will be the bigger companies," said Francois M. Chavel, president and CEO of SOREMA N.A. in New York.

"The combined ratios of the big guys are up, but whether it is because of acquisitions or they want to send a signal to the market is unknown," he said. The largest reinsurance compa-

nies have such a big share of the market that they truly decide whether the market will turn, and "we are just following," he said.

"Jan. 1 will be very instructive as to the intentions of the big reinsurers," Mr. Chavel said.

Few reinsurers, insurers or brokers at the Rendez-Vous appeared to expect further rate reductions at the year-end renewals, said Robert F. Orlich, president and CEO of Transatlantic Holdings Inc. in New York.

"It seems pretty clear that we have reached the bottom. I haven't heard anything about rate reductions," he said.

But a true turn in the market will require more than just rate increases, Mr. Orlich said.

"Part of softness has been not only rate reductions, but less-than-proper underwriting information. With some

markets, when you ask them for more information, they just move on," he said.

And rates do need to increase significantly as well, Mr. Orlich said.

"Some rates have substantially deteriorated in the past, and a 10%, 20% or even 30% increase will not be enough," he said.

And while retro rates will likely increase, other reinsurance may hold still, Mr. Orlich said.

"It obviously will not be across the board; there is still way too much capital chasing too few risks," he said.

And rate reductions have happened for so many years that individual cedents and brokers may find it difficult to accept increases, added Paul A. Bonny, president-international operations at Transatlantic Reinsurance Co. in London.

"A lot of brokers have never been

told that they can't have a rate decrease," he said.

Hardening lines

Among the lines of business most likely to see higher rates at year end are workers comp and umbrella liability, according to CNA Re's Mr. Adamson. "Workers comp is looking at about a 120% combined ratio and needs big rate surgery," he said.

Workers comp reinsurance pricing is also likely to be driven higher by expectation of losses from the Unicover pool (see story, page 18).

"People need to get back to underwriting discipline," Mr. Adamson said, including more selectivity on risks being underwritten and better rating.

Rates also will rise in the retro market, he said.

As reinsurers look at the combined ratios of business they cover, some workers comp, umbrella, general liability and health care ratios have grown, Mr. Adamson said.

"If you write high-combined-ratio business, those affect income. It's a question of how much of an underwriting loss you are prepared to take," he said.

"There may be a few client situations, deal by deal, where rates can remain favorable. You don't want to paint everything with a broad brush," he said.

The signs of a turn in the market are beginning to show through, said Jacques Blondeau, chairman and CEO of SCOR S.A. in Paris.

Retrocessional capacity in Australia has shrunk dramatically; reinsurers in the United States have suffered poor results in the first half of 1999, with policyholder surplus falling nearly 7%; and some large reinsurers have indicated that they are now prepared to cut back on poorly performing business, he noted.

"Everything is driving in the same direction," Mr. Blondeau said.

In particular, the sharp decrease in retrocessional capacity will impact small and medium-sized reinsurers that are dependent on the retro market to support their capacity, he said.

And rates for aviation, satellite and marine risks are likely to increase, as reinsurers have suffered large losses in those areas, Mr. Blondeau said.

Rates appear to be heading higher, said James P. Bryce, senior vp at International Property Catastrophe Reinsurance Co. Ltd. in Pembroke, Bermuda.

But each cedent will be assessed differently, and it still won't be clear what will happen until the actual renewal date arrives, he said.

Pricing always is contingent on three variables, Mr. Bryce said: exposure, experience and the supply of capital.

"If exposures go up the price goes up; if there's a loss, then there's an acceleration in pay-back. . . . And if you look at all the loss activity, the supply in capital seems to be going in one direction, but we'll find out what happens on January 1," Mr. Bryce said.

"At July 1 renewals, we saw rate increases for Florida exposures" in the retrocessional market, said Mr. Rohlf of Hannover Re. "It's tough to get below an 8% rate on line for 75- to 100-year exposures, or less than 7% for 100- to 250-year exposures," he said.

"But, if the wind doesn't blow, it's difficult to believe rate increases will continue," he said before Hurricane Floyd began doing its damage.

There is already some tightening in certain pockets of the reinsurance market, said Arthur S. Underwood, senior vp at PXRE Corp. in Edison, N.J.

For example, reinsurance and retro rates have already increased in Chile, he said.

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Opinions

End harassment of RRGs

HOW MANY TIMES do risk retention groups have to fight and win the same legal battle in court before regulators will accept the outcome?

That question is being raised in Oregon, where state regulators are refusing to follow a federal court ruling that found them in violation of the federal Risk Retention Act beyond the specific RRG that filed the suit.

The issue involved isn't a tough one, as we report this week. Oregon requires automobile dealers and distributors selling service warranties to demonstrate financial responsibility. One way a dealer can do this is to purchase a reimbursement insurance policy from an insurer authorized to do business in Oregon. To be authorized, an insurer must be a member of the state insurance guaranty association.

This requirement poses an obvious problem for risk retention groups. They cannot, under federal law, be members of guaranty associations. As a result, an RRG, no matter how financially sound, cannot provide reimbursement liability policies in Oregon to auto dealers or distributors offering warranty service protection to consumers.

Quite properly, an RRG challenged Oregon's requirement as violating the federal Risk Retention Act, which says the groups are free to operate nationwide after meeting the licensing requirements of any state and which pre-empts state laws and rules that discriminate against them.

Oregon regulators disagreed. State financial responsibility laws and rules, they said, are not pre-empted by the Risk Retention Act. But as Magistrate Janice Stewart wrote, the most rational reading of the Risk Retention Act is that, while states can specify an acceptable means of demonstrating financial responsibility, such as requiring policyholders to buy a minimum amount of coverage, those means cannot discriminate against RRGs as a class.

As the magistrate rhetorically asks in her ruling, if requiring auto dealers to buy policies from authorized insurers—which, under Oregon law, cannot be RRGs—doesn't discriminate against RRGs as a class, then what would?

She found in favor of the group that filed, National Warranty Insurance Co., RRG (a Risk Retention Group).

That ruling should definitively end any questions of whether Oregon's financial responsibility requirements discriminate against RRGs as a class.

But Oregon regulators apparently don't see it that way. They say they will comply with the magistrate's order, but only as it applies to NWIC, the RRG that filed the suit. Even an appeals court affirms the ruling, as we feel is certain, Oregon regulators are refusing to promise that they will apply the ruling to any RRG other than NWIC.

Oregon regulators say that because only one party—NWIC—filed suit, Magistrate Stewart's ruling applies only to that group.

Whether that is technically true is not the point. The point is that all RRGs writing the same coverage as NWIC would be discriminated in the same way by Oregon's financial responsibility law as NWIC has been. If another



suit were filed by a different RRG, there is no reason to believe that Magistrate Stewart would rule differently.

By refusing to apply the court decision more broadly, all Oregon will accomplish is to force other RRGs to file suit. Since the facts will be the same as in the case with NWIC, the state inevitably will lose those battles, too. All that will have been accomplished is that RRGs and the state will waste both time and money on unnecessary litigation. Surely, Oregon has better ways to use its legal resources.

Regrettably, the situation in Oregon is not unique; it is part of a pattern of state harassment against RRGs. It was only a few years ago that RRGs had to fight a Louisiana law and insurance department requirements that imposed a wide variety of fees and capital surplus requirements on RRGs; in clear violation of federal law, the requirements were promptly struck down by courts.

At the same time, states are imposing on RRGs an array of fees that appear to be pre-empted by federal law, while a South Carolina municipal association is trying to impose a "licensing" tax on RRGs that are domiciled in other states but that do business in South Carolina.

State insurance and other officials need to be reminded why Congress passed the Risk Retention Act. Legislators concluded, after exhaustive research by a federal task force, that state rules made it very difficult for employers to band together to cover their own risks and that federal pre-emption was therefore necessary.

RRGs serve an important public-policy purpose. Their presence injects more competition into the marketplace and encourages traditional insurers to fairly price their programs. These are benefits regulators should not forget.

Regulators also should know that, if harassment continues, Congress surely will again be forced to intervene.

Don't ignore lessons from Floyd

HURRICANE FLOYD struck the East Coast of the United States last week with less vigor than had been anticipated, but it could have been much, much worse.

Not only were losses minimized because the storm lost a little of its punch before making landfall in North Carolina, but, more importantly, residents and businesses in the Southeastern United States also took ample precautions to minimize damage and get out of harm's way.

We hope businesses and individuals along the East Coast do not consider those efforts wasted or, worse, grow complacent in the face of future storms.

No doubt some in Florida now feel foolish and frustrated at having packed up and evacuated areas that seemed most at risk before Floyd veered to the north. But that rapid response and reaction is precisely what will minimize storm losses, loss of life and injury when a storm does hit.

The Walt Disney Co., for example, probably lost millions of dollars in revenue by shutting down its vast theme park in Florida early in the week. And without actual property damage, odds are the business interruption is not insured.

That expense, however, is nothing compared with the liability Disney would have faced for the potential injuries or deaths of workers and park patrons kept in harm's way.

The same is no doubt true of other Florida businesses that closed down as the storm churned across the Atlantic.

A big reason for this widespread risk avoidance is Hurricane Andrew, which showed many in the insurance industry and elsewhere the enormous potential for damage from a hurricane.

As with Andrew, the toll from Hurricane Floyd could have been much worse. Knowing that, we can only hope that people will not let down their guard for the storms to come.

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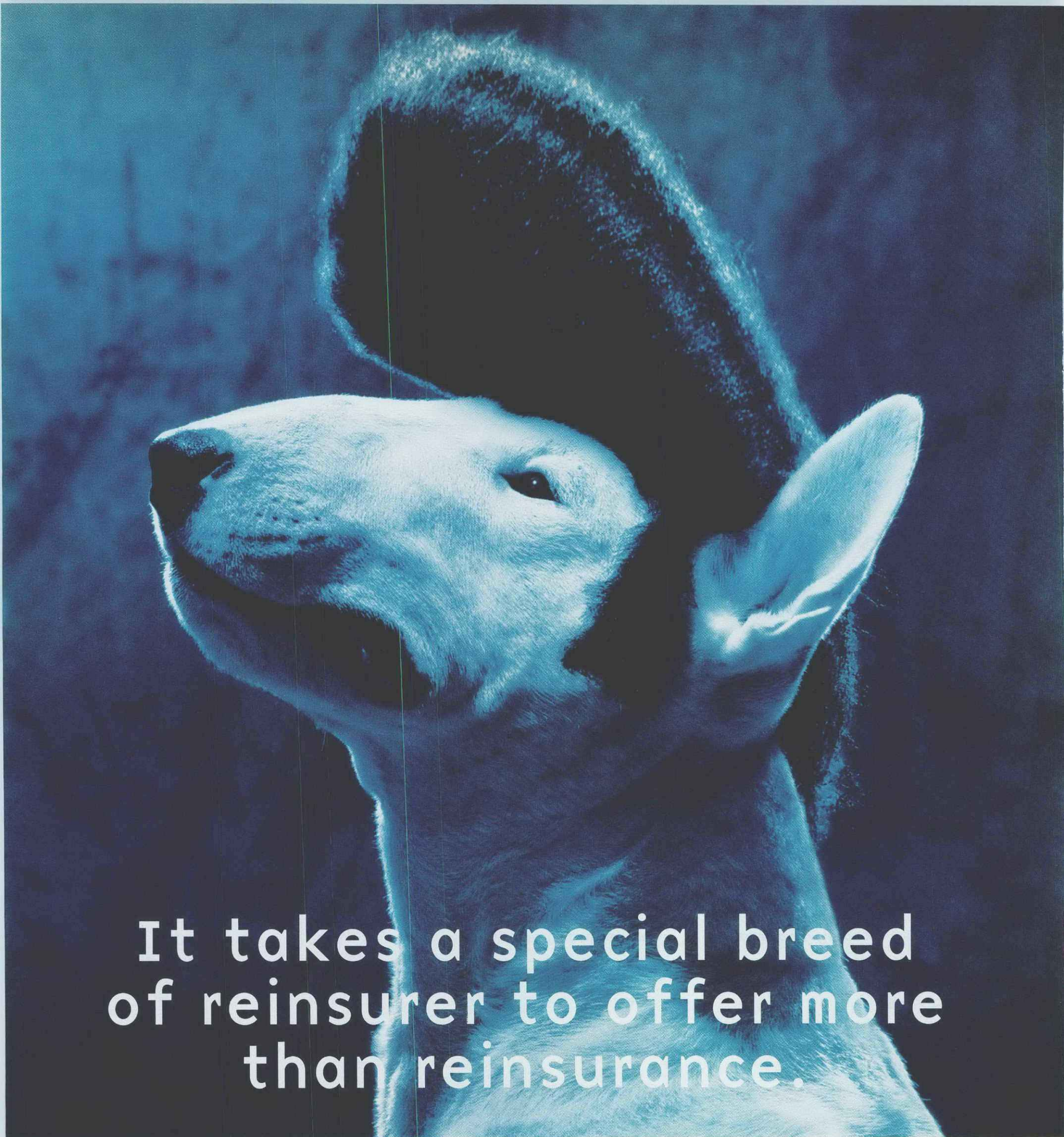
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Market

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"We've seen some pretty big increases in Chile because people felt that things were severely underpriced," Mr. Underwood said.

And while recent renewals for Mexican business did not see major increases, there seemed to be a change in the atmosphere of the market, he said.

"There was some difficulty in getting things done in Mexico, which seems to indicate that there was some resistance...but it was all worked out," Mr. Underwood said.

The reduction in retro capacity should lead to increases in rates, said Mr. Zettervall of HartRe.

"The demand for retro coverage will exceed supply," according to Mr.

Zettervall.

Therefore, reinsurers' costs will increase, but it is still not clear whether the reinsurers will pass on those costs to primary cedents, he said.

Reinsurers still may bear the increased costs themselves in the face of continued overcapacity, Mr. Zettervall said.

"But notwithstanding the fact that there's still a lot of capital in the market, there's an awareness that something has to change. If that change doesn't happen now, then a more massive change will happen later," he said.

Most likely, there will be selective increases for reinsurance at this year's end, Mr. Zettervall said.

ACE Ltd. renewed its retrocessional coverage for its property catastrophe business on July 1, and "there was some increase," said Brian Duper-

reault, chairman, president and CEO of the Hamilton, Bermuda-based insurer and reinsurer.

"The terms were reasonable because we really haven't given them that much in terms of losses," he said.

There also has been some firming in space, marine and some aviation business, Generali's Mr. Pagnanelli said.

S&P's Mr. Watson also cited a potential for firmer pricing in marine and aviation business.

"Capacity for low-level losses is diminishing," said Bernhard C. Fink, CEO of ERC Frankona Reinsurance A.G., the Munich, Germany-based subsidiary of Employers Reinsurance Corp.

At the lower level of reinsurance programs, it's an opportunistic market, he said. "We hope to get out of these lines and remain in areas where we can get more appropriate rates."

Despite all the talk of rate increases at the Rendez-Vous, there appears to be little evidence of increases in reinsurance rates, said John Berger, president of Chubb Re, a Bernardsville, N.J.-based unit of Chubb Corp.

"Who's pulling out and where are rates actually going up?" he asked rhetorically.

Although retro capacity has diminished, the rest of the reinsurance market still has plenty of capacity, Mr. Berger said.

"The commercial guy that is buying a direct insurance policy is not paying any more for it," he said.

Although direct rates remain low, however, they have not sunk to the level of reinsurance rates, said Mr. Duperreault of ACE.

"Reinsurance pricing is significantly lower than insurance, so it needs to change, and there is a momentum for

that," he said.

But reinsurers still are trying to expand their business, and they are willing to accept low rates to achieve that end, Mr. Berger said.

Chubb Re will expand its business at year end if retro rates do increase, he said. "We'll write more for the right price."

"The market is soft, and I don't think we'll see any dramatic changes," said Max F. Furrer, chairman and CEO of Rhine Reinsurance Co. Ltd. in Basel, Switzerland.

And even if there is a hardening of rates in some areas on Jan. 1, 2000, the increased use of two- and three-year policies over the past several years will mean that the full effects will not be felt immediately, he said.

On the other hand, reinsurers have reached the point where they are unwilling to cut rates further, so few companies will renew their reinsurance coverage at lower rates this year, Mr. Furrer said.

Catastrophe losses

One of the factors putting pressure on reinsurers to raise rates is an increase in catastrophe losses.

After a relatively light year in 1997, reinsurers incurred heavy catastrophe losses in 1998, including hurricanes Georges and Mitch, the Canadian ice storm and various hail and windstorms, among other events.

Catastrophe losses in 1999 already were on track to meet or exceed last year's level even before Hurricane Floyd threatened damage.

In addition, the growth of quota share reinsurance underwriting puts reinsurers' loss experience more in line with that of the primary companies, compared with excess-of-loss reinsurance, said S&P's Mr. Watson.

"This year, we have had a few substantial losses," notwithstanding the earthquakes in Turkey and Greece, said Mr. Pagnanelli of Generali. "Given these losses, the market should have a reaction."

If losses from the earthquakes in Turkey and Greece hit hard at small to medium-sized reinsurers, it could push them out of the market, said Dirk Lohmann, CEO of Zurich Re in Zurich, Switzerland. Such companies are highly exposed, compared to how much premium they have received for the risk, and compared with the rest of the market, he said.

"There are a lot of losses out there. Turkey hurts. Oklahoma tornadoes. It all just eats into business. That will start to drive cat rates as attritional losses grow," said Mr. Adamson of CNA Re.

The increase in catastrophe losses affecting reinsurers may not necessarily lead to rate increases, said John T. Sinnott, chairman and CEO of Marsh Inc. in New York.

For example, the aviation market has not yet turned despite the losses it has suffered, he said.

"Aviation is a very small and discrete market, but you look at its loss ratio and there still hasn't been any change in rates," Mr. Sinnott said.

And satellite insurers have suffered some large losses over the past year, but rates have not increased dramatically, he said.

But in other areas, there does seem to be a tightening, said Edmund R. Megna Jr., president and CEO of the United States division of Guy Carpenter & Co. Inc., the reinsurance brokerage unit of Marsh.

For example, more insurers are re-entering the market in Florida, and there is a high demand for reinsurance capacity, he said.

Rates already are stabilizing, and a large hurricane loss would likely lead to a dramatic increase in rates, Mr. Megna said.

But even a large loss likely would

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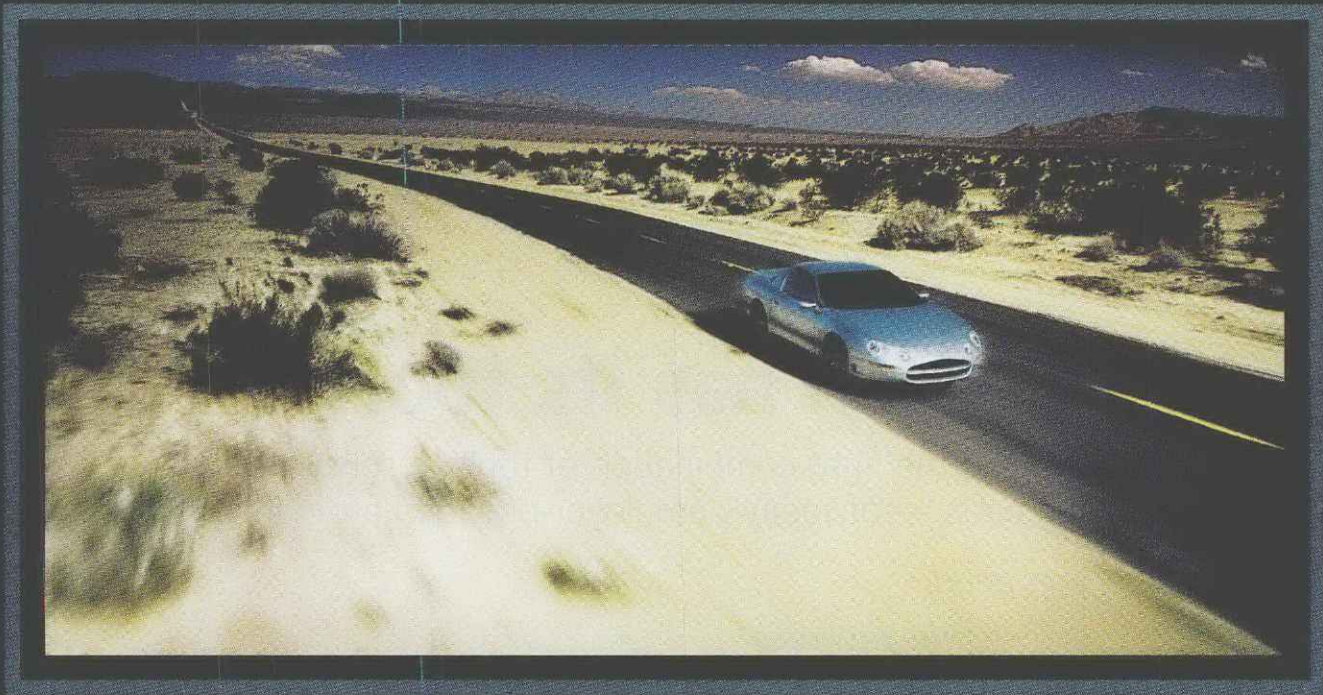
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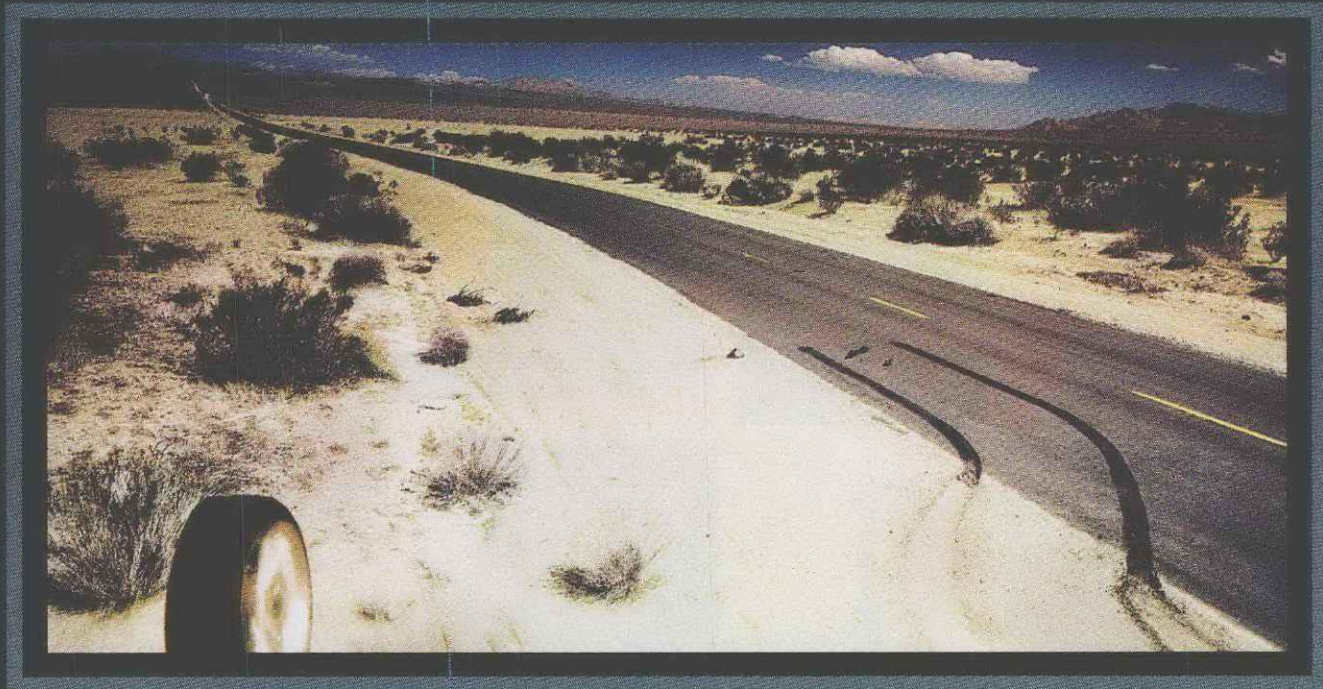
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Market

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not lead to the huge rate increases that were imposed by reinsurers in 1992 after Hurricane Andrew, as more capacity is available to return to the market, he said.

"Bermuda reinsurers have been retrenching, Lloyd's has more capacity, investors that divested their equity interest in Bermuda market may jump back in, and the capital markets products have been developed," Mr. Megna said.

"There's a lot of noise, a lot of static on the line" about whether rates will begin firming at year end, said H. Rocker Channell Jr., president of Aon Re Worldwide Inc. in Chicago.

"A lot of conversations are trying to

see where the market will go and how a company should be positioned to be successful," he said.

Cedents that have had good relationships with reinsurers and good loss experience in the past are not necessarily going to see higher rates at year end, Mr. Channell said.

Some selective lines of reinsurance look ready to tighten at year end, said John M. Pelly, chairman and CEO, reinsurance at Willis Faber & Dumas Ltd. in London.

A series of large single losses at industrial plants will likely affect retrocessional rates for facultative contracts and property per risk treaties, Mr. Pelly said. In addition, the Unicovert problem will lead to a general tightening on accident and health business, and hurricane losses in the Caribbean in 1998 should lead to

higher property reinsurance rates for those risks, he said.

"The industry has had about five years of rate reductions, and we seem to be returning to a more regular pattern of losses, so reinsurers are beginning to build up some resolve," Mr. Pelly said.

And while some reinsurers who have survived the soft market are well-positioned to take advantage of a rate increase, the increases may come too late to help others, he said.

"Some companies are extremely well-positioned for an upturn, but some of those out there are already dead," Mr. Pelly said.

Insurance buyers are likely to resist any broad market turn, one executive says.

"As a buyer of reinsurance, Zurich wants quality, stable security that un-

derstands our exposures and won't paint us with a broad brush when there's an adverse development," Mr. Lohmann said. "Don't throw the baby out with the bath water."

Zurich's reinsurance buyers have spent a lot of time with its reinsurers explaining their business, he said. Most of what Zurich buys is excess-of-loss reinsurance, though some of its business units do purchase pro rata coverage, he said.

As a reinsurer, though, even long-term clients have gotten about as much rate relief as they can from reinsurers, Mr. Lohmann said. "In a number of instances, we'll see business go" rather than pay higher prices, he said.

Walking away from business

Walking away from underpriced business was a strong theme at this

year's Rendez-Vous.

Triggering much of the discussion was news of Swiss Reinsurance Co.'s ambitious "Triple 20 program," which it launched earlier this year.

Under this program, the reinsurer plans to reduce its catastrophe reinsurance capacity by 20% in markets with inadequate rates, cut administrative costs 20% by 2001 and review the least profitable 20% of its business, a spokesman in Zurich said.

"There is a rule that 80% of profits come from 20% of clients," noted Mr. Watson of S&P. "Similarly, 80% of losses come from just 20% of clients," he added.

While a 20% cut in expenses may be difficult for Swiss Re to achieve, putting out such a large figure gets people's attention and focuses them on savings more than would a 5% expense reduction goal, said Robert J. Mebus, managing director of S&P in New York.

Also, while several reinsurers have made statements about reducing the volume of poorly priced business they will underwrite, not all of their offices have gotten the message, Mr. Watson said. "Setting a target at least moves the company in the right direction."

ERC Frankona in June began reassessing each piece of business it writes with an eye to withdrawing from markets or accounts that are inadequately priced, Mr. Fink said.

"We looked at everything and decided which markets we should keep and even raise market share, which ones we would remain in if rates can rise, and finally, ones to leave," he said.

"The last category, which accounts for about 20% of gross premiums, is one where ERC Frankona will not compromise," said Mr. Fink.

In reviewing its business, ERC Frankona did not seek a fixed rate increase across the board, instead reviewing each risk on a case-by-case basis. "In some cases, 150% would not be enough; in others, maybe restructuring the program would be enough," Mr. Fink said.

"Some clients are happy to hear the message and are reassessing their needs and exploring whether they must take the same approach with their primary clients," he said.

SOREMA N.A. also has trimmed underpriced business from its book as it aims to be very conservative on the treaty reinsurance side, Mr. Chavel said. "We've shrunk our treaty book by about 30% over the last three years," he said. "We're only a marginal player (in treaty business), but that's fine in the current market."

Some reinsurers appear to have "reached their pain threshold," said Alan G. Murray, vp at Moody's Investors Service Inc. in New York.

"Some companies are beginning to pull back from the market and accept less premium volume," he said.

But, at the same time, reinsurers are looking to increase their premium from other lines, such as primary insurance, Mr. Murray said.

"They are competing with their clients. They are trying to get business at any cost," he said.

Executives at the Rendez-Vous also were waiting to see how Munich Reinsurance Co. will negotiate its year-end renewals. Munich Re has such a large share of the reinsurance market that several executives predicted that the market cannot harden without a concerted effort by Munich Re to increase its rates.

A spokesman for Munich Re said the reinsurer would write business for profits rather than growth.

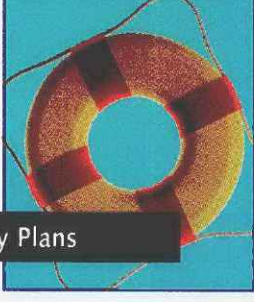
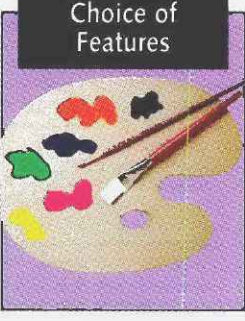
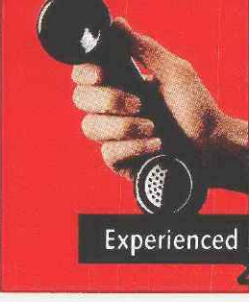
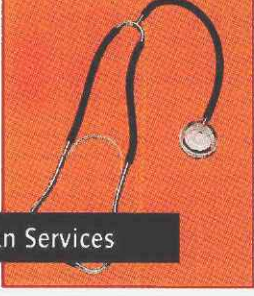
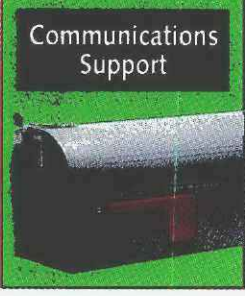
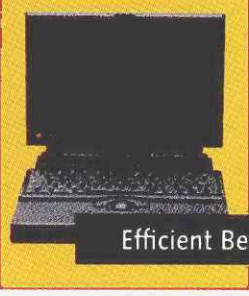


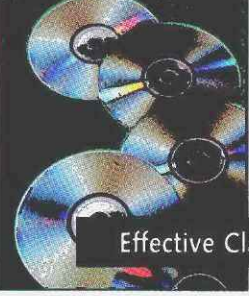
And, given the poor results of most of the reinsurance market, there should be "a turnaround situation," he said.

Each cedent, however, will be
See Market on page 14

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Market

Continued from page 12
judged on its own loss experience, the spokesman stressed.

Munich Re itself was affected by the Turkish earthquake, as it has a 15% share of the Turkish market. But much of the business written by Munich Re in Turkey is health reinsurance, and that will not be affected by the earthquake, he said.

Munich Re's losses for the quake will be "within our calculations," the spokesman said.

Reinsurer CEOs today more than ever are talking about shedding underpriced business and have resolved to do so, said Mr. Adamson of CNA Re. "I think you have to be prepared to lose the business," he said.

CNA Re examined its expenses starting in July 1998. By January, it determined that it was not making enough money for the risks it was assuming and began to re-examine deals and products with inadequate profits.

"For the last few years, we haven't had underwriters and brokers in the industry, we've had order-takers," Mr. Adamson said. "We have to get back to underwriting and brokering. It will take some guts."

Mr. Furrer of Rhine Re said rates for facultative reinsurance, in particular, have fallen so much in recent years that his company has substantially reduced its portfolio.

As a result, the reinsurer has tried to build up its book of non-traditional reinsurance business, Mr. Furrer said. "The margins are thin, but the risks are thin, too."

Other reinsurers also are looking to curb their traditional lines and expand in other lines of business.

SCOR has tried to weather the soft market by reducing its traditional business, Mr. Blondeau said. In the first six months of 1999, the reinsurer reduced its traditional property and casualty reinsurance business by about 5% and increased its life reinsurance and non-traditional business, he said. While the life and non-traditional business will not replace the dropped business, those two lines will expand significantly in 1999, Mr. Blondeau said.

Life insurers are looking for strong reinsurers to provide capacity and expertise, and sectors such as the utility industry increasingly are looking for non-traditional coverages for such exposures as weather risks, he said.

One property/casualty area where reinsurers can grow is program business in the United States, he said.

SCOR expects to write about \$100 million in program business this year, mostly for small and medium-sized commercial insurers, but also for affinity groups, Mr. Blondeau said. "These people are reinventing mutual companies, but they are not keeping the risk." Instead most of the risk is passed on to the reinsurers that back up the programs.

The key to writing the business successfully is to have a balanced book of business, he said. SCOR currently works with about 20 to 25 managing general agents, which it audits at least once a quarter, Mr. Blondeau said.

Similar opportunities could emerge in Europe as Internet-based insurers seek reinsurers to back up their business, Mr. Blondeau said.

"The Internet companies are looking to be pure distributors," he said.

Timing of renewal negotiations could be a factor in the prices cedents obtain, some executives said.

Some clients of ERC Frankona already are seeking extensions of their current programs, as they know that January renewals will be a "difficult scenario," said Mr. Fink.

In recent years, many insurers

sought to delay renewals to get better deals, he said. Now, reinsurers may try to put off renewals until later so that it becomes more apparent to cedents that rates must increase, Mr. Fink said.

"We expect clients to try and renew early in the season, and many are approaching us now for Jan. 1 renewals," Mr. Rohlf of Hannover Re said.

Clients who complete their renewals early in the season may get better terms than ceding companies that wait until late December, agreed Mr. Adamson.

Meanwhile, there is a segment of the brokerage and underwriting community that has never seen a hard market, noted Mr. Adamson. Managing client expectations during renewals will be a challenge for those individuals, he said. **B**

Old clause brings new worry for reinsurers on Y2K issue

By GAVIN SOUTER
and PAUL D. WINSTON

MONTE CARLO, Monaco—A new twist to the Year 2000 problem was bugging reinsurers at this year's Rendez-Vous de Septembre: the sue and labor clause.

Last year, the main Year 2000 worry for reinsurers was liability coverage. This summer, though, a new menace appeared when several large corporations filed claims under the sue and labor clause of their property policies.

GTE Corp. was the first corporation to file a claim under the clause, followed by Xerox Corp. and then Unisys Corp. (BI, July 5; July 26). The policyholders claim that their insurers should pay the costs for remediating their computer systems to make them Year 2000 compliant.

They argue that the sue and labor clause obliges a policyholder to prevent potential losses and that insurers are compelled to reimburse any costs they incur in doing so.

Insurers argue the clause—which was originally included in marine policies in the 17th century to ensure that shipowners took emergency steps to prevent a ship from sinking—applies only to imminent losses. And, because large corporations have known about the Year 2000 problem for several years, losses cannot be classified as an imminent, they argue.

Most reinsurers in Monte Carlo agreed that the sue and labor clause should not apply to Year

Continued on next page

out of our minds™



Rendez - Vous

Continued from previous page
2000 remediation.

Insurance indemnification is for fortuitous losses, said James P. Bryce, senior vp of International Property Catastrophe Reinsurance Co. Ltd. in Pembroke, Bermuda.

"Y2K is not fortuitous, and there hasn't been any damage," he said.

The main concern for Year 2000-related losses will be for liability issues, rather than property losses, and those liability losses will not be clear until next year, Mr. Bryce said.

"The Year 2000 situation is an open issue. You'd be remiss in saying the sue and labor clause is nothing, as you never know how courts are going to interpret a 200-year-old maritime clause," said Dirk Lohmann, chief executive officer of Zurich Re in Zurich,

Switzerland.

One possible safeguard for reinsurers, he said, is that there have been many court rulings to date on coverage for lost data. Most of these lawsuits have been brought as liability suits alleging third-party negligence, rather than first-party property claims, he noted. But, courts in most of those liability suits have ruled that loss of data does not qualify as damages, Mr. Lohmann said.

Another argument against liability for Y2K losses is that this situation is not a sudden development, he noted. "It did not happen yesterday."

If the industry gets into coverage arguments over when the Y2K loss occurred, however, it could wind up with the same triple trigger of liability that hit insurers in as-

bestos and environmental cases, Mr. Lohmann warned.

The sue and labor clause will likely lead to some payments by insurers and reinsurers, said John Berger, president of Chubb Re, a Bernardsville, N.J., unit of Chubb Corp.

'You'd be remiss in saying the sue and labor clause is nothing, as you never know how courts will interpret it.'

— Dirk Lohmann

"I think there will be a lot of settlements because nobody wants to set a precedent. So there will be losses, but it won't be the end of

the world," he said.

As long as the issue remains unresolved, more and more policyholders will make claims, as the potential payments could be significant, most reinsurers and brokers agree.

The possibility of making a claim under the sue and labor clause likely is under discussion in the legal departments of most major corporations, said John T. Sinnott, chairman and CEO of Marsh Inc.

But the ultimate determination of whether the clause applies will be made in court, he said.

"The word 'fortuitous' is going to get a real workout," added Marsh President Brandon W. Sweitzer.

Although the sue and labor clause was not designed to respond

to Year 2000 remediation costs, the claims filed will inevitably lead to significant legal action in the United States, said Jacques Blondeau, chairman and chief executive officer of SCOR S.A. in Paris.

"There will be millions of dollars in defense costs," he said.

The actions by GTE, Xerox and Unisys have set the stage for Year 2000 claims from policyholders, said Edmund R. Megna Jr., president and CEO, United States division at reinsurance broker Guy Carpenter & Co. Inc.

"We'll see a flurry of activity and that will obviously involve some expenses for things like declaratory judgments," he said.

"I see some significant defense costs coming for the industry," said Hans D. Rohlf, managing director and chief underwriting officer-North America for Hannover Reinsurance Co. of Hannover, Germany.

"At Hannover Re, underwriters began discussing the Y2K issue two and half years ago. We looked into various segments. We met with property people, discussing business interruption and contingent business interruption. What slipped our analysis, though, was the sue and labor clause," he said.

It is difficult to estimate the industry's exposure because, due to differences in policy wordings, each claim may be handled differently, Mr. Rohlf said.

"It will take a long time to sort out, but it will be interesting to see who's putting up reserves—or admitting that they are putting up reserves," said Mr. Rohlf. A lot of these costs, he added, will go straight to company's balance sheets.

"Everybody has made their decision in how to approach Y2K, so they now are waiting to see," said William J. Adamson, CEO of the CNA Re unit of Chicago-based CNA Financial Corp.

"If the sue and labor clause forces coverage, all bets are off," he said.

Outside of the sue and labor issue, reinsurers appear to be philosophical over the extent of Year 2000 claims. Many of the insurance and reinsurance contracts currently in force will cover the crucial period as last year's renewals were often extended by several months to avoid disputes over which policies will apply to any Year 2000 losses. Consequently, there is little more that can be done to combat the problem through underwriting or exclusions, they say.

"One thing I'm most surprised at is the quiet about Y2K," said Bernhard C. Fink, CEO of ERC Frankona Reinsurance A.G. in Munich. "Maybe there's no talk because it's too late to do anything."

What has been done so far has differed from reinsurer to reinsurer.

"The Year 2000 risk, in my view was not treated correctly from the beginning. The market talked too much about the implications of the problem without trying to achieve a consistent approach. The solutions of inclusion or exclusion (of Y2K risks) has differed widely by company and country," said Benito Pagnanelli, deputy general manager of Assicurazioni Generali S.p.A. of Trieste, Italy.

"Until Jan. 1, 2000, though, we won't really know very much," he said of the reinsurance industry's exposure.

"We expect a lot of litigation. How much it will all cost is in the hands of God."

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Mahoney

Continued from page 16

bypass insurers, Mr. Mahoney said.

For example, often when policyholders make claims, the first thing they get back from their insurers are reservation-of-rights letters. A narrow interpretation of coverage will then follow, and eventually the policyholder may only be paid, say, 80 cents on the dollar, he said.

Additionally, insurers and reinsurers are offering coverage for only a

small portion of the risks policyholders face, Mr. Mahoney said.

For example, for some high-tech firms, their tangible assets represent only a tiny percentage of their market capitalization, he said. "Their real value is derived from intangible assets such as brand names and intellectual capital. Insurance has not yet really addressed this whole field of reputational risk," Mr. Mahoney said.

To succeed in the changing world, brokers must deliver better value, he said. In order to do so, they must focus on their clients' needs; broaden their

range of risk management skills; and invest in information technology to interface with clients rather than just using IT for back-office functions, Mr. Mahoney said.

In addition, insurers, reinsurers and brokers must cooperate as an industry to offer better service to policyholders, Mr. Mahoney said.

"If any of us are not delivering value added, we should own up and pass the task to someone else," he said.

"We really need to have the whole industry working together," Mr. Mahoney said. **BI**

Unicover losses may come for years

By **PAUL D. WINSTON**
and **GAVIN SOUTER**

MONTE CARLO, Monaco—Reinsurers generally do not expect further problems to emerge for the industry

from reinsurance pools like the controversy surrounding the ill-fated Unicover Managers Inc. workers compensation pool.

However, most also agree that the losses arising for companies that reinsured the pool will be significant and could take years to unravel.

Earlier this year, the workers comp reinsurance pool managed by Unicover unraveled amid allegations that unexpected explosive growth in premiums could generate \$2 billion or more in losses for pool's retrocessionaires (*BI*, March 15). Those losses could, in turn, flow to those companies' retrocessionaires, and so on, through the market.

Unicover's troubles became public when the parent of Cologne Life Reinsurance Co.—which was both a member and retrocessionaire of the reinsurance pool—disclosed a \$275 million pretax loss related mainly to reserving for Unicover exposures.

Since then, another workers comp carve-out pool, this one managed by IOA Re, has entered the spotlight as Cologne Life Re seeks to void its participation in that pool (*BI*, Aug. 30).

"Life reinsurers and accident and health pools have been involved in workers compensation business on the high excess layers usually reserved for catastrophic situations for about 20 years, but the competitive rush for more premiums led many companies to accept working layer risk at prices typically paid for higher excess layers," according to Standard & Poor's Corp.'s "1999 Global Reinsurance Highlights."

"What was different with Unicover is that over time, treaty conditions underwent subtle changes. The retrocessionaires went from providing a high excess layer to a working layer. The companies in some cases didn't realize how exposed they were to working-layer losses and were unaware that the terms had changed," explained Donald S. Watson, a director of S&P in New York.

"Unicover is a progression of something that's been in the market for 10 years," agreed Dirk Lohmann, the chief executive officer of Zurich Re in Zurich, Switzerland.

"Life insurers (in the Unicover pool) didn't realize how exposed they were. Some tried to reinsure out of the problem, rather than simply quit writing the risk," Mr. Lohmann said.

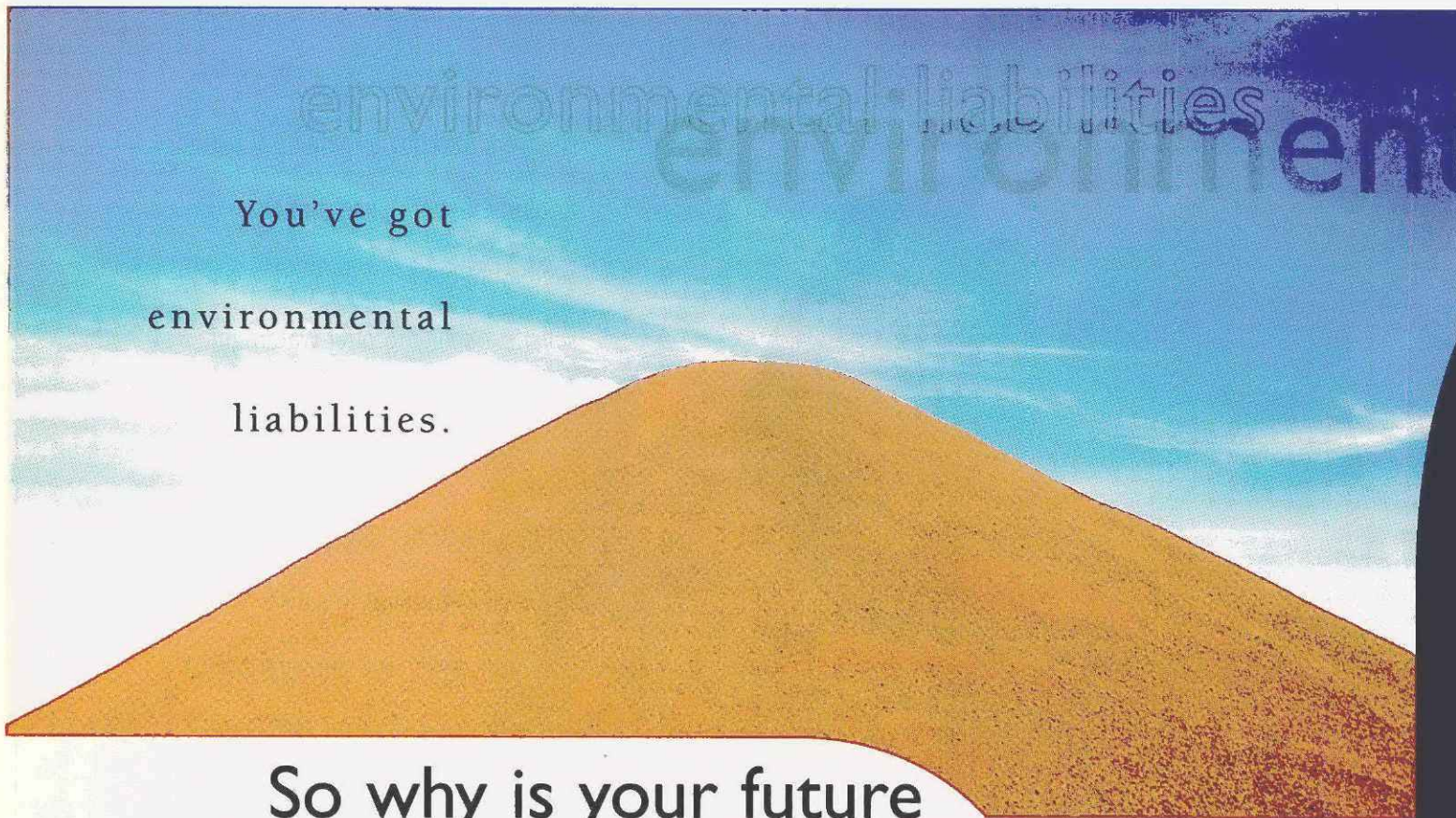
The unusual aspect of the Unicover collapse was that it happened before large losses were suffered on the business placed in the pool, said Dennis Zettervall, CEO of HartRe Co. L.L.C., a Hartford, Conn.-based unit of The Hartford Financial Services Group Inc.

"Usually it takes actual losses to blow something up; this blew up before the losses actually materialized," he said.

The early emergence of the problem will force reinsurers to make pricing adjustments earlier, Mr. Zettervall said.

Brokers also will feel some of the losses from the Unicover situation, predicted Hans D. Röhlf, managing director and chief underwriting officer-North America for Hannover Reinsurance Co. of Hannover, Germany. E&O litigation against brokers will have a "sizable impact," he predicted.

Already, for example, Odyssey Re (London) Ltd. is suing broker Stirling Cooke Brown Holdings Ltd., alleging the broker fraudulently assumed
See Unicover on page 20



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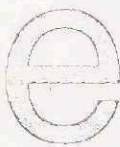
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Unicover

Continued from page 18
business on the reinsurer's behalf, including deals that originated with Unicover (BI, April 5). Stirling Cooke rebuts the allegations and has filed to dismiss the suit.

Unicover may be followed by other problematic programs coming to light, said John Berger, president of Chubb Re, a Bernardsville, N.J., unit of Chubb Corp.

"There are a lot of programs out there that are supported by cheap reinsurance that are not viable in the long term," he said.

Unicover, a managing general underwriter, has problems reminiscent of those reinsurers ran into in the early 1980s when they supported business written by managing genera-

agents, Mr. Berger said.

"In the early 1980s we had MGAs, and people lost their shirts. Today we have MGUs and that's OK!" he quipped.

"It just goes to prove that we never learn in this business," Zurich Re's Mr. Lohman said of the Unicover fiasco. "It all happened with the LMX spiral 10-12 years ago," he said, noting that claims from 1983's Hurricane Alicia still pop up today because the LMX spiral was so big.

"Unicover demonstrates that no matter how hard we try in this industry, another one always comes along," said Max Taylor, chairman of Lloyd's of London. "It shows how the industry still has the capacity to create a massive, complex multiparty risk structure. As a result, companies get tiny premiums for the risk assumed."

The losses from the Unicover pool

will likely lead to hardening in the workers comp reinsurance market, said Edmund R. Megna, president and CEO of the U.S. division at Guy Carpenter & Co. Inc. in New York.

"Some companies in the U.S. will be facing renewals with part of the program having used Unicover, and it will be difficult to duplicate at the same terms," he said.

The removal of cheap reinsurance with the collapse of Unicover will force primary underwriters to be more disciplined, said Mr. Zetter, all of HartRe. "In the end it's a healthy thing," he said.

More problematic pools still could emerge, said Robert F. Orlich, president and CEO of Transatlantic Holdings Inc. That could reduce capacity further and increase rates, he said.

"From our perspective, that creates opportunity," Mr. Orlich said. **BI**

Capacity shrinks as Aussies exit retro

By PAUL D. WINSTON
and GAVIN SOUTER

MONTE CARLO, Monaco—The financial difficulties of major Australian reinsurance companies is a leading factor behind higher prices for retrocessional coverage worldwide, reinsurers say.

The Australian reinsurance market alone accounted for as much as 30% of worldwide retrocessional capacity, according to some estimates. As a result, the

withdrawal of that capacity, as Australian companies either scale back their underwriting or run off the business, will be felt worldwide.

Other reinsurers say, however, that companies will likely retain larger net lines rather than pay higher prices for scarcer retrocessional capacity.

Three major Australian reinsurers—New Cap Reinsurance Corp. Ltd., Reinsurance Australia Corp. Ltd. and the reinsurance unit of GIO Insurance Ltd.—together incurred estimated losses in fiscal 1998 of about \$1 billion Australian (\$639 million) (BI, Aug. 30).

New Cap Re may be liquidated; GIO Re will be sold or run off by its parent; and ReAC is significantly revising its underwriting strategy in an effort to turn around results.

"If a competitor goes out of business, we should be happy, but we are not because it really has negative implications for our industry," said Benito Pagnanelli, deputy general manager of Assicurazioni Generali S.p.A. of Trieste, Italy.

"If anything, it could raise professional and technological standards for our industry," he said of the problems among the Australian reinsurers.

"There is a problem when companies take short-term gains without looking at long-term risks. The losses always come later," Mr. Pagnanelli said.

There appears to have been a problem in the quality of underwriting, as well as a problem of the Australian reinsurers' timing in trying to deploy their capital in the midst of soft market conditions, said Donald S. Watson, a director of Standard & Poor's Corp.'s Insurance Ratings Service in New York. While GIO Re has been in operation since 1986, ReAC started in 1993, and New Cap Re was launched in 1996.

"It's a tough situation for any start-up—you cannot not write business; your investors demand it," he said.

The problems of the Australian reinsurers are expected to be felt during year-end renewals, some executives said.

The loss of the Australian companies' capacity will have a significant impact on rates in the retrocessional market, said H. Rocker Channell Jr., president of Aon Re Worldwide Inc. in Chicago.

"When you look at what New Cap Re and GIO Re wrote, they kept writing after other markets like Bermuda and London had stopped," he said. "A concern now is whether some other companies will be opportunistic and step into the void," he said.

The retrocessional market appears to be ready to harden due to the reduction in Australian capacity, said Robert F. Orlich, president and chief executive officer of Transatlantic Holdings Inc. in New York.

And brokers are trying to line up alternative capacity, he said. Larger reinsurers should benefit from the withdrawal of capacity as retrocessionaires now will focus more on security and financial

See Australia on page 24

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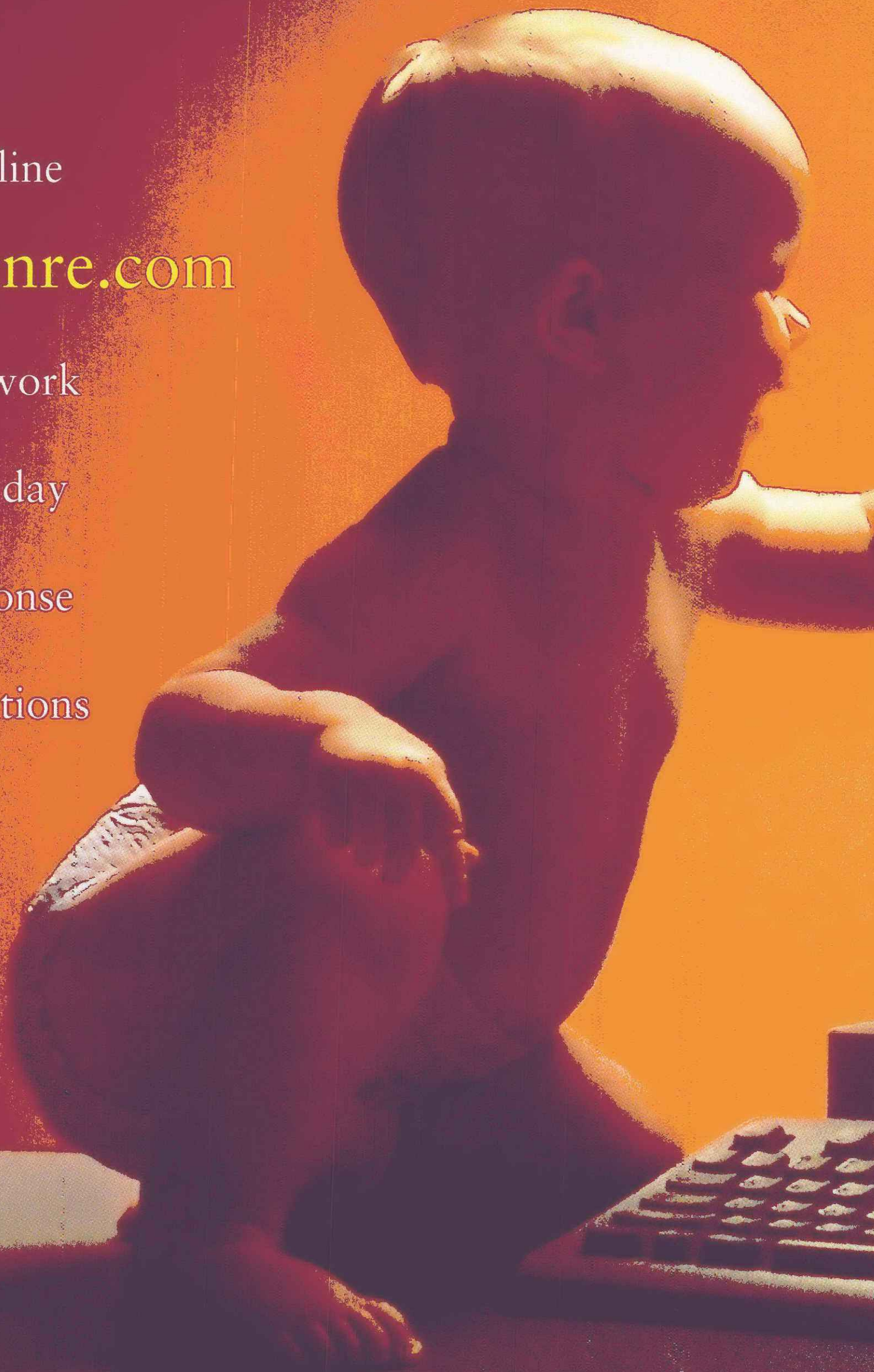
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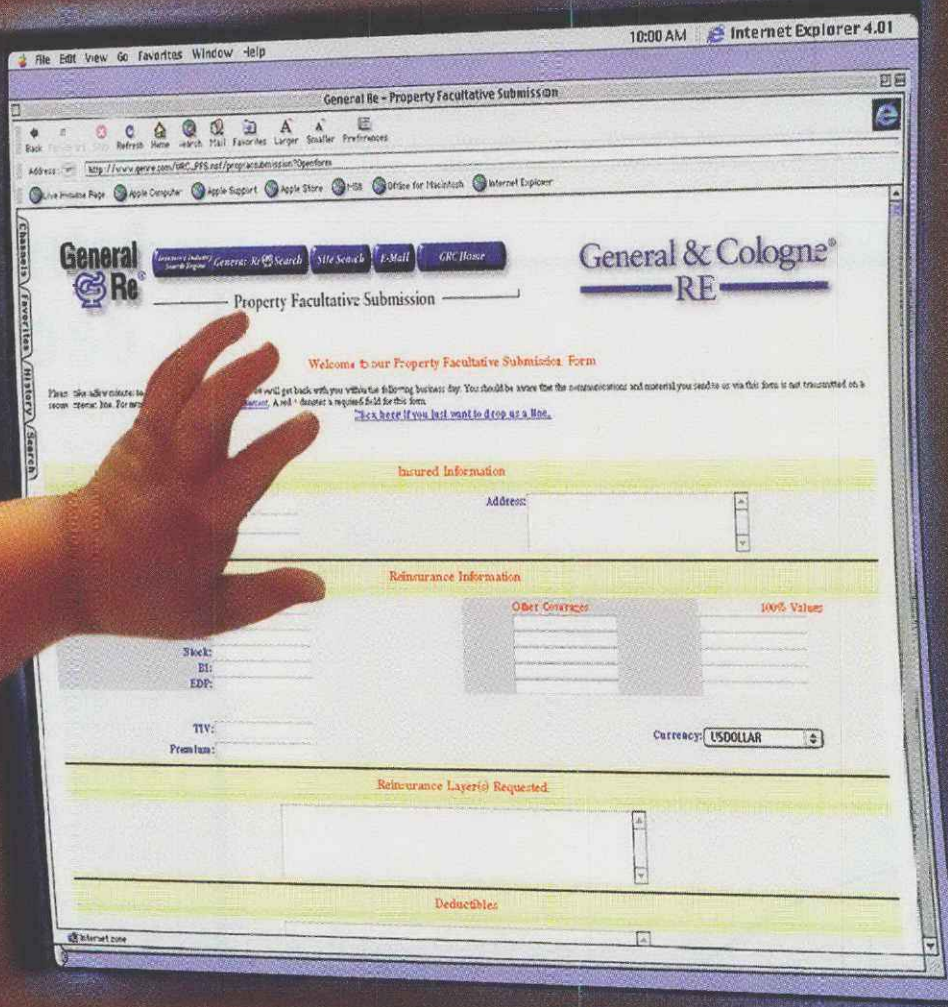
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Continued from page 20
strength, he said.

Transatlantic offers retrocessional reinsurance coverage, but it will be looking for substantially increased rates before it signs on to some programs, Mr. Orlich said.

The withdrawal of the capacity in Australia could lead to new opportunities for other retro writers, agreed Paul A. Bonny, president-international operations at Transatlantic Reinsurance Co. in London.

"We think our business is pretty simple; the problem is that everyone tries to complicate it, and they try to get cute," he said.

Estimates vary, but the retro capacity provided by the Australian companies clearly was significant,

said Jacques Blondeau, chairman and CEO of SCOR S.A. in Paris.

"All that is gone, so you know that the market is going to change," he said.

Retro pricing likely will increase as a result of the withdrawal of capacity, said Arthur S. Underwood, senior vp at PXRE Corp. in Edison, N.J. But the full effect of the withdrawal of the Australian capacity likely will not be felt at this year-end, he said.

"A lot of them were three-year deals, so any impact would be moderated by that process," Mr. Underwood said.

Other reinsurance executives downplayed the consequences of the Australian reinsurers' withdrawal.

If the retrocessional capacity provided by the Australian companies disappears, it won't have a big impact, as ceding companies will retain

1998 losses are up for reinsurers Down Under

Company	Estimated 1998 losses*
GIO Re	- \$485 million
New Cap Re	- \$128 million
ReAC	- \$27 million

* Losses for fiscal 1998 converted to U.S. dollars at year-end exchange rate.
Source: company reports

the risk, said Francois M. Chavel, president and CEO of SOREMA N.A. in New York.

"It was an opportunistic buy," he said of the market for the Australian retrocessional capacity.

"This is an extremely efficient market, and, at the end of the day, an efficient market finds the weak spots," Mr. Chavel said of all the poor risks that were placed by brokers with the Australian companies.

There is no shortage of retro capacity, but, with the exit of the Australian capacity, there will likely be a shortage of low-priced retro capacity, said James P. Bryce, senior vp at International Property Catastrophe Reinsurance Co. Ltd. in Pembroke, Bermuda.

And, even at higher rates, retro business is not necessarily attractive, as it is difficult to track, he said.

"You don't know what you are getting," Mr. Bryce said.

IPC writes a small amount of retro

business, but it is territory-specific and loss-specific, he said.

The Australian market was writing a lot of retrocessional business, but they were not the only companies writing it, S&P's Mr. Watson observed.

"Retrocessional protection in the property market is highly opportunistic," he said. "In 1997, this business all went to the bottom line because there were few losses. With more losses in 1998, it took a hit," he said of the retro market.

The reason this market is so volatile is that a retro reinsurer doesn't know where its risk is coming from, because it is so far removed from the original risk, explained Mr. Watson.

"Whenever a loss occurs, you're likely to get hit—as you'll have a piece of it, even though you may not have known you had it," he said. **BI**

Attendance decreases

MONTE CARLO, Monaco—The reinsurance industry continues to flood this tiny principality in early September, but the number of attendees is declining.

Official attendance at the 1999 Rendez-Vous de Septembre was about 2,250, down from 2,322 in 1998. But because many attendees do not register and others preregister but don't attend, the official figures do not reflect the true number of reinsurance executives in Monte Carlo Sept. 6-10.

This year, however, it was certainly easier to get a table at the Cafe de Paris, one of the central meeting points for attendees.

Attendees cram the cafes, restaurants, bars and hotel lobbies of Monte Carlo during what for decades has been the first meeting of the renewal season.

While the number of attendees decreased, the number of countries represented at the meeting increased. Attendees traveled to Monte Carlo this year from 84 countries, up from 76 in 1998.

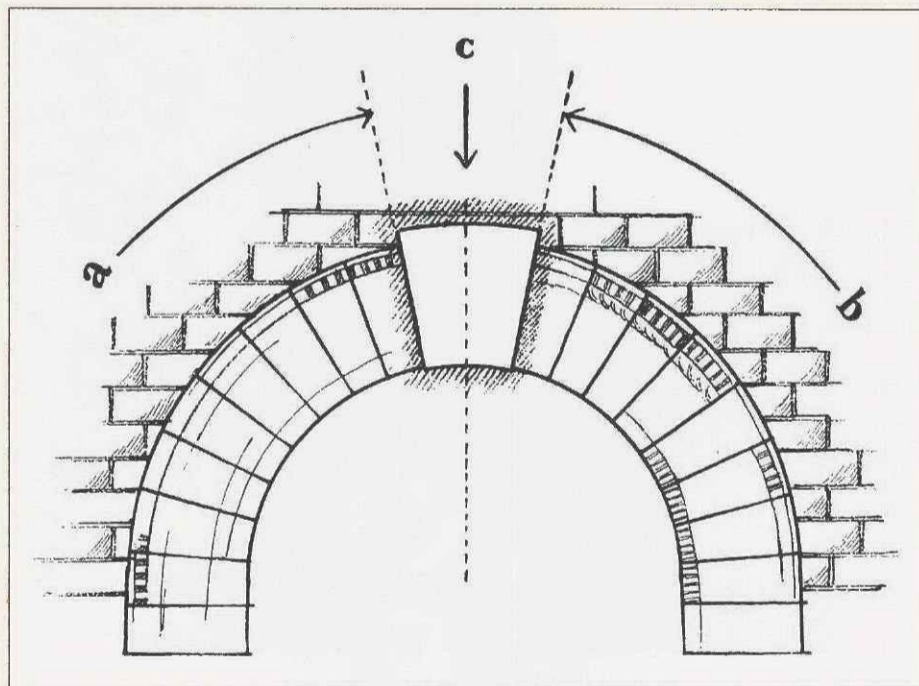
"This shows that emerging countries are slowly coming to take an interest in reinsurance," said Antoine Jeancourt-Galignani, chairman of Assurances Generales de France in Paris and president of the Rendez-Vous.

While most of the discussions at the Rendez-Vous take place during informal meetings, a formal program centers on a particular theme on the Tuesday morning of the meeting.

This year the theme was New Information Technologies. Speakers were Rob Eckelmann, general manager-Europe, Middle East and Africa at Intel GmbH in Munich, Germany; Marinus A. Jacometti, executive board member of ACHMEA, an Amsterdam, Netherlands-based insurer; and Kevin Ashby, chief executive officer of WISE in London.

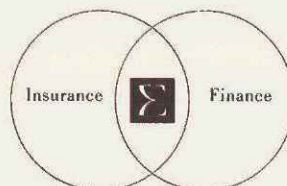
The formal meeting took place, as usual, at the Centre de Congres Auditorium de Monte-Carlo. Next year, however, the auditorium is being given over to arts events. A new conference center, the Grimaldi Centre, is being built, but it may not be open in time for the 2000 Rendez-Vous. Consequently, next year's registration and formal program will be held at the Sporting Club d'Hiver, next to the Hotel de Paris.

Next year's Rendez-Vous will be held Sept. 4-8. For more information, contact Rendez-Vous de Septembre, Direction du Tourisme et des Congres, 2A Boulevard des Moulins, MC 98030, Monaco. 377-92-16-60-50; fax: 377-92-16-61-35. **BI**



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Expansion

Continued from page 26

Mid Ocean Reinsurance Co. Ltd. had unsuccessfully tried to expand into Europe prior to its acquisition by XL, Mr. Keeling said. Rather than attempting to develop independently, the reinsurer needed to commit capital to a venture based in Europe to attract business, he said.

"They are an independent company, and we have great faith in the management of Le Mans Re. With additional capacity and products, we think they are very well-positioned to take a significant lead in Continental Europe," Mr. Keeling said.

HartRe Co. L.L.C. also is expanding in Europe, said Dennis Zettervall, chief executive officer of the reinsurance unit of The Hartford Financial Services Group Inc.

The reinsurer has recently opened offices in Milan, Italy, and

Paris, adding to its existing European offices in London; Madrid, Spain; and Munich, Germany.

Although the market remains soft, HartRe will be well-positioned to expand in Europe when the market turns, he said.

"We plan to be very patient, and we will be looking to establish long-term relations with clients," Mr. Zettervall said. "We think the market is moving more toward excess of loss, and buyers will want more choice," he said.

At the same time, some European reinsurers are seeking to expand from their home markets.

Rhine Reinsurance Co. Ltd. began to expand after it was purchased by Kohlberg Kravis Roberts & Co. L.P. in 1997, said Max F. Furrer, chairman and CEO of the Basel, Switzerland-based reinsurer.

Rhine Re, which already had offices in Toronto and Singapore, has established an operation in Bermuda, opened a representative office in Tokyo and is in the pro-

cess of receiving regulatory approval for a new operation in London.

The Bermuda company writes only a quota share coverage for Rhine Re in Basel, but it will eventually write other business as well, Mr. Furrer said.

The London operation is expected to receive regulatory approval by October. It will be headed by Dennis Purkiss and a team of managers who worked with Mr. Purkiss at his former company, Zurich Re (London).

In 1998, Rhine Re also bought five insurance-related subsidiaries of Bankers Trust Corp., which it consolidated and renamed Rhine Re Financial Ltd. Rhine Re Financial, with offices in New York, London and Jersey in the Channel Islands, specializes in capital markets-based insurance products.

Rhine Re plans to open another branch office in Stockholm, Sweden, Mr. Furrer said.

"We believe in operating in



PHOTO: KATHRYN J. MCINTYRE

Reinsurance industry executives gathered in Monte Carlo, Monaco, this month to attend the annual Rendez-Vous de Septembre.

markets and not trying to just market out of Switzerland," he said.

At present, Rhine Re writes predominantly property reinsurance, but it plans to expand its life reinsurance and its liability reinsurance business, Mr. Furrer said.

The importance of international reach also was illustrated by CNA Re CEO William J. Adamson's decision to move to London from Chicago to temporarily cover a sudden vacancy in the managing director's position.

Mr. Adamson moved to London to oversee CNA Re's U.K. operations after the resignation of Tim Madden, an executive vp who resigned as managing director of the London reinsurance unit to return to the United States.

"It's such an important office to us, I decided to go. I can do more to help CNA Re this renewal season from London than in Chicago," said Mr. Adamson. "Something decisive needed to be done to show we'll be successful and will meet our commitments, and to counteract naysayers," he said.

CNA Re's U.K. operation wrote about \$475 million in net premiums in 1998, more than the approximately \$420 million it wrote from the United States.

Despite widespread restructuring moves at parent CNA Financial Corp., the Chicago-based

reinsurance unit has been largely left alone. CNA Re accounted for more than one-third of corporate profits in 1998, Mr. Adamson said. While the company overall may be undergoing change, each business segment may be dealt with differently, he noted.

One international market receiving a great deal of interest from reinsurers is Lloyd's of London, which has lately seen numerous insurance and reinsurance companies investing in syndicates and agencies.

Some question whether these investors are in the market for the long haul, though.

"The reinsurance market goes for fads," said Dirk Lohmann, CEO of Zurich Re in Zurich, Switzerland.

Twenty years ago, the fad was to form a London company, and then everyone "got killed" on losses, he said. The next fad was to form captives and reinsurers in Bermuda. Now, the fad is to invest in Lloyd's, he said.

Many companies, however, do not fully appreciate how Lloyd's works, Mr. Lohmann said. And in about two to three years' time, many people will question their investment, he predicted.

The current auction prices for stamp capacity are so much higher today than in recent years, even though profitability is lower, he noted. **BI**

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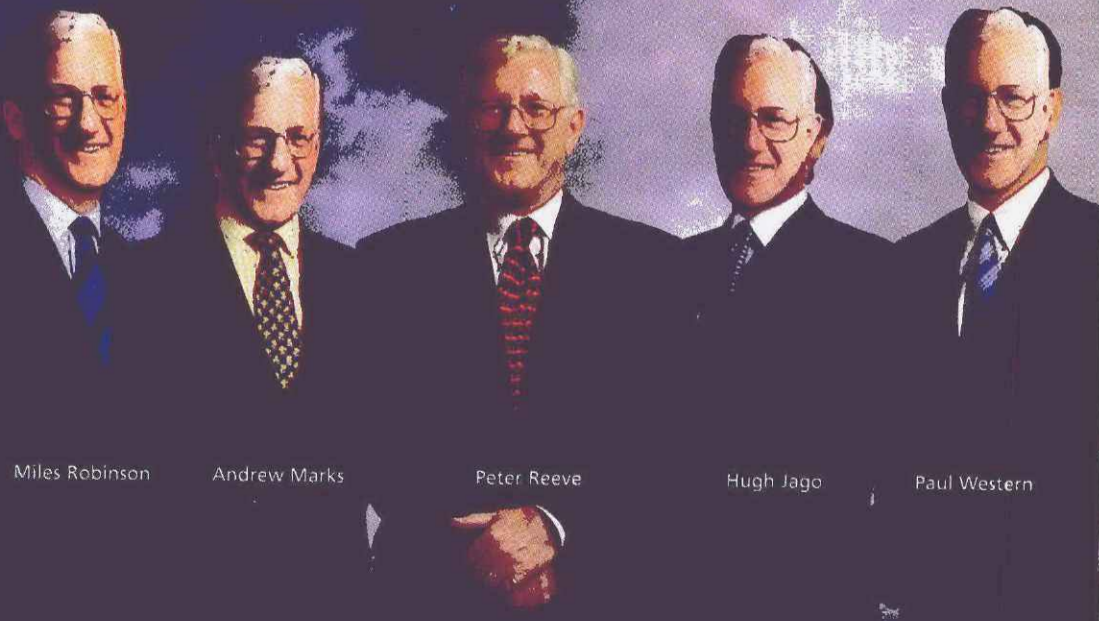
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Risk securitization calm before storm

By **PAUL D. WINSTON** and **GAVIN SOUTER**

MONTE CARLO, Monaco—Greater use of capital markets instruments is a concept ahead of its time—though that moment may have arrived with the onslaught of last week's Hurricane Floyd.

Several reinsurance executives said during the annual Rendez-Vous de Septembre earlier this month that it could take a major catastrophe, on the scale of 1992's Hurricane Andrew, to spur wider interest in the capital markets.

Those comments came only a week before Hurricane Floyd gathered steam in the Atlantic and threatened to strike the U.S. coast with more intensity and perhaps cause greater damage than did Andrew.

Speaking before Hurricane Floyd struck, however, most executives said that while capital markets were a promising develop-

ment, they were unlikely to unseat traditional reinsurance companies.

Reinsurance continues to be easier, quicker and more cost-effective to place than structured capital markets solutions, the executives said.

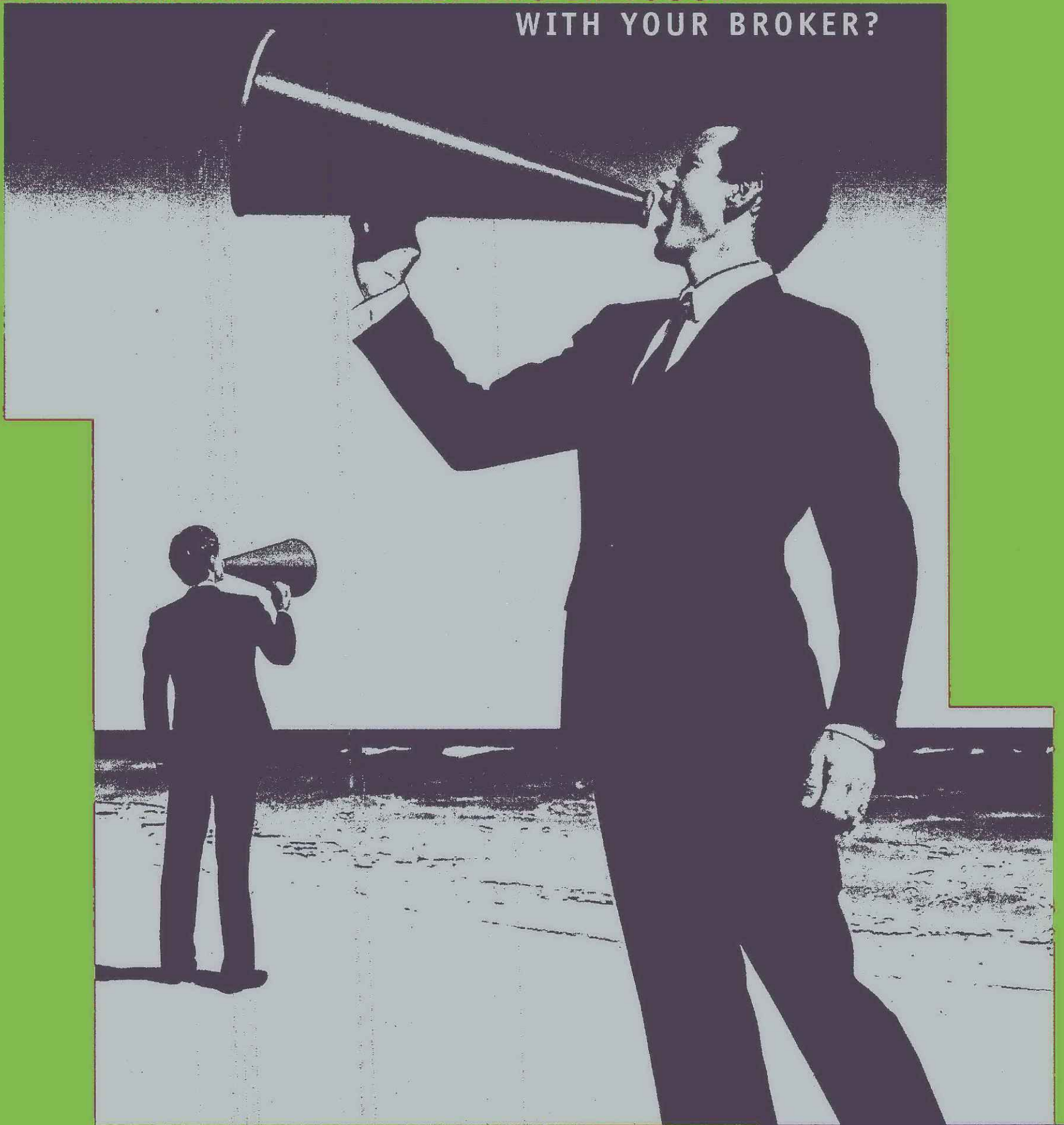
At the same time, most reinsurers are hedging their bets and are using risk securitization, particularly for property catastrophe exposures.

"You see occasional deals done, but it will take time," said William J. Adamson, chief executive officer of the CNA Re unit of Chicago-based CNA Financial Corp. "A lot of clients don't want to take basis risks," he noted.

"In general terms, alternative risk transfer has not been really successful, but it's now in consideration by everyone, including Generali," said Benito Pagnanelli, deputy general manager of *See Hedging on page 32*

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Hedging

Continued from page 30
Assicurazioni Generali S.p.A. of Trieste, Italy.

"At first, it was seen as a financial way to solve balance sheet problems. It now has become a new way to attract capital to the reinsurance industry," he said.

It is too soon to see whether capital markets are having an impact on demand for traditional reinsurance, Mr. Pagnanelli said. That will take two to three years, he predicted. For now, he said, there are still some doubts to be addressed about taxation and regulation before it is more widely used.

Others also cited regulation as a hindrance to use of these products.

In the future, the capital markets are likely to become more involved in offering derivative-type products rather than typical catastrophe bonds, predicted Dirk Lohmann, CEO of Zurich Re in Zurich, Switzerland.

One current impediment to greater use of derivative products, according to Mr. Lohmann, is that regulators are generally opposed to derivatives and require that they be accounted for differently than

other reinsurance programs.

A derivative is an investment that "derives" its value from an underlying asset or from the movement of an indicator, such as interest rates or a catastrophe loss index.

One of the first reinsurers to take advantage of risk securitization was Hannover Reinsurance Co. of Hannover, Germany.

"Risk securitization gives us additional opportunities," said Hans D. Rohlf, managing director and chief underwriting officer-North American for Hannover Re. The company not only issues cat bonds, but it also is frequently offered a chance to invest in such instruments, Mr. Rohlf said.

There now are indications that a small secondary market is developing for cat bonds, he said.

To date, the German reinsurer has structured three life and three non-life deals with capital markets participation, Mr. Rohlf said. "So far, while investors have had to pay an individual loss here and there, they are sticking with us because, overall, they are making a profit," he said.

Investors willingness to remain with reinsurance cat bonds in general will be tested if a big "An-

drew-style loss" occurs, Mr. Rohlf said. Such an event could also drive new investor interest in the bonds, he added.

ERC Frankona Reinsurance A.G. uses the term "strategic re" to refer to a broad range of alternative risk financing mechanisms, including finite risk and capital markets instruments, according to

'It's necessary for (reinsurance) prices to go up for securitization to take off.'

— Brian Duperreault

Bernhard C. Fink, CEO of the Munich, Germany-based subsidiary of Employers Reinsurance Corp.

"Regardless of the name, it is reinsurance that is not exclusively shifting risk," Mr. Fink explained. Such business is not likely to replace most of the traditional risk-shifting products that clients seek from reinsurers, he said.

The inability of securitized products to compete on price with traditional reinsurance is one of the main hindrances for the new prod-

ucts, said Edmund R. Megna, president and CEO of the U.S. division at Guy Carpenter & Co. Inc. in New York.

In the past, many reinsurers that have been working on securitized deals have eventually turned them down in favor of traditional retrocessional coverage, he said.

"We've been successful in generating new retro business where we've found companies have been working on securitized arrangements but, because of time and cost issues," have instead sought traditional retro coverage, Mr. Megna said.

Securitized insurance and reinsurance products still are not as efficient as conventional coverage, and their success appears to be dependent on increases in reinsurance rates, said Brian Duperreault, chairman, president and CEO of ACE Ltd. in Hamilton, Bermuda.

"It's necessary for prices to go up for securitization to take off, but whether that will actually come to pass, I don't know," Mr. Duperreault said.

"Traditional reinsurance is too cheap for these alternative structures to be competitive," said Francois M. Chavel, president and CEO of SOREMA N.A. in New

York. "These deals are very expensive for all but certain layers."

As more deals are done, though, capital market deals could become more efficient, one reinsurer suggested.

If retro prices increase sufficiently, securitized products could become more popular, though reinsurers and cedents still need to adopt a different mind-set before they really take off, said Arthur S. Underwood, senior vp at PXRE Corp. in Edison, N.J.

"It needs a mental adjustment. You need to have a few big securitized deals happen, and then people might say, 'Oh!', and it could pick up. . . . It will probably take a little longer than people think," Mr. Underwood said.

Securitized products also will have to compete with other alternative risk transfer products if reinsurance prices start to climb, said Dan Malloy, president and CEO of Stockton Reinsurance Ltd. in Hamilton, Bermuda.

If low-priced retro capacity disappears, reinsurers will look for alternatives such as aggregate stop-loss coverage, which offers coverage based on a reinsurer's loss ratio, Mr. Malloy said.

Stockton Re has not sold many of these coverages over the past several years because reinsurers have not suffered sufficient losses to feel that they need to pay for the alternative coverage, Mr. Malloy said.

And aggregate stop-loss coverages are often more efficient than retro coverages because the premium is not paid all at once, he said.

"One of the problems with retro is that you pay for the retro up front, but your premiums come in over 24 months," Mr. Malloy said.

Hannover Re has an advantage over other companies offering risk securitization, Mr. Rohlf said, in that it structured its first capital markets deal in 1993. Because of that history, its recent deals were much easier to create.

"We'll continue to explore that area as an alternative means to generate capital," Mr. Rohlf said.

"These vehicles are complex, and the reaction time (for creating coverage) is not as fast as with reinsurance," he said. "In a prolonged hard market or property cat market, though, it may have an impact—but not yet."

ERC Frankona's Mr. Fink agreed that the property cat market is one in which the capital markets may make inroads on the traditional reinsurance market.

If property catastrophe rates start to climb, that could trigger much-greater interest in these alternative risk financing tools, said Mr. Adamson of CNA Re.

Even Lloyd's of London is interested in new risk securitization opportunities.

"Many Lloyd's underwriters express frustration that they are not in the alternative risk transfer business," observed Max Taylor, chairman of Lloyd's. "But they have always been very creative at developing solutions, so Lloyd's has been an 'alternative' market for some time," he said.

Securitized products, however, are not necessarily a good fit with the current structure of the market. So the Lloyd's market is examining its rules and structure to see if it would be possible to accommodate some of these new risk financing tools, Mr. Taylor said.

Eventually, the whole securitization area—including bonds, hedges and swaps—will become an important part of the market, he predicted. **BI**

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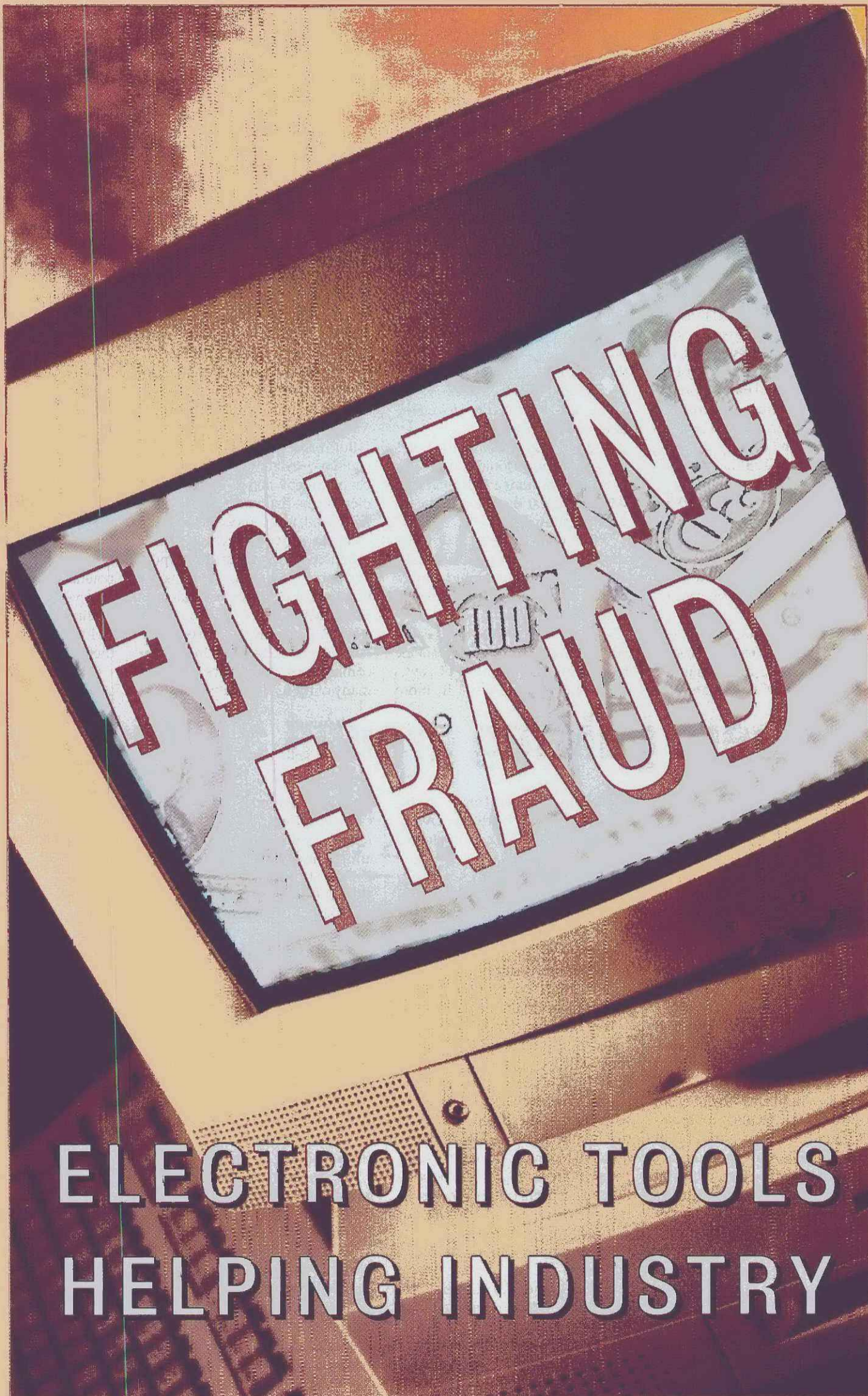
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COOPERATIVE EFFORT AIMS TO SNUFF OUT ARSON CLAIMS
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Netting fraud: Online training tool explored

By **RODD ZOLKOS**

The Internet may prove a valuable tool in fighting insurance fraud if a distance learning program under consideration by the National Assn. of Independent Insurers and the FBI becomes reality.

If it does come to fruition, the Internet-based insurance fraud prevention and investigation program could improve the quality of insurance fraud training, expand the universe of those trained to prevent and detect the problem and increase law enforcement emphasis on insurance fraud, the program's proponents suggest.

"It's a fascinating set of ideas," said John Eager, director of claims services at the National Assn. of Independent Insurers in Des Plaines, Ill.

The NAI's interest in using the Internet to teach fraud prevention and investigation techniques stems from an earlier pilot program the FBI conducted that used distance learning techniques for law enforcement education.

"The FBI did a project in 1997; it was sort of a pilot of a distance learning program," Mr. Eager said. "They used different delivery means.

"And then they wrote a fairly comprehensive report on the results," he said.

What the FBI found, he said, was that the project yielded good results from the standpoint of training quality, "and they saved many mil-

lions of dollars in the process."

So far, discussions with the FBI have been "very preliminary," the NAI's claims services director said.

But, the attractions of such a program to both the federal law enforcement agency and the NAI are very much the same as those that draw the FBI together with its other partners in educational programs.

"If the FBI right now partners with universities like the University of Virginia, for instance, one of the reasons they do that is that they want to give input into the criminal justice curriculum," Mr. Eager said.

By the same token, "If the insurance industry were to partner with the university or the FBI, you could put a little more emphasis on white-collar crime," he said.

The thinking is that the results of such a joint effort would be an insurance fraud-focused curriculum, a broadening of the message about the problems stemming from insurance fraud and an increased FBI emphasis on insurance fraud investigation, Mr. Eager said.

And, upon completing the training, participants would conceivably put their insurance fraud-fighting skills to work at the FBI or in the insurance industry.

"I think the FBI gets about 7,000 applicants a year and they take about 700, so there might be more job opportunities in the insurance area," Mr. Eager said.

Mr. Eager believes the Internet environment could improve insurance fraud training in a number of ways.

For one, it could result in more

consistent training.

For another, virtual reality-type teaching techniques could offer students a chance to get realistic lessons, such as examining a possible arson site for clues, without needing to go out into the field.

And the Internet training also could increase the number of people involved in the fight against insurance fraud, as the reduced cost of training would mean that insurance companies could afford to train more people.

Don Nettle, assistant vp of claims security at United Services Automobile Assn. in San Antonio, said the last point is particularly significant.

With an Internet-based training program, insurance companies could train more people without needing to rely on those working in their special investigative units to provide the training, he said.

"It's an extra area of training that, in the past, the companies have not addressed because their (special investigative units) were rather small," Mr. Nettle said.

But this sort of distance learning could be used to "sensitize" a number of underwriters and claims handlers to the hallmarks of insurance fraud, and, in the process, make the company's investigative units more productive by getting them more and better information about possible fraud cases from those individuals, he explained.

"That's the only way we get referrals unless we get an informant coming forward, and we don't get many of those," Mr. Nettle said.

And, he noted, not only does the distance learning approach allow companies to train more people without putting extra demands on those in the special investigative units, it also allows claims handlers and underwriters to be trained with less disruption to their routine than if they had to gather at a set time and location for a traditional class.

"This is less disruptive and intrusive," Mr. Nettle said. Meanwhile, it gives investigative units more time for actual investigations.

The distance learning approach to fraud training is an idea whose time has come, Mr. Nettle said.

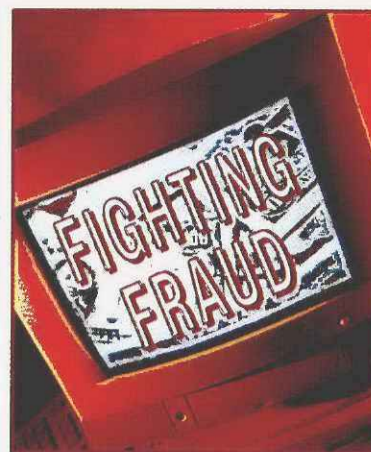
"There are several reasons why its time has come," he said. "Some of them are mandated reasons from state insurance departments."

He noted that many states now require insurance companies to train underwriters and claims handlers to recognize potential instances of insurance fraud, so that they can refer possible fraud to companies' investigative units and state fraud bureaus.

"The mandate is that we have a comprehensive training program for our claims people and underwriters," he said. "The mandates mean that we can't make believe anymore that fraud isn't there."

And such a program also could potentially help employees of investigative units meet their own continuing education requirements "without taking them away from their jobs," Mr. Nettle said.

Companies the NAI has talked to about the idea have been enthusias-



tic, Mr. Eager said.

"They've said, 'What a great deal for our agents,'" he said. "The companies we've been talking to have been trying to get their agents to look at these (fraud) indicators before they bind."

The effort to craft a distance learning insurance fraud investigation and prevention program remains in its early stages, but the NAI is optimistic, Mr. Eager said.

"We're just trying to get enough information together from the initial meetings and continue the discussions," Mr. Eager said. "I think our mission now is to get together the substantive parts of it, the mechanics, and see how it's received."

"We're gathering a lot of good information," he said, adding that he thinks the idea could "resonate with a lot of different sectors."

And, ultimately, Mr. Eager suggested, the Internet program could be the vehicle for spreading the message of the issue of insurance fraud to a broad audience, prompting widespread recognition that it's better to prevent insurance fraud than to fight it after it has occurred. **EI**

Insurers gaining ground against health care fraud

By **SALLY ROBERTS**

While its precise financial impact on the industry is unknown, experts say health care fraud each year accounts for billions of dollars of the nation's total health care expenditures.

Through the use of advanced technology, education, legislation and a closer working relationship with law enforcement authorities, though, health insurers say they are detecting and prosecuting more cases of fraud today, resulting in millions of dollars a year in restitution.

While fraud can be committed by any party in the health care delivery and payment system, experts say most fraud is committed by health care providers.

Not surprisingly, the most common type of health care fraud committed by providers continues to be billing for services that never were rendered, either by augmenting otherwise valid claim charges for services performed or by using patient names and health insurance information to fabricate claims.

"Fraud always is an evolving type

of situation," noted Patricia A. Ingeno, director of health care investigations for CIGNA Corp. in Bloomfield, Conn.

"Things change within the health care world, and so does the type of person who wants to commit fraud," Ms. Ingeno said. The movement toward a paperless environment through electronic billing and data transfer, for example, "adds a new element" to the game, she said.

Tom Brennan, director of the special investigation unit for Highmark Inc., which operates as Highmark Blue Shield in western Pennsylvania and as Pennsylvania Blue Shield elsewhere in the state, noted that the actual number of health care providers involved in fraud is quite small compared to the total provider population. "That small number, however, is extremely capable of doing a lot of damage," Mr. Brennan said.

The estimates of damage from fraud vary.

In 1992, the U.S. General Accounting Office reported to Congress that losses from health care fraud amounted to as much as 10% of the nation's total annual health care expenditure, or as much as \$84 billion in 1992.

The Washington-based National Health Care Anti-Fraud Assn. esti-

mates that the proportion of health care dollars lost to fraud falls in the range of 3% to 5%. At a time when annual health care spending in the United States totals more than \$1 trillion, that amounts to \$30 billion to \$50 billion in fraud, according to the NHCAA.

"Fraud represents a minimum of \$30 billion a year, which is a big enough wake-up call for anyone," said Bill Mahon, executive director of the NHCAA.

The 1992 appointment of Janet Reno as U.S. attorney general thrust health care fraud into the spotlight. Ms. Reno ranked combating health care fraud as her No. 2 priority on a list of law enforcement initiatives, behind fighting violent crime.

The issue was again brought to the fore in 1996 with the passage of the Health Insurance Portability and Accountability Act. HIPAA established a new Health Care Fraud and Abuse Control Program, designed to coordinate federal, state and local law enforcement programs to control fraud and abuse in all health plans. The 1996 act also made health care fraud a federal criminal offense, and it contained provisions for conducting investigations, audits and inspections related to the delivery of any payments for health care.

"The climate changed radically in the '90s," Mr. Mahon said. Health care fraud "is high on the list for every federal agency today."

As a result, health insurers today have a "much better chance of inducing law enforcement to take a case and to prosecute than ever before," he said, citing the statistic that 54% of all federal health care fraud convictions today include a prison sentence.

"That's a big change," Mr. Mahon said, noting that health care fraud convictions in past years typically yielded community service and probation sentences.

Law enforcement has geared up and "become very aggressive in the fight against health care fraud," agreed John Malloy, director of special investigations at Humana Inc. in Louisville, Ky. "They will take cases if there is a significant dollar amount," he said, adding that "many times, the dollar amount is rather significant."

Mr. Malloy said Humana's 24 fraud investigators have ongoing workloads of about 30 cases each and that between 50% and 60% of Humana's potential cases of fraud are handed over to law enforcement agencies.

"We have a good relationship

with law enforcement and really began focusing in 1998 on educating all of our associates" in how to detect fraud and what to do when they identify potential cases of fraud, he said.

Humana will not disclose the specific amount of money it has recovered through its special investigative unit. But Mr. Malloy said that for every \$1 spent within the investigating budget, Humana saves between \$8 and \$9 in recoveries.

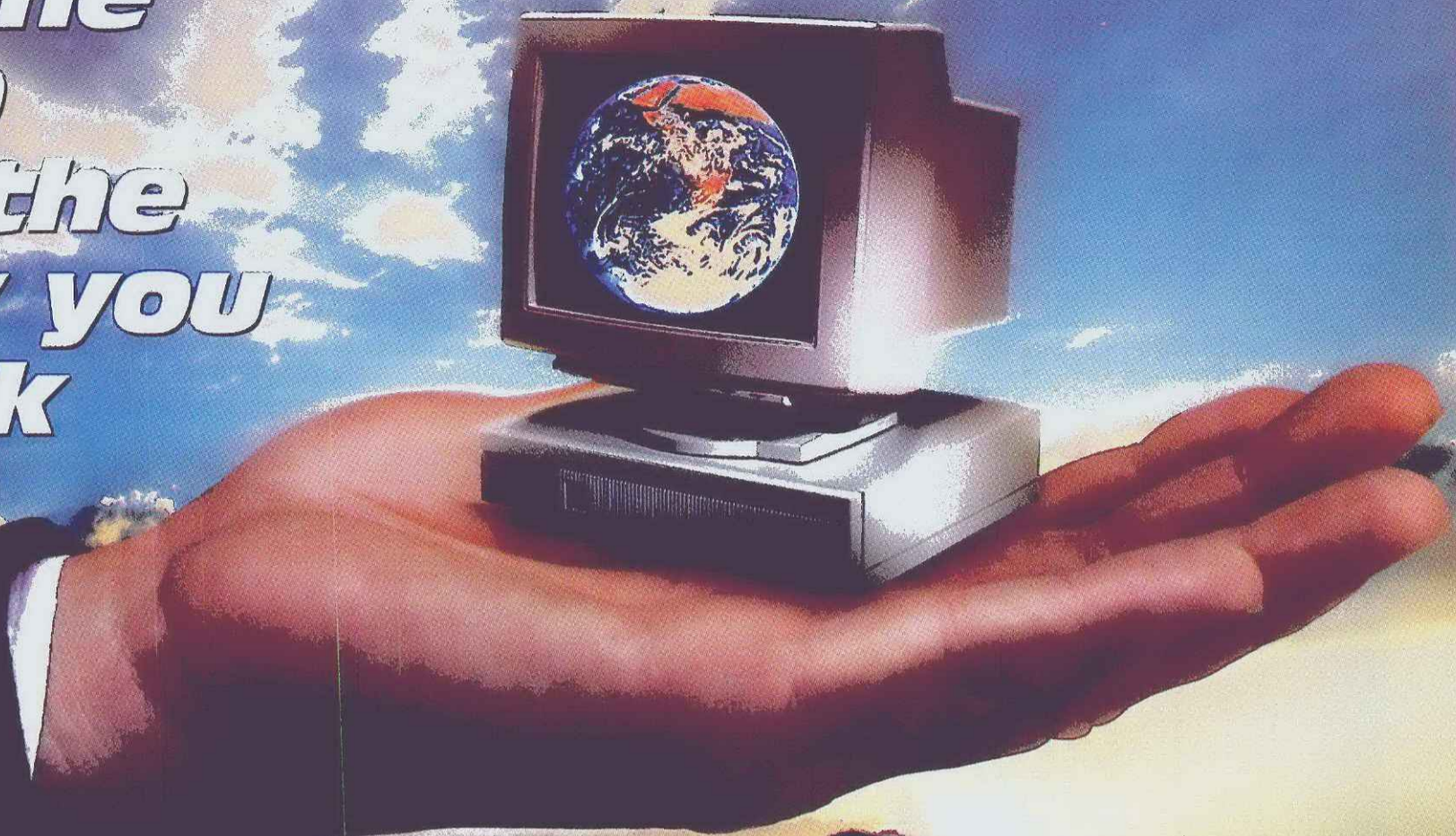
"I think that the level of awareness has risen greatly," he said. "In years past, people didn't know how to identify fraud. They are much more engaged in the identification process, and law enforcement is paying much more attention to it now."

A greater awareness of health care fraud is similarly responsible for the increased number of potential cases of fraud being flagged at Highmark today, according to Mr. Brennan.

Currently, Highmark receives an average of about 800 fraud tips each year. That is a significant increase over the period from 1992 through 1995, when the company received an annual average of only 80 to 150 referrals, Mr. Brennan said. That increase is not necessarily due to a greater number of fraud cases;

See **Health care** on page 32D

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Health care

Continued from page 32B

rather, it reflects Highmark's efforts, beginning in 1996, to educate its internal departments in fraud detection and reporting.

"Fraud was always there; it just wasn't identified," he said.

In 1998, Highmark saved \$1,032,185 through refunds, claim denials and suspensions. Of the cases the company investigated, there were 10 indictments and nine fraud convictions, Mr. Brennan said.

During the second quarter of 1999, Highmark's special investigative unit saved the company \$2.8

million, Mr. Brennan said. Taking into account all the unrecoverable funds from fraud cases resolved during the quarter, the total dollar amount of identified fraudulent activity jumps to \$8.9 million.

One of the biggest recoveries for Highmark this year came from a phony physical therapy business, U.S. Rehab, that was billing insurers for physical therapy services when, in fact, patients were receiving exercise and personal training services at Philadelphia-area fitness centers. That case resulted in restitution of more than \$3.5 million for Highmark, an amount accounted for in the first quarter. The case also resulted in prison sentences for six people.

In all, \$11.9 million in false claims were filed by U.S. Rehab and \$6.3 million was paid in reimbursement by various health insurers in the area, according to press accounts.

Mr. Brennan said the money recovered by Highmark's fraud unit is put into a fund used "to maintain premium costs." If the recovered claims can be identified as belonging to a specific account or group, Highmark will refund the money to those members.

As health care fraud has become a bigger priority for federal agencies, many states have also passed legislation establishing state insurance fraud bureaus and other insurer anti-fraud requirements.

The NHCAA's Mr. Mahon pointed to legislation in New Jersey as an example of a concerted state-level anti-fraud effort. He said the state has passed legislation that requires an insurer to have an anti-fraud plan and a special investigation unit, to train claims personnel to detect fraud, and to submit annual reports on anti-fraud activities. The state requires health insurers to have in their investigation units a staff ratio of one investigator per 60,000 lives covered by policies.

Other state-level legislation has allowed health insurers to combat fraud by sharing information.

According to the NHCAA, 46 states now grant immunity to insur-

ers for reporting suspected fraud to law enforcement authorities, and 27 states grant immunity to insurers for sharing information with other insurers.

It is very rare that an unscrupulous provider is defrauding just one company, Mr. Mahon said. The typical mode of operation, he said, includes defrauding 12 companies at one time, but in small increments, to minimizing the chance of being detected.

The trend today is that when an insurer identifies a dishonest provider or suspicious cases, it shares that information with other insurers in the hopes of detecting the activity early on, he said.

"The toughest thing in the world to do is to get the money back," Mr. Malone said. "Prevention is the key," he said, and information sharing provides a means of keeping fraud from escalating.

"It's the kind of area with no boundaries in terms of competition," noted Ms. Ingenu of CIGNA's health care investigation unit. "When it comes to health care fraud, we all work together on this."

Ms. Ingenu said that, within NCHAA, there is a database that allows insurer members to input data from investigations and to access data to see whether a particular provider under investigation has been flagged by other insurers.

Health insurers agree that technology is key to preventing and detecting fraudulent activity today.

In addition to having sophisticated analysis software that flags anomalies in claim submissions, many health insurers today also are equipped with provider profiling technology. This technology allows an investigator to construct a peer group of doctors in a specific region and to run comparisons against similar groups of doctors.

Like many of its competitors, Wellpoint Health Networks Inc., the national for-profit group health division of Blue Cross of California in Thousand Oaks, relies on technology to help identify unusual activity and patterns that warrant investigation.

"We are always looking at new systematic ways to look at preventing fraud," said Susan D'Avignon, who runs the fraud investigation unit for Wellpoint as director of internal audits.

"There is a lot of data that flows through the company," said Ms. D'Avignon, who also is a partner with Arthur Andersen L.L.P. "It's a real challenge to keep up with it and review it. There is new technology coming out all the time to get better views. We looked at a new system within the past six months to see if there's something better to help us detect more-sophisticated fraudulent schemes. We're always asking ourselves if we've got the best technology working for us."

Wellpoint also spends a lot of time on the prevention side, educating its employees about how to detect fraud, Ms. D'Avignon said.

In the future, "my prediction is that we'll see more investment in technology than we have today in

See **Health care** on page 32E

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Software aiding insurer's investigations

By GAVIN SOUTER

Fraud investigations that once took days at Prudential Property & Casualty Insurance Co. have been reduced to about 15 minutes thanks new software, according to one of the insurer's chief investigators.

By using a process that involves a few clicks of a mouse rather than sifting through thousands of files, the Holmdel, N.J., insurer has greatly enhanced its ability to crack down on fraudulent claims, said Thomas J. Mulvey, national director of the special investigation unit at Prudential.

In one instance, a quick check of an auto insurance claim revealed

that the claimant was involved in more than 70 other claims filed with Prudential and other insurers, Mr. Mulvey said.

With the system "we can review the same number of files in about 15 minutes that previously would take three to four days of an investigator's time," he said.

The software, NetMap for Claims, was developed by Alta Analytics. NetMap is linked up with the Insurance Services Office Inc.'s anti-fraud system, the ISO Claim-Search database.

By combining the vast claims information on the ISO database and the searching and cross-referencing capabilities of the software, insurers should be able to reduce considerably the costs of fraud, which has been estimated to cost the property/casualty industry as much as \$20 billion a year, said Richard P. Bcehning, president of American Insurance Services Group, a claims data unit of ISO.

The new system also will free up insurers' investigators, he said.

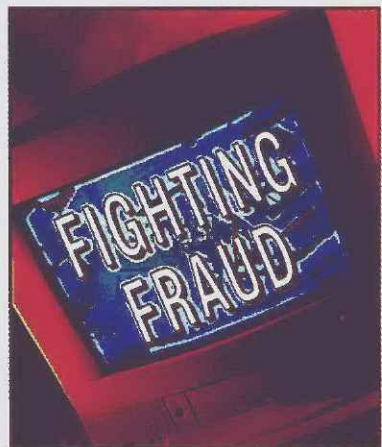
"It is a dramatic improvement in

the way they utilize their time," Mr. Boehning said.

The system allows an insurer to first cross-reference a claim with its own claims records, and then cross-reference it against 135 million other property, liability, auto, worker compensation and other claims in the ISO database.

Prudential has been using the system for about six months, said Mr. Mulvey.

In one case, a California auto claim was filed with Prudential and entered in to the NetMap system to



cross-reference it against other Prudential claims.

See **Software** on page 32H

Health care

Continued from previous page
the area of fraud detection," she said. In addition, "we'll continue to see a close working relationship (with law enforcement authorities) and see an even more open approach to working together to identify trends and share information between authorities and private carriers."

In 1998, Wellpoint investigated 2,027 potential cases of fraud, Ms. D'Avignon said. Of those cases, 393 were referred to law enforcement authorities, resulting in 20 arrests.

Aetna U.S. Healthcare also relies on its fraud and abuse management system to detect fraudulent claims, said Michael P. Stergio, director of special investigations in Middletown, Conn.

The system, which was installed in 1995, allows Aetna to measure providers' behavior patterns based on certain characteristics. For example, Aetna can view the procedures performed by all the dentists in Detroit and compare the resulting patterns against those of peer groups to identify suspicious trends.

Aetna's special investigation unit each year flags, on average, 700 cases of potential fraud, Mr. Stergio said.

Since 1992, the unit has recovered \$130.7 million from fraud investigations. "A majority of that goes back to the customers," he said.

Mr. Stergio added that, at the moment, Aetna has roughly the same amount outstanding in nine cases in various stages of litigation.

"The health care system is based on honesty, which lends itself to dishonest providers," he said, pointing out that the 97% to 98% of honest providers in the system "are the industry's greatest allies" in combating fraud.

"Nobody wants a bad cop caught more than a good cop," Mr. Stergio said. "It's the same thing with the medical profession."
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Software

Continued from page 32E

Immediately, the software showed that the claimant had used two different addresses when dealing with the insurer.

The information drew the interest of the investigator, who then went a step further in the cross-referencing process and discovered that the claimant had filed five previous claims with Prudential and had used two social security numbers, five addresses and four telephone numbers.

"So it appears that we were following the right path, because the

claimant was going out of his way to have different pieces of information to identify himself," Mr. Mulvey said.

One more click of the mouse revealed that the claimant had links

Because the software let Prudential cross-reference the claim against many others, 'A single claim with a low dollar value led to a huge potential fraud.'

— Herb Jones

with 17 other claimants. For example, they had used one of his addresses or phone numbers or they

were involved in one of his claims as a passenger or the other driver in an accident.

"Now we have the information that shows us the people and entities related to our investigation, so we go back to ISO to look at the big picture," Mr. Mulvey said.

When the software was used to access the millions of claims with other insurers in the ISO database, an even more suspicious picture emerged, he said.

The claimant was involved in 69 claims with 19 other insurers and has reported another four social security numbers, 25 ad-

resses and three telephone numbers.

When all that data was used to make a further search, it is revealed that the single claimant was linked in some way with 148 other people.

The information yielded by the software was reported to state authorities, who are conducting a criminal investigation, Mr. Mulvey said.

Without the software and the access to the ISO data, the investigation would have been far more laborious, he said.

"We would have manually accessed claims files and brought them into a room in boxes and tried to find links from claim to

claim," Mr. Mulvey said.

The investigation also allowed the insurer to uncover a very large possible fraud, said Herb Jones, president and chief executive officer of Alta Analytics in Westerville, Ohio.

"A single claim with a low dollar value led to a huge potential fraud," he said.

The initial implementation charge for the system is between \$300,000 and \$500,000, and a similar fee is charged annually.

So far Prudential and four other insurers have signed up for the system: CNA Financial Corp.; Nationwide Mutual Insurance Co.; Progressive Corp.; and Travelers Group Inc. **BI**

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Better training a key to snuffing out arson

By Ed Noonan

IN JANUARY 1996, Joe Logan, a maintenance worker at the Howard Johnson Hotel in Bowling Green, Ky., set fire to the hotel, killing four guests. This is something Mr. Logan's employer, Suresh Kumar, hadn't counted on when he paid Mr. Logan to set the blaze; he simply wanted the insurance money.

Mr. Kumar's hotel had recently been given one of the lowest quality assurance scores in the chain's history, and it was going to require \$400,000 in renovations. Interestingly, Mr. Kumar had filed six claims for fire damage at another hotel he owned in Nashville during the previous year.

In the ensuing investigation by local fire officials and the federal Bureau of Alcohol, Tobacco and Firearms, Mr. Logan confessed to the crime and implicated Mr. Kumar. Both are now serving life terms in prison.

According to the National Fire Protection Assn., arsonists are believed to set 500,000 fires in the United States each year. Unfortunately, the majority are never arrested, and only 2% of investigations result in a conviction.

And according to a study by the Law Enforcement Assistance Administration, 14% of arsons are estimated to be arson-for-profit. Applied to current statistics, that's 70,000 fires.

Bottom line? The typical arsonist is more likely to get an insurance check than a prison sentence.

As an industry, we should be deeply troubled by this. According to the NFPA and LEAA, Americans spend \$2 billion each year on arson. Here's where the money goes: \$280 million to pay criminals in arson-for-profit schemes; \$460 million to clean up after revenge incidents; \$140 million for fires set to cover up other crimes; \$280 million for fires set by the mentally ill; and \$840 million for fires set by vandals, many of them adolescents.

If every incident of arson could be proven, this crime would be the

IT Perspective

major cause of property damage due to fire in the United States. And the problem doesn't end there.

Each year in the United States, fire kills 4,000 people, injures another 20,000 to 25,000 and destroys approximately \$8 billion worth of property. In fact, the United States has one of the highest fire-death rates in the world—about 25% higher than the rate in Canada, more than a third higher than in the United Kingdom and almost 250% higher than in Switzerland.

One of the fundamental reasons for these statistics, I believe, is that we have failed to educate the public about fire-related risks. For example, a popular U.S. building style today features homes with soaring two-story foyers. While this design is architecturally imposing, fire experts describe it as a very efficient chimney—in a fire, smoke rises easily to the second story, where it can silently choke a family to death in minutes.

But there's another problem.

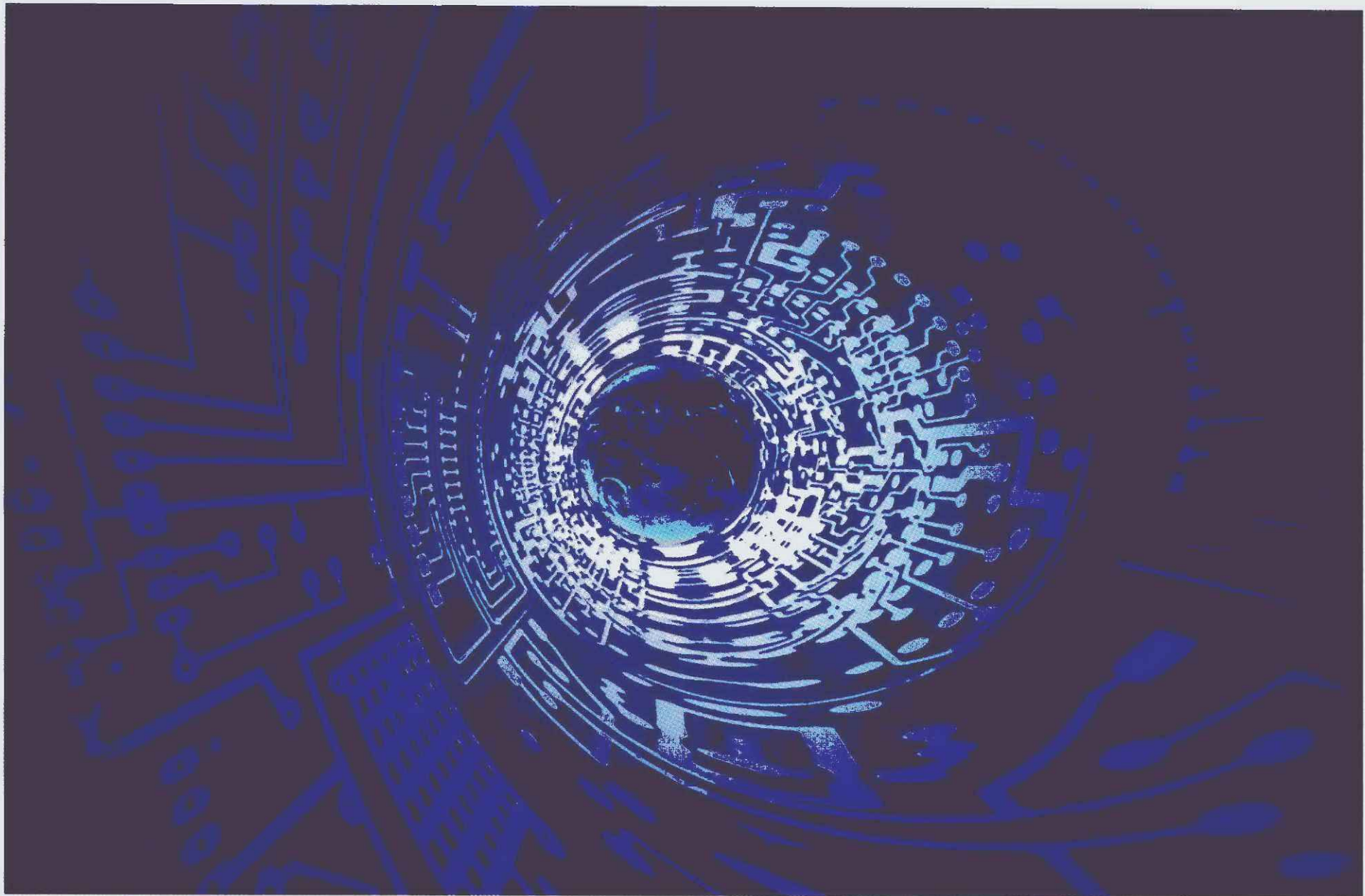
Approximately 2 million fires are reported annually in the United States. According to NFPA, the cause of roughly a third of those is recorded as "undetermined."

Why? Fire investigation is a very complex process. Many fire investigators do not have adequate training opportunities to develop the skills required to solve these cases. And those who do get training often don't have the opportunity to work enough fire scenes to maintain the skills they were taught.

To be effective, fire investigators must learn not only how to recognize, collect and preserve evidence from the charred remains of a fire, but they also must be proficient in a host of additional skills, such as interviewing witnesses, case management and testifying in court.

What can the insurance industry do? Our industry has an obligation to lead this crusade.

Obviously, developing better ways **See Fires on page 32I**



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Fires

Continued from page 32H
to select and manage risk is important to us, but we have the opportunity here to do something that will reach beyond our bottom line. Helping fire investigators develop the specialized skills necessary to better identify the causes of fire will touch communities all across the country. I think we have a responsibility to help make our communities safer places to live and work.

American Re-Insurance Co. is part of a national initiative to improve the fire investigation skills of the nation's firefighters, police and prosecutors, as well as the insurance industry.

We've partnered with the ATF, the NFPA and the U.S. Fire Administration to produce an interactive CD-ROM-based training program called InterFIRE VR.

With InterFIRE VR, users can explore an actual fire scene on a search for evidence, listen to the advice of top U.S. fire investigators or, via a resource file, see Internet links to various insurance industry databases that track insurance claims for fire loss.

This partnership has allowed each organization to specify its own "best practices" and to share information across disciplines. The benefits are significant. Some examples include:

- Firefighters will learn that, in addition to saving lives and property, they may also be entering the scene of a crime. Evidence about how a fire started can be either destroyed or preserved, depending on their actions.

- Law enforcement officials will discover the wealth of information

contained in the insurers underwriting and claim files. This information is available through existing immunity legislation in all 50 states. Investigators simply need to know how to ask for it.

Will a partnership approach like this make a difference? We think so. That's why the InterFIRE VR developers have decided to distribute as many free copies as possible to their respective audiences. For American Re, that includes our competitors in the insurance industry. This is an issue that rises above mere competitive considerations.

Beyond that, the program is available via the Internet or through a toll-free telephone information line, 877-INTERFIRE (877-468-3734), to anyone with a professional interest in fire investigation. A nominal shipping and handling fee will apply to these orders.

Of those fires classified as "undetermined" in origin, many are caused by arson, though some will surely turn out to be from less sinister causes, such as cooking, heating and appliances. (Believe it or not, the plastic housings of crockpots and similar appliances are combustible.)

Whatever the cause, when more fires are solved, more fires will be prevented, more arsonists will be caught, and more lives saved.

What can insurers do? Well, it should go without saying that you should support fire and police departments in the communities where you work. Let local officials know that you favor aggressive prosecution of arsonists.

But insurers must also walk the walk. Here are a few ways to do that:

- Participate in the fight. To combat arson, insurers have created the Insurance Committee for Arson Control, which serves as a national resource, education and communications organization.

ICAC sponsors and coordinates the activities of the National Arson Forum, a gathering of leaders from the public and private sectors to exchange information and develop new resources to aid all participants in the arson battle.

Another group is the National Insurance Crime Bureau, which provides training to insurance claims personnel and investigates questionable insurance claims, including suspected arson. Make sure your company supports such efforts.

- Share information. Does your company file its property claims with ISO ClaimSearch, which was formerly known as the PILR database? Of the 60,000 to 70,000 reports that PILR receives each month, about 14% are flagged as suspect, thereby increasing dramatically the chance that an arsonist will be caught.

- Create a special investigation unit. Rather than simply pass losses on to policyholders, many insurers have set up such units to investigate suspicious fires and collect evidence that can be forwarded to officials for prosecution.

The results of setting up an investigative unit may vary, but, on average, they save \$10 for every dollar invested, according to the International Assn. of Special Investigation Units. With that sort of return, continuing to do nothing is not an acceptable choice.

- Put teeth in your state's fraud bureau. Most states have fraud bureaus, but not all require insurers

to forward suspicious claims to their state's fraud bureau. If your state doesn't, urge your state legislators to change the law.

- Make insurance fraud a crime. Insurance fraud is illegal in all states, but some laws are more effective than others. Prosecuting insurance fraud is easier in states where it is identified as a specific crime in the penal code and where the elements that constitute insurance fraud are defined, along with the penalties that can be imposed. Otherwise, it falls under general fraud provisions such as fraud by deception. Again, talk to your legislators.

In the five minutes it took to read this article, arsonists set five fires,

starting almost 1,400 each day. That's five arsonists who should go to jail but probably won't. That is countless businesses and lives destroyed. And that is too high a price for our society and our industry. **BI**



Ed Noonan is chairman and chief executive officer of American Re-Insurance Co. in Princeton, N.J.

Regulators target sales of bogus notes

By SARA HANSARD

Crain News Service

Securities regulators are cracking down on an estimated 1,000 insurance agents coast to coast over the sale of worthless promissory notes that may have cost investors as much as \$100 million over the past two years.

The agents' main selling point was that the notes were secured by a number of insurance companies. The agents told their potential buyers—mainly senior citizens—that the notes were as safe as bank accounts or certificates of deposit, explained Laura Royal, a senior investigator in the Florida Department of Banking and Finance.

Ms. Royal, who is coordinating

the 16-state crackdown, said more than two dozen agents have been charged so far. "You'll see more actions in the near future," she said.

Federal officials have linked one of the companies involved with one of the insurers, based in Barbados, to organized crime figures recently indicted in a high-profile stock fraud case.

Ms. Royal counts about two dozen potential offerings that may be connected to the scheme. The interest payments "have either bounced or are not forthcoming," she said. "The more we talk to the agents, it seems we find one more offering every couple of weeks."

Ms. Royal said, "The worst part of my job is to have to tell the victims, 'I don't think you will get your money back.'"

One such victim is 62-year-old Marine Sheely, who works at a minimum-wage job at Goodwill Industries in Toledo, Ohio. Ms. Sheely said, "My whole life savings is gone. My son's in a rest home. I feel like ending it all."

Ms. Sheely said she bought a nine-month \$88,000 note with a 10.9% interest rate issued by World Vision Entertainment Inc. of Orlando, Fla., from James Chmielowicz, a chartered life underwriter who then was vp and general manager of Vaughn Williams & Associates Inc. in Toledo.

Owner Vaughn Williams Jr. said he recently fired Mr. Chmielowicz, after 16 years at the firm, for selling the notes without authorization.

"He was told three years ago, 'Jim, you are not authorized in any way to do that through Vaughn Williams & Associates, because we want no part of that,'" Mr. Williams said.

Mr. Chmielowicz said he sold the notes through Fraternal Services Insurance in Pittsburgh. Fraternal Services did not return calls.

"I've had many clients over the past couple of years that have had the notes and taken the money out." But recently, Mr. Chmielowicz said, two clients who hold World Vision notes haven't been paid.

Ronnie Tyre, 58, of Charlotte, See **Notes** on page 32L

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1998 DIRECTORIES

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Feb 2	Utilization Review Providers & Case Managers
Feb 16	Third-Party Administrators
Mar 2	Benefit Information & Claims Systems
Mar 16	Risk Management Consultants
Apr 6	401(k) Plan Administrators
Apr 27	Captive Managers
May 25	Environmental Risk Management Consultants
Jun 8	Alternative Risk Financing Facilities
Jun 15	EAPs & Dependent Care Resources & Referral Services
Jul 20	Agents & Brokers
Aug 3	Prescription Benefit Managers
Aug 17	Property Loss Control Consultants
Aug 31	Leading Reinsurers Worldwide
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Nov 9	Reinsurance Brokers
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1999 DIRECTORIES

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Notes

Continued from page 32f

N.C., said he lost \$550,000 of the nearly \$1 million he invested in late 1997 and early 1998 in notes sold by Reeves-Marcus Ltd. of Charlotte.

Alan Elam, president and owner of Reeves-Marcus, could not be reached for comment, according to his assistant.

Mr. Tyre, who had retired from his own medical supply business, is looking for work once again. He said his father also lost \$100,000. "I don't expect, realistically, to get my money back," Mr. Tyre said, "but I'm going to put these guys out of business one way or another."

Ms. Royal said it wasn't until state regulators convened in May in Tampa, Fla., that they understood how widespread the selling of the notes had become.

David Sutton, assistant statewide prosecutor for Florida, said the insurance agents "have varying degrees of culpability. The top people recruited the agents. Some of them had reason to believe this was (nonsense); some didn't."

That's small comfort to Ms. Sheely. She said Mr. Chmielowicz told her, "Oh boy, have I got a deal for you." The beginning of July, he was supposed to send it in six installments. Nothing so far. . . I work hard. . . I'm so darn tired."

Like Mr. Chmielowicz, the other agents typically worked for small, independent agencies and are not connected with big insurers, ac-

ording to regulators. They have formed a task force called States Working Intrastate Fraud Together, or SWIFT, to combat the operation.

SWIFT is working in California, Florida, Georgia, Indiana, Kentucky, Maryland, North Carolina, Pennsylvania, Ohio, South Carolina, Texas and Utah. The task force will receive cooperation from officials in Mississippi, Nebraska, North Dakota and Wisconsin.

Ms. Royal said about 10 start-up businesses throughout the country were involved, issuing millions of dollars in promissory notes that were payable over nine months. Many of the notes were backed by Tangent Insurance Co. of Barbados, which, she said, "has never paid on any of these bonds."

Securities regulators have served World Vision and four other companies with cease-and-desist orders against issuing any additional notes. The other companies are Lifeblood Biomedical of Orlando; Ameritech Petroleum Inc. of Dallas; Capital Acquisitions Inc. of Denver; and Yucatan Investment Corp. Inc. of Lapaz, Ind.

Other companies remain under investigation, Ms. Royal said. She added that agents of Fraternal also sold promissory notes for Lifeblood.

Attorneys for the companies and their officers did not return calls.

Another company that used Tangent as its bonding agency, Legends Sports Inc. of Altamonte Springs, Fla., was closed by the Securities and Exchange Commission in 1996 for the sale of unregistered securities.

Legends was named as one of the companies whose stock was manipulated in a case brought in June by the U.S. attorney's office in Brooklyn, N.Y. Eighty-five people were indicted in one of the largest-ever stock fraud roundups. Some of the indicted individuals were linked to organized crime, prosecutors said.

Florida has also charged more than two dozen insurance agents in state court in connection with the note scam. Charges include the sale of unregistered securities and unauthorized insurance, and the sale of securities by unlicensed dealers.

Those agents "did not bother to call the Department of Insurance to find out if it was unlawful for an offshore bond company to sell the notes in Florida," which requires a certificate of authority, said Mr. Sutton, the state prosecutor. He said he also has charged several people with racketeering and securities violations in connection with the case.

In April, Maryland started administrative action against Brian Schutsky, who operates BLS Insurance Service in Keymar, for securities violations in connection with the notes. Mr. Schutsky has denied the charges, his lawyer said.

Mr. Tyre said he invested after reading an ad in the Charlotte Observer newspaper. The ad read: "No stock market risk. 10-15% fixed return on your investment. No fees, no loads ever. The principal is guaranteed. Your interest is guaranteed. IRAs, Roth IRAs, SEPs, 401(k)s accepted."

A secretary at Reeves-Marcus said: "We do not sell promissory notes any more. The ad we place on Sundays is for something else."

But a spokesperson for the Observer's retail advertising department said that Reeves-Marcus, which had run the ad last year, recently resumed running it. The ad has appeared several times in recent months.

Ms. Royal, the Florida investigator, explained the scam: "The companies need capital. They get involved with these brokers that promise to raise money for them. They raise a lot of money real quick through the insurance agents."

"There's no way you can pay a nine-month note back," she continued. "We're seeing an average of \$5 million to \$10 million per company."

The start-ups have little revenue and end up defaulting, she said.

An official of one company, former Legends Sports President James Staples, recently pleaded guilty to racketeering, organizing a scheme to defraud, conspiracy, securities fraud and other violations in Florida's Sanford County Circuit Court. The court handed down a \$12 million judgment against Mr. Staples.

His lawyer, David Fussell, declined to comment.

Donald Lykkebak, the lawyer for David Trotter, an insurance agent who recruited others to sell the Legends Sports notes, said his client has pleaded not guilty to the racketeering charges.

"The agents are the innocent people in this whole matter," said

David Ervin of Fern Park, Fla., who represents Greenville, S.C., insurance agent Gregory Elie. Mr. Elie sold one \$130,000 promissory note for Legends and is contesting three securities charges.

"The real bad guys are at the top, the ones that ran Legends Sports," said Mr. Ervin. "And the state has settled with Staples."

A Florida statute stipulated that promissory notes that mature in nine months or less time "are not securities, and they are exempt from the securities laws," Mr. Lykkebak said. "So it's quite an arguable issue as to whether or not these were securities."

The state has since changed its law, however, to require that short-term notes be high-quality commercial paper.

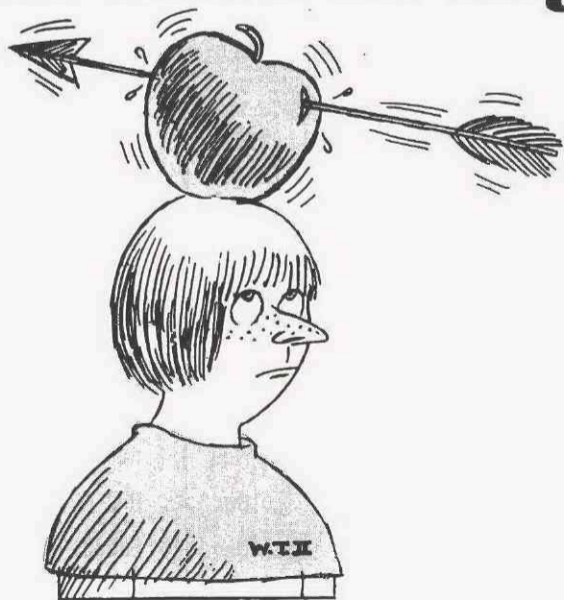
Kyle Trimble, an examiner with the Kentucky Department of Financial Institutions, said the annual interest rates promised for the notes were 10.75% to 11%, on top of commissions of 13% to 15%. Insurance agents were paid 6% to 8% of the commissions, he said.

David Jonson, deputy attorney general of the South Carolina Securities Division, who is investigating similar cases, said he sees the insurance companies as potentially liable for inadequately supervising their agents.

"Insurance companies are possibly looking at substantial liability," he said. "Insurance commissioners are aware of this."

Sara Hansard is a reporter for *Investment News*, a sister publication of *Business Insurance*.

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IT Briefs

Fraud alliance

PALOS HILLS, Ill.—An alliance announced last week between the National Insurance Crime Bureau and US Investigations Services Inc. will give insurers a weapon against internal fraud.

US Investigations, an Annandale, Pa.-based company, will conduct investigations when internal fraud is suspected at member companies of the NICB.

James Spiller, associate vp of the

Palos Hills, Ill.-based NICB, said in a written statement that the alliance represents a significant benefit for the more than 1,000 insurers that belong to the NICB.

"Internal fraud costs our members millions of dollars every year," Mr. Spiller said. "As the insurance industry grows and changes, the potential for internal fraud will increase. This alliance puts us in an excellent position to address internal fraud now and in the future."

Bank name changed

INDIANAPOLIS—The directors of NAMIC Bancorp, the holding company affiliated with the National Assn. of Mutual Insurance Cos., have renamed its financial institution Assurance Partners Bank.

The new name replaces NAMIC Bank, the name used since the association first decided in 1997 to pursue a federal thrift charter.

Assurance Partners Bank will provide insurance agents and policyholders of investor companies and other prospects a number of financial products and services through a variety of delivery channels.

The bank will conduct business nationwide from its headquarters in Carmel, Ind., and initially will offer home equity, automobile and personal consumer loans, first residential mortgages and small-business loans. **BI**

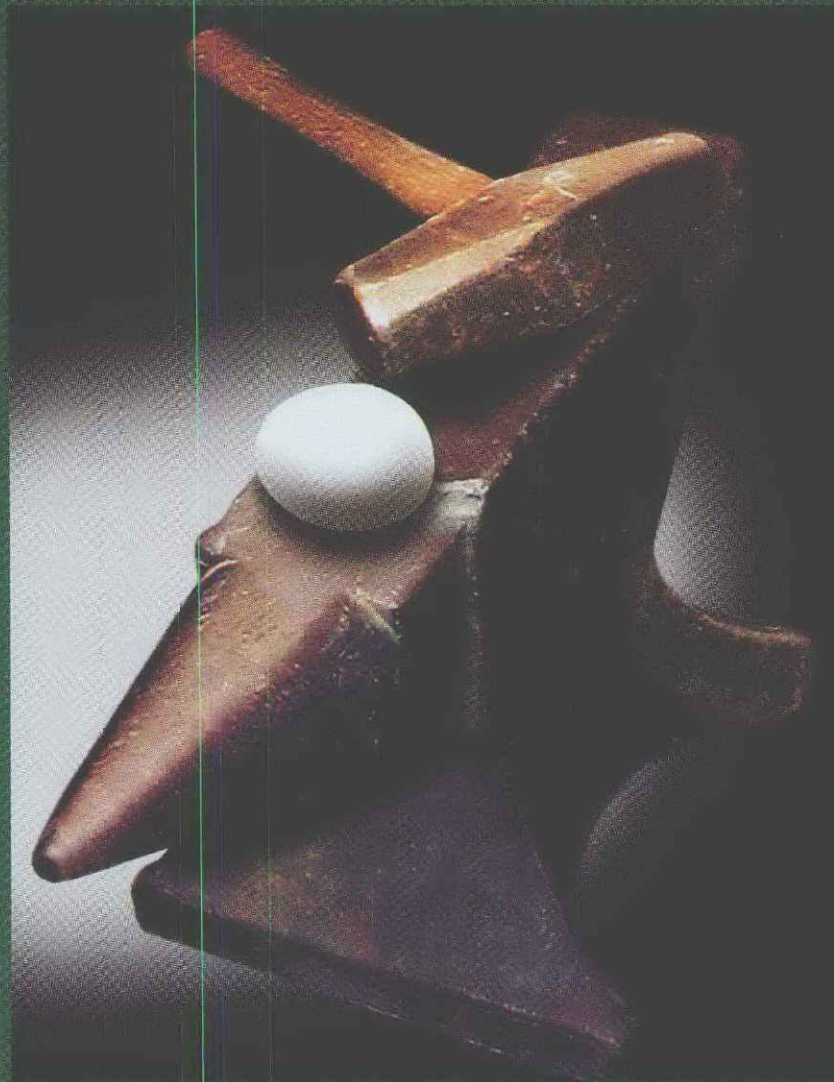
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Parents can bear liability for acts of 'children'

By Jeffrey B. Kirschenbaum

IMAGINE THIS: THE CALL you have just received comes as a bit of a surprise—an unexpected voice from the distant past. And though your last communication ended on a positive note, you can't say you are happy to be hearing from him today.

In the world of business risk and liability, no news is good news—and lawyers, you've learned, rarely call just to chat. It is general counsel for DeltaHoldings, a company that your investment group, NewVentures, committed a substantial amount of money to in the 1980s, based on the then-value of Delta's stake in a wide—some would say bewildering—array of businesses. As you recognize his voice, you realize that you haven't spoken to him since the fall of 1989, the day your majority share in Delta became final. It was a red-letter day for your group. Delta's pharmaceutical businesses in particular showed exceptional promise, and you and your partners were thrilled to add them to your increasingly diversifying portfolio.

But the voice on the other end sounds troubled, and the news he is conveying is not at all good.

When you make sense of everything he has to say, you begin to feel differently about that special day in 1989. Delta is facing a government-mandated environmental cleanup action. Among the many businesses that Delta accumulated in the merger-driven '80s were several chemical plants in Ohio and Pennsylvania, and potential liabilities arising from those acquisitions are finally coming to light. In addition, the stock valuation of Delta has taken a beating in recent months, and there is a serious question whether the company will be able to pay for the cleanups and remain in business. But that is not all.

General counsel for Delta is telling you—implores you—to contact your lawyers, because the federal government has named your company as a party to the cleanup action.

The theory upon which the action is based is that your investment group is the alter ego of Delta, and therefore should contribute toward the costs of cleaning up half a dozen sites.

How could this have happened? General counsel patiently explains that the law allows for such suits, and that a recent U.S. Supreme Court case—*United States vs. Bestfoods*—explicitly acknowledges the validity of alter-ego liability in the context of government-mandated cleanups. The theory is that if a parent company is, in the eyes of the law, identical with the subsidiary, then the courts will allow aggrieved investors to dig into the deeper pockets of the parent. He further explains that the law, as enunciated, is meant to protect investors from fraud.

But naturally, you wonder, why me? What fraud has my company perpetrated? How can we be the alter ego of a company that we do not control, whose offices are across the country? And, by the way, I thought the point of investing in Delta, as opposed to taking over management, was to cede control and liability for the company's operations. Doesn't the law of corporations protect parents from such liability? How did the shield of corporation law that was supposed to protect us suddenly become a sword?

Such questions are certainly understandable. Few corporate parents think about the further potential liability that a subsidiary company might incur. Parents should and do expect the full protections provided under corporate law—most importantly, the promise that the parent will be free from liability for the subsidiary's losses. It is often said that the corporation is like a veil that shields its shareholders from corporate debts and similar obligations. If a judgment is entered against a corporation, its shareholders will be liable only for the amount of their investment in the corporation; the shareholders' personal assets are not subject to liability. Thus, the very strong and time-honored law of corporations protects the shareholders from liability beyond their investments.

But therein lies the rub—that is, the strength of the corporation to act as a shield, even on occasion against reasonable claims beyond the shareholders' investment. The protections of the corporation are so strong, in fact, that the courts need to ensure that these protections are not exploited for the purpose of defrauding investors.

Where the act of incorporation was carried out to perpetrate a fraud—such as where an unscrupulous manager sets up a shell corporation to take money from unsuspecting investors—the courts will allow the investors to “pierce the corporate veil” and sue the shareholders for personal assets.

In the context of a parent/subsidiary relationship, that means that corporate parents could be liable. To succeed in such a lawsuit, however, plaintiffs would need to establish that the parent and the subsidiary are “alter egos”—i.e., that for all intents and purposes, the parent and the subsidiary are one and the same entity. In most states, this argument requires a bottom-line finding that there was a “unity of interests” between the two corporations. Under well-established federal law, “unity of interests” is measured by determining the amount of respect given by shareholders to the separate identity of the corporation.

Thus, a corporate parent may be found liable for alter-ego liability for failure to accord its subsidiary a separate identity. And despite the public policy on which alter-ego liability is based, the courts in some jurisdictions may rule in favor of the plaintiff without a finding of fraud. In those states, a corporate parent would be well advised to avoid

The legal theory is that if a parent company, in the eyes of the law, is identical with the subsidiary, the courts will let aggrieved investors dig into the deeper pockets of the parent.

even the appearance that the two corporations are identical, a point addressed in more detail below.

Just as important to consider is the basis for Delta's environmental liability—the far-reaching Superfund law, formally known as the Comprehensive Environmental Response, Compensation and Liability Act. With an eye firmly fixed on expeditious cleanups, CERCLA imposes liability on a broad class of persons without regard to fault. Section 107 of the Act holds liable:

- Past and present owners of any location where hazardous substances have come to be located.
- Past or present operators of locations containing hazardous substances.
- Anyone who accepted hazardous substances for transport to the location.

Despite the strength and breadth of CERCLA, only recently have corporate parents begun to worry that they, too, might be held liable for environmental liabilities facing their subsidiaries. As noted earlier, in most cases corporate parents may rightly seek refuge behind the corporate veil. In the *Bestfoods* case, the Supreme Court noted that there was “nothing in CERCLA which purported to reject” this “bedrock principle” of corporate law.

Still, the court noted that there was nothing in CERCLA purporting to reject “an equally fundamental principle of corporate law”: that “the corporate veil may be pierced and the shareholder held liable for the corporation's conduct when the corporate form would otherwise be misused to accomplish certain wrongful purposes, most notably fraud, on the shareholder's behalf.”

Thus, the very far reach of CERCLA—a law that has ensnared countless parties in long and expensive litigation, also can extend to corporate parents in cases where state law allows the corporate veil to be pierced. As noted above, in some states the veil may be pierced even absent a showing of fraud.

For some corporate parents, what is needed is a complete rethinking of the parent/subsidiary relationship. For others, it may just involve a careful effort to translate common sense notions into a firm, corporate policy. Here are a few key pointers for corporate decision-makers.

• **Insist upon independent management.** The most potentially damaging facts in alter-ego lawsuits are those supporting the plaintiff's claim that the two companies are

not managed independently. Parents should avoid the appearance that they can wear one of two hats, depending on the managerial problem they face.

There are several ways that courts approach this issue. First, a court may examine facts suggesting that the key decision-makers are not employees of the subsidiary but rather employees of the parent. In fact, often the parent and the subsidiary “share” employees—a questionable practice if only because it might lend the appearance of an alter-ego relationship. At the very least, parents should make sure that the subsidiary can govern itself as an independent organization, even if ultimately it must answer to the parent. In the case of Delta, the decision to designate a director of the parent company to serve on the joint venture's management committee could prove disastrous in court.

In the *Bestfoods* case, the Supreme Court noted that a parent that involves itself in the affairs of a company may be subject to liability under two different theories. If the management of the company and the parent are in fact the same, the government may prevail under the theory that the company is the alter ego of the parent. This can be characterized as derivative liability assumed by the parent. In addition, a parent may be subject to direct liability in cases where an officer for the parent took actions that put the subsidiary at risk. Such was the case in *Bestfoods*. Even though the Supreme Court found that the corporate parent was not subject to derivative (alter ego) liability, the factual record showed that the parent was perhaps subject to direct liability because of independent actions taken by an employee of the parent.

The court noted evidence of such actions in the record developed by the trial court. The district court found that the defendant “became directly involved in environmental and regulatory matters through the work of Williams, (the defendant's) governmental and environmental affairs director. Williams became heavily involved in environmental issues at (the chemical plant). He actively participated in and exerted control over a variety of (the plant's) environmental matters, and he issued directives regarding (the plant's) responses to regulatory inquiries.”

The court concluded that this evidence created the possibility that the defendant parent corporation may have been directly liable for the alleged environmental damage in the CERCLA suit. The *Bestfoods* decision, therefore, should serve as a cautionary tale to corporate parents that involve themselves intimately in the managerial affairs of their subsidiaries: As the U.S. Supreme Court has amply demonstrated, there is more than one way to skin a cat.

• **Fiscal management.** In the world of alter-ego liability, there is perhaps no greater threat to the corporate parent than the “commingling” of funds. In fact, the commingling of money is often counted among the most persuasive types of evidence in alter-ego liability suits. U.S. courts will consider the following as evidence of a lack of fiscal independence:

- ✓ The parent treated the subsidiary's assets as its own.
- ✓ The diversion or commingling of assets.
- ✓ Undocumented loans or advances from the parent to the subsidiary.

✓ The subsidiary has no payroll or checking account. Back to our hypothetical case, NewVentures' practice of issuing undocumented loans and advances may be evidence of commingling, even though ownership of the funds is carefully tracked through journal entries. Attempts to justify the arrangement on grounds that its purpose was simply to minimize bank charges would probably fall upon deaf ears in the context of an alter-ego lawsuit. At most, this logical explanation would be considered a mitigating factor.

• **Be formal.** Many parents unwittingly run their subsidiaries without regard to legal and corporate formalities, which can put parents at great risk. The courts have considered the following factors when deciding whether alter-ego liability is appropriate:

- ✓ The subsidiary's failure to issue stock to the parent.
- ✓ Inadequate or incomplete corporate minutes.
- ✓ Maintenance of the subsidiary's records in the

See **Liability** on next page

Liability

Continued from previous page
parent office.

✓ The failure to remain in "good standing" in the state of incorporation.

To avoid liability, a parent who is involved in the business operations of its subsidiary should make certain that the subsidiary operates under the same corporate and legal strictures that apply to all independent businesses.

Finally, parents should remember the warning struck at the outset: that a plaintiff may base a lawsuit on the subsidiary's mere appearance as the alter ego of the parent. The truth is that, in a court of law, appearances do matter. Here are some other factors that the courts consider when deciding alter-ego liability:

✓ Subsidiary has no full-time employees, only

independent contractors.

✓ Using parent company letterhead, business cards.
✓ Same address and telephone number for parent and sub.

✓ Confusing/similar names.

✓ References to the "Group," i.e., parent and subsidiary, in correspondence and agreements.

Several other factors discussed in this article may very well fall into the category of things that give the appearance of an alter ego when in fact there is none. For example, a subsidiary may not conduct its payroll with its own bank account because it was deemed more efficient to delegate that operation to the parent company. Or the subsidiary and parent may share employees for certain tasks for economic reasons.

However sound the policies that drive these practices, parent companies should be aware that these practices ultimately might lend credence to an alter-ego liability

claim. It may be that the oft-neglected corporate policy of risk management should rule the day on this issue. In any case, keeping the hazards of alter-ego liability in mind when laying down the foundations for a subsidiary should help parents ensure that the two companies are independent, both in fact and in the eyes of the law. **BI**



Jeffrey B. Kirschenbaum is a managing partner in the San Francisco law firm Berg & Parker L.L.P.

Author offers compelling account of 1900 hurricane

"Isaac's Storm"

By Erik Larson

Crown Publishers, 201 E. 50th St.,
New York, N.Y. 10022; 212-751-2600
\$25

By Mark A. Hofmann

Nearly a century ago, when no one bestowed names such as Andrew and Floyd upon hurricanes, a nameless horror engulfed Galveston, Texas.

On Sept. 8, 1900, a hurricane unlike any in memory struck the booming coastal city. When it subsided, it left the city in ruins and at least 6,000 of its residents dead. Galveston, then locked in a fierce commercial rivalry with Houston, never fully recovered its prominence.

Erik Larson—a former staff writer for the Wall Street Journal who now contributes to Time, the Atlantic Monthly and other national magazines—dubs that nameless hurricane "Isaac's storm," after Isaac Monroe Cline, the head of the U.S. Weather Service's Galveston station. The tale Mr. Larson weaves in his book intertwines the story of the hurricane, from its probable beginnings—"it began, as all things must, with an awakening of molecules"—to its grim aftermath and beyond, with that of Isaac Cline.

The Isaac Cline that emerges in this account is a complex and, in some ways, tragic figure. He was, foremost, a man of science, a medical doctor who studied climate and health. He was a family man, a Sunday school teacher and a sometimes-quarrelsome brother. He was also more than a bit of a self-promoter, particularly during the 55 years he lived beyond the storm.

After Mr. Larson describes how the sight of the angry sea led one of Dr. Cline's neighbors to telegraph his wife—

Books & Ideas

who was then heading home via the railroad—to stay in San Antonio because he feared a great storm would strike the city, the author notes:

"Legend holds that the sea convinced Isaac of the same thing—that he raced back to the office, galvanized the station into a flurry of action, then sped back to the beach and warned everyone he saw to flee the city or retreat to the center of town. Later, Isaac took personal credit for inciting 6,000 people to leave the beach and its adjacent neighborhoods. If not for him, he claimed later, the death toll would have been far higher. Perhaps even double.

"But Isaac's response, and that of his station, was, in reality, more ambivalent..."

Risk managers, loss control experts and claims professionals should all find "Isaac's Storm" hard to put down. It bristles with human drama, and its technical—yet immensely readable—description of how the storm developed ranks among the best scientific writing that has appeared in the general book market for some time. Mr. Larson portrays the storm in a style that varies from the almost lyrical to an eerie and calm recitation of facts that is menacing in its straightforwardness.

Consider these passages:

"The hurricane had begun sculpting the Gulf the moment it left Cuba, and now it transmitted storm swells toward Galveston.

"Waves form by absorbing energy from the wind. The longer the 'fetch,' or the expanse of sea over which the wind can blow without obstruction, the taller a wave gets. The taller it gets, the more efficiently it absorbs additional energy. Generally, its maximum height will equal half the speed of the wind..."

And: "Whenever a deep-sea swell enters shallow water, its leading edge slows. Water piles up behind it. The wave grows again. It is this effect that makes earthquake-spawned tsunamis so deceptive and so deadly. A tsunami travels across the ocean as a small hump of water but at speeds as high as 500 miles an hour. When it reaches land, it explodes."

Mr. Larson's descriptions of the storm's impact and its aftermath, drawn from eyewitness accounts, rank among some of the most gripping passages in recent non-fiction. They're on a par with those in Sebastian Junger's best-selling "The Perfect Storm."

Isaac's storm is little remembered today. It did not become the stuff of legend. Nor did Isaac Cline himself, despite his efforts to the contrary. By the time of his death in 1955 at the age of 93, he was little recognized, except within a small circle of individuals interested in hurricane forecasting, and among certain art experts, for the weatherman had become a shrewd collector and seller of Chinese bronzes and Early American portraits.

"Isaac's Storm" should restore the man and the storm to the more prominent places in the history of natural disaster that both merit. **BI**



Mark A. Hofmann is Washington Editor of Business Insurance.

Injured bagel-buyer entitled to comp benefits: Court

An employee injured when she slipped and fell while buying bagels for an office Christmas breakfast that her boss has instructed her to coordinate was entitled to workers' compensation benefits, the Court of Appeals of North Carolina ruled.

Marilyn S. Floyd was employed by First Citizens Bank in December 1993 when she slipped and fell while buying bagels for an office Christmas breakfast that her boss had instructed her to coordinate for the bank's entire city office. Ms. Floyd suffered a serious back injury as a result of the fall. She filed for and was awarded workers compensation benefits. The employer appealed.

On the appeal, the employer argued that Ms. Floyd's injury did not arise in the course of her employment. The court said that where the "... fruit of certain labor accrues either directly or indirectly to the benefit of an employer, employees injured in the course of such work are entitled to compensation under the Workmen's Compensation Act." The court said it is clear that when a superior directs a subordinate employee to go on an errand or to perform some duty beyond his normal duties, the act expands to encompass injuries occurred while she was engaged in activity directly related to the employer's request that she

Legal Briefs

coordinate the breakfast. The court affirmed the award of benefits.

Floyd vs. First Citizens Bank, Court of Appeals of North Carolina, March 2, 1999 (BI/01/O.-\$10).

Exclusion ruled unambiguous

An exclusion in a business interruption insurance policy for losses caused by power failure occurring away from the insured premises was not ambiguous, according to the Supreme Court of South Dakota.

Lakes' Byron Store Inc. operates a hunting resort on Lake Byron near Huron, South Dakota. Auto-Owners Insurance Co. issued a policy to Lakes' providing coverage for business interruption but excluding losses caused by power failure occurring away from the insured premises. A severe snow and ice storm hit the area Oct. 23, 1995. Power poles and lines were broken across much of South Dakota. Lakes' was without power from Oct. 23 through Oct. 31. It submitted a claim for food spoilage and

business interruption. The insurer denied coverage because the power failure occurred away from the premises. Lakes' sued the insurer for breach of contract. The trial court ruled for the insurer.

On appeal, Lakes' argued that the description of the premises was ambiguous. But the court was satisfied that the insured premises was limited to Lot 1 and the buildings located thereon and did not include the leased lands used for hunting purposes. The court noted that none of the power poles or lines located on Lot 1 was damaged. Therefore, the court agreed with the trial court that the power failure occurred away from the described premises and the exclusion precluded coverage.

Lakes' Byron Store vs. Auto-Owners Insurance, Supreme Court of South Dakota, Feb. 24, 1999 (BI/05/Au.-\$10). **BI**

These abstracts were prepared by Mayo H. Stiegler. Copies of these decisions are available by sending a \$10 check payable to Mayo H. Stiegler, to Business Insurance, 740 N. Rush St., Chicago, Ill. 60611-2590. List the number for each opinion.



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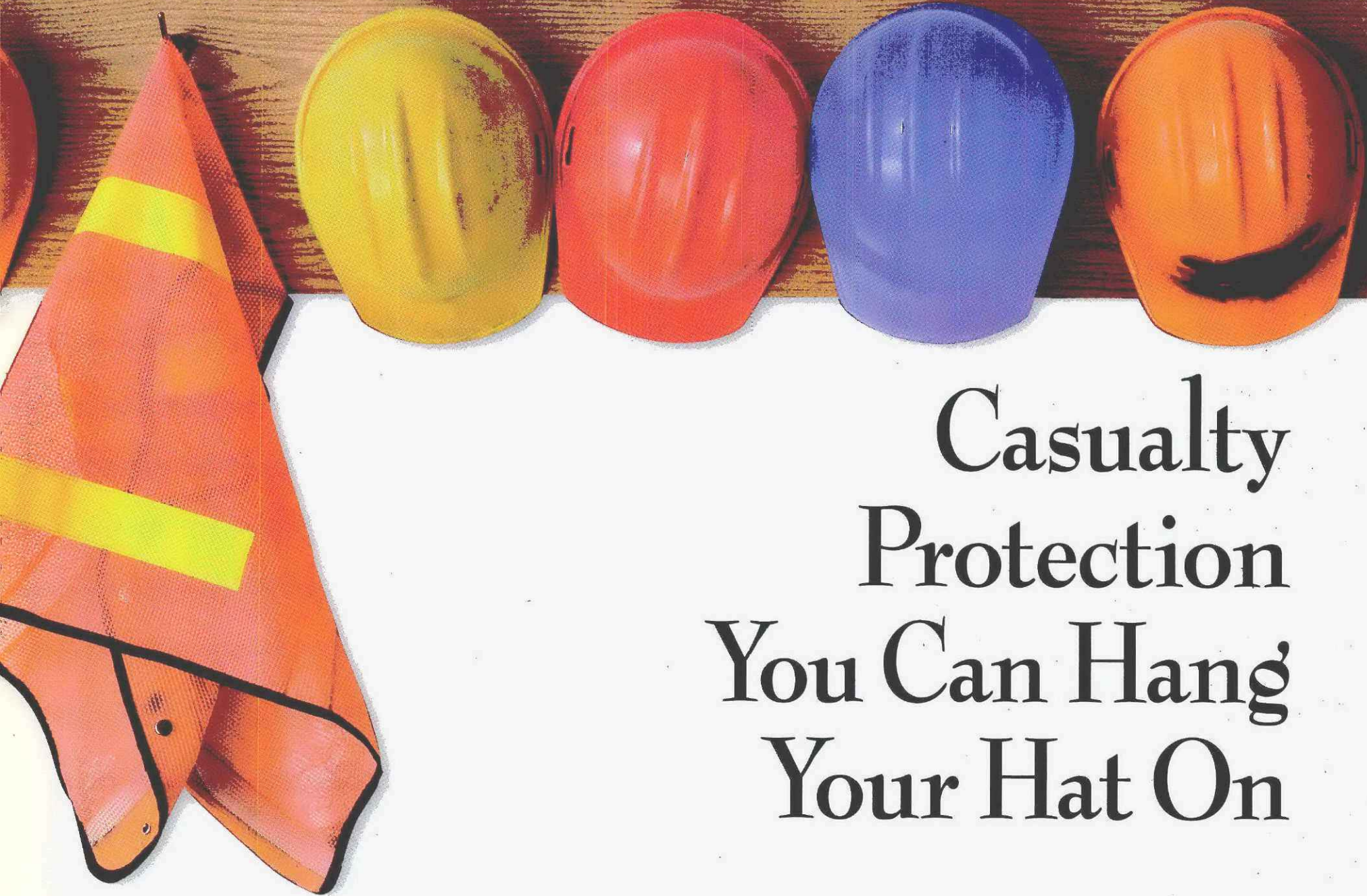
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SEPTEMBER

SEPT. 23-24. Environmental Liability Management Conference in Dallas, sponsored by The Institute for International Research; \$1395 for main conference only. Institute for International Research, P.O. Box 102914, Atlanta, Ga. 30368-2914; 888-670-8200.

SEPT. 23-24. Insurance Industry and Information Technology Solutions conference in Irving, Texas, sponsored by META Group's Insurance Information Strategies; \$636 for META Group clients and \$956 for all other attendees. META, www.metagroup.com; 800-945-6382.

SEPT. 25-29. National Assn. of Life Underwriters annual convention in Nashville, Tenn., sponsored by the NALU; \$325. cdixon@nalu.org; 202-331-6032.

SEPT. 26-28. LOMA's annual conference in San Diego, sponsored by the Life Office Management Assn; \$595 for members of LOMA and \$835 for others. www.loma.org; 800-275-5662, ext. 5.

SEPT. 26-29. American Health Care Assn. conference in Honolulu, sponsored by AHCA; \$495 for members and \$695 for non-members. www.ahca.org; 800-797-7491.

SEPT. 27-OCT. 1. Independent Insurance Agents of America Annual Convention and Trade Show in Las Vegas, sponsored by IIAA; \$469 for members and \$545 for non-members. IIAA, 127 S. Peyton St., Alexandria, Va. 22314; 800-221-7917.

SEPT. 28-30. Advanced Pension Conference in Chicago, sponsored by Corbel/PPD; \$750. Corbel Educational Services, www.corbel.com; 800-326-7235, ext. 1237.

OCTOBER

OCT. 2-6. National Assn. of Insurance Commissioners Fall National Conference in Atlanta, sponsored by the NAIC; \$425. NAIC Meetings Department, P.O. Box 87-5410, Kansas City, Mo. 64187-0335; 816-889-4400.

OCT. 3-5. 1999 Managed Care Institute in Palm Beach Gardens, Fla., sponsored by the Healthcare Financial Management Assn.; \$795 for members and \$895 for non-members. HFMA, Terry Arya, 2 Westbrook Corporate Center, Suite 700, Westchester, Ill. 60154; 800-252-4362, ext. 362.

OCT. 3-6. American Society for Healthcare Risk Management annual conference and exhibition in Chicago, sponsored by ASHRM; \$475 for members and \$575 for non-members. ASHRM, 1 N. Franklin St., Chicago, Ill. 60606; 312-422-3980.

OCT. 3-6. Disease Management Congress and Exposition in Boston, sponsored by the National Managed Health Care Congress; \$1,395. NMHCC Inc., P.O. Box 102713, Atlanta, Ga. 30368-2713; 888-882-2500.

OCT. 3-6. International Society of Certified Employee Benefit Specialists Symposium in Orlando, Fla., sponsored by ISCEBS; \$650 for members and \$750 for non-members. Edye Biwer, ISCEBS, P.O. Box 209, Brookfield, Wis. 53008-0209; 414-786-8771.

OCT. 4-5. Indoor Air Quality Seminar in Atlanta, sponsored by Air Quality Sciences Inc.; \$525. Air Quality Sciences Inc., aqs@mindspring.com; 770-933-0638.

OCT. 4-6. Annual State Blues Anti-Fraud Conference in Pittsburgh, sponsored by Highmark Blue Cross & Blue Shield. No fee. Cheryl Blumenstine, Senate Plaza, 3N, Senate Ave., Camp Hill, Pa. 17011; 717-731-2027.

OCT. 10-12. Risk Management Forum in Chicago, sponsored by Liberty Mutual. No fee. Tina Ziegler, Liberty Mutual, 175 Berkeley St., Boston, Mass. 02117; 617-574-5727.

OCT. 12-16. Self-Insurance Institute of America Inc.'s National Educational Conference & Expo in Washington, sponsored by SIIA; \$795 for members and

\$1195 for non-members. P.O. Box 15466, Santa Ana, Calif. 92735; 800-851-7789.

OCT. 13. Georgia Return to Work Issues in Workers Compensation seminar in Athens, Ga., sponsored by Lorman Education Services; \$189. Lorman Education Services, P.O. Box 509, Eau Claire, Wis. 54702-0509; 715-833-3959.

OCT. 14-15. Corporate Benefits Conference in Minneapolis, sponsored by the International Foundation of Employee Benefit Plans and the Council on Employee Benefits; \$540 for IFEBP/CEB members and \$640 for non-members. Colleen Radi, colleenr@ifebp.org; 414-786-6710, ext. 8219.

OCT. 14-15. Critical Illness Insurance Products and Services seminar in Las Vegas, sponsored by the Mass Marketing Insurance Institute; \$295 for members and \$390 for non-members. Mass Marketing Insurance Institute, 2841 Main, Kansas City, Mo. 64108; 816-221-7575.

OCT. 15-19. Pharmaceutical Care Management Assn. Annual Meeting and Conference in Tucson, Ariz., sponsored by PCMA; \$1,495 for members and \$2,500 for non-members. PCMA, 2300 Ninth St. S., Suite 210, Arlington, Va. 22204-2320; 703-920-8480.

OCT. 15-22. National Safety Council's Annual Congress and Expo in New Orleans, sponsored by the National Safety Council; \$555 for members and \$735 for non-members. National Safety Council, Registration and Housing Office, c/o IIS, 108 Wilnot Road, Suite 400, P.O. Box 825, Deerfield, Ill. 60015-0825; www.nsc.org.

OCT. 17-19. Chartered Property Casualty Underwriters Annual Meeting and Seminars in Boston, sponsored by the CPCU Society; \$425 for members and \$475 for non-members. CPCU Society, P.O. Box 3009, Malvern, Pa. 19355-0709; 800-932-2728, ext. 2769.

OCT. 17-20. National Managed Health Care Congress-Fall and NMH/IT in Los Angeles, sponsored by the National Managed Health Care Congress; \$1,695. NMHCC Inc., P.O. Box 102713, Atlanta, Ga. 30368-2713; 888-882-2500.

OCT. 18-19. Risk Management and Employee Benefits Conference and Exhibition in Chicago, sponsored by the Chicago and Wisconsin Chapters of the Risk & Insurance Management Society Inc.; \$275. REBEX '99, 60 Revere Drive, Suite 500, Northbrook, Ill. 60062; 847-480-9712.

OCT. 18-20. Business Insurance Seventh Annual Workers Compensation and Disability Management Conference in Marina del Rey, Calif., sponsored by Business Insurance in conjunction with International Business Forum; \$695 for risk managers, \$995 for all others. International Business Forum, 100 Merrick Road, Suite 500, West Building, Rockville Centre, N.Y. 11570; 516-594-3000.

OCT. 19-20. PricewaterhouseCoopers Annual Executive Conference for the Life Insurance Industry in New York, sponsored by PricewaterhouseCoopers; \$1295. 704-541-2800.

OCT. 20-22. Offshore Life and Annuities Forum in Nassau, Bahamas, sponsored by International Business Communications; \$1599. IBC USA Conferences Inc. 225 Turnpike Road, Southborough, Mass. 01772-1749; 508-481-6400.

OCT. 21-22. Florida Reinsurance Forum in Orlando, Fla., sponsored by Reinsurance Directions Inc.; \$795. Paul Walther, Reinsurance Directions Inc., 120 International Parkway, Suite 220, Heathrow, Fla. 32746; 407-333-1600.

OCT. 25-26. Medical Malpractice Liability Insurance Forum in Dallas, sponsored by the Institute for International Research; \$1,395. Institute for International Research-NY, Conference Administrator, P.O. Box 102914, Atlanta, Ga. 30368-2914; 888-670-8200.

OCT. 25-26. P&C Claims Congress in Chicago, sponsored by Global Business Research Ltd.; \$1,495. Conference Administrator, Global Business Research Ltd., 190 Stamford Ave., Stamford, Conn. 06902; 800-868-7188.

OCT. 26-27. Fort Lauderdale Mariners Club 11th Annual Marine Seminar in Fort Lauderdale, Fla., sponsored by the Fort Lauderdale Mariners Club; \$165 before Oct. 8 and \$200 after. Susan Moynihan, zue@gate.net; 954-522-7755.

OCT. 26-28. Natural Hazards Toolkit for the 21st Century conference in Memphis, Tenn., sponsored by the Institute for Business & Home Safety; \$100 for members and \$150 for non-members. IBHS, 175 Federal St., Suite 500, Boston, Mass. 02110; www.ibhs.org.

OCT. 27. Georgia Return to Work Issues in Workers Compensation Seminar in Athens, Ga., sponsored by Lorman Education Services; \$189. Lorman Education Services, P.O. Box 509, Eau Claire, Wis. 54702-0509; 715-833-3959.

OCT. 27-29. Annual National Disability Management Conference and Exhibit in Washington, sponsored by UNUM Life Insurance Company of America; \$1025 for members and \$1145 for non-members. Ann Makowski, Washington Business Group on Health, 777 N. Capitol St. N.E., Suite 800, Washington, D.C. 20002; 202-408-9320.

OCT. 28. Illinois CPA Society Insurance Conference in Chicago, sponsored by the Illinois CPA Society; \$259 for members and \$299 for non-members. Bridget Peterson, 222 S. Riverside Plaza, Chicago, Ill. 60606; 312-993-0393.

OCT. 29. California Self-Insurers Assn. Symposium in Commerce, Calif., sponsored by CSIA; \$99 for members and \$109 for non-members. CSIA, Joe Markey, 1010 11th St., Suite 250, Sacramento, Calif. 95814; 323-650-6089.

OCT. 29. New Reimbursement Rules and Employer Responsibilities Seminar in Chicago, sponsored by the American Academy of Physician Assistants; \$299 pre-registration and \$350 on-site. AAPA, www.aapa.org; 703-836-2272, ext. 3405.

OCT. 29-NOV. 3. Annual Employee Benefits Conference in Orlando, Fla., sponsored by the International Foundation of Employee Benefit Plans; \$750 for conference. IFEBP, 18700 W. Bluemound Road, P.O. Box 69, Brookfield, Wis. 53008-0069; 414-786-6700.

OCT. 30-31. Certificate of Achievement in Public Plan Policy in Orlando, Fla., sponsored by the International Foundation of Employee Benefit Plans; \$605 for IFEBP members and \$705 for non-members. Colleen Radi, colleenr@ifebp.org; 414-786-6710, ext. 8219.

OCT. 31-NOV. 3. National Assn. of Independent Insurers annual meeting in San Diego, sponsored by the NAI; \$400 for members and \$500 for non-members. NAI Annual Meeting c/o NAI, P.O. Box 78070, Milwaukee, Wis. 53278-0070; 847-550-9353.

NOVEMBER

NOV. 3. Return to Work Issues in Workers Compensation in Illinois Seminar in Rockford, Ill., sponsored by Lorman Education Services; \$179. Lorman Education Services, P.O. Box 509, Eau Claire, Wis. 54702-0509; 715-833-3959.

NOV. 4-5. Health Technology Assessment Information Service Conference in Philadelphia, sponsored by ECRI; \$295 for members and \$595 for non-members. Michele Patterson, ECRI, 5200 Butler Pike, Plymouth Meeting, Pa. 19462-1298; 610-825-6000, ext. 5519.

NOV. 4-5. Insurance Issues for the Year 2000 Seminar in Boston, sponsored by the Defense Research Institute's Insurance Law Committee; \$595 for members and \$645 for non-members. DRI, P.O. Box 72225, Chicago, Ill. 60678-2225; 312-795-1101.

NOV. 7-10. American Insurance Services Group INSTECH Conference in Orlando, Fla., sponsored by Insurance Services Office Inc.; \$595. www.iso.com; 212-898-6696.

NOV. 7-10. Society of Insurance Research's Annual Conference in St. Petersburg Beach, Fla., sponsored by Society of Insurance Research; \$525 for members and \$575 for non-members. Stan Hopp, 691 Crossfire Ridge, Marietta, Ga. 30064; 770-426-9270.

NOV. 8-10. Crisis Management Planning Course in Phoenix, sponsored by the Risk & Insurance Management Society Inc.; \$675 for members and \$825 for non-members. RIMS, Professional Development Department, 655 Third Ave., New York, N.Y. 10017-5367; 212-286-9292.

NOV. 8-10. Export Credit and Political Risk Convention in Washington, sponsored by IBC Global Conferences Ltd.; \$2,000. The Bookings Department, IBC UK Conferences Ltd., Gilmoora House, 57-61 Mortimer St., London W1N 8JX, England; 0171-453-5498.

NOV. 10-12. Professional Liability Underwriting Society annual conference in New York, sponsored by PLUS; \$720 for members and \$900 for non-members. PLUS office, 4248 Park Glen Road, Minneapolis, Minn. 55416; 800-845-0778.

NOV. 11-12. Life Insurance Product Development, Innovation and Distribution Summit in New Orleans, sponsored by the Strategic Research Institute; \$1,495. Strategic Research Institute, 333 Seventh Ave., Ninth Floor, New York, N.Y. 10001-5004; 800-599-4950.

NOV. 14-17. Ninth World Captive and Alternative Risk Financing Forum in Miami, sponsored by Business Insurance, Skandia/Sinser and Tillinghast-Towers Perrin; \$975 for risk managers, \$1,250 for all others. Tina Gassman, World Captive Forum, 4248 Park Glen Road, Minneapolis, Minn. 55416; 612-928-4659.

DECEMBER

DEC. 2. Litigating Insurance Claims Seminar in Washington, sponsored by McKenna & Cuneo L.L.P. No fee. Paul DeGeest, McKenna & Cuneo L.L.P., 1900 K St., N.W., Washington, D.C. 20006; 202-496-7500.

DEC. 4-8. National Assn. of Insurance Commissioners Winter National Convention in San Francisco, sponsored by NAIC; \$425 before Nov. 3, \$450 before Dec. 1. 816-842-3600.

DEC. 5-8. Fourth Annual Summit on International Managed Care Trends in Miami Beach, Fla., sponsored by the American Assn. of Health Plans; \$1,395. AAHP, Dept. No. 0612, Washington, D.C. 20073-0612; 877-291-2247.

DEC. 9-10. Financial Services Integration Symposium in Atlanta, sponsored by Georgia State University; \$450. Anne Shaw, Georgia State University, P.O. Box 4036, Atlanta, Ga. 30302-4036; 404-651-0931.

DEC. 9-10. Insurance Coverage and Practices Seminar in New York, sponsored by the Defense Research Institute's Insurance Law Committee; \$595 for members and \$645 for non-members. DRI, P.O. Box 72225, Chicago, Ill. 60678-2225; 312-795-1101.

JANUARY 2000

JAN. 20-21. Atlanta Risk & Insurance Management Society Educational Conference in Atlanta, sponsored by Atlanta Chapter of RIMS; \$150 for members and \$175 for non-members. Donna Hobbs, Equifax Inc., 1600 Peachtree St., N.W., Atlanta, Ga. 30309; 404-888-5085.

MARCH

MARCH 7. California Long-Term Care Symposium in Pasadena, Calif., sponsored by the American Assn. for Long-Term Care; \$115. www.ltcsales.com/conference; 805-379-3910.

APRIL

APRIL 30-MAY 5. The Risk & Insurance Management Society Inc.'s Annual Conference & Exhibition in San Francisco, sponsored by RIMS; \$745 for members and \$1,045 for non-members. www.rims.org; 800-713-7467.

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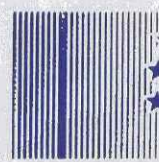


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Lutheran group sets up cash balance plan

By VINEETA ANAND
Crain News Service

ST. LOUIS—The Lutheran Church, Missouri Synod, isn't counting on God alone to take care of its workers.

The church, which is the second largest Lutheran organization in the United States, has used \$315 million in excess pension assets to set up a cash balance plan alongside its traditional pension plan.

The Supplemental Retirement Account is a plain-vanilla cash balance plan established as an add-on to the Concordia Plans and Pension Plan for Pastors and Teachers. The two plans have a combined \$2.6 billion in assets.

"To me the message is very clear. Before an employer considers converting from a (defined benefit plan) to a 403(b) or 401(k) plan, they should consider very hard a cash balance plan option," said Dan Leeman, executive director of the synod's Worker Benefit Plans section, which oversees the plans. "We looked at probably 15 different options to properly utilize the over-funded amount."

Towers Perrin, the church's actuary, was part of the team that came up with the idea of the cash balance plan, which was implemented in January.

"Wow! It's unusual," said Susan Breen-Held, consulting actuary at the Principal Financial Group in Des Moines, who works with church pension plans.

Because church retirement plans are not subject to funding limitations imposed under federal pension law, the church can continue contributing to its traditional plan while using the excess assets for the new plan.

Moreover, because churches are tax-exempt organizations, there is no question of deductibility on contributions to pension plans, Ms. Breen-Held said.

The church contributes 3.2% of pay for single workers and 4.5% of pay for married workers annually to the original plan.

The surplus assets are the result of

heavy exposure to the stock market—75% of the total allocation, with the remaining 25% in bonds—and the church increased its equity exposure to 80% at the beginning of the year, anticipating increased lia-

covered by the defined benefit plan also will accrue benefits under the new cash balance plan.

Although it is technically a defined benefit plan, and its assets are commingled with the traditional

September's five-year Treasury bill rate. The interest rate that applies this year is 4.62%.

When workers retire, they may choose to take their new account balances as a monthly pension check for life, or in a lump-sum payment. Workers also may opt to take a partial cash payment, with the remainder rolled over into an individual retirement account.

Workers who joined the organization this year received no opening balance in the cash balance plan. Existing employees received an opening account balance based on their salaries and tenure, based on average salaries from and going back to 1965.

Vineeta Anand is a reporter for *Pensions & Investments*, a sister publication of *Business Insurance*.

'Before an employer considers converting from a (defined benefit plan) to a 403(b) or 401(k) plan, they should consider very hard a cash balance plan option,' says Dan Leeman.

bilities from an aging workforce, Mr. Leeman said.

Under the new arrangement, the church's 28,000 pastors, teachers and full-time administrative staff

plan, the new plan provides workers with hypothetical individual accounts, to which the church credits 1.5% of pay annually, and an interest credit tied to the preceding

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Nominations for the 2000 *Business Insurance* Risk Manager of the Year and Risk Management Honor Roll are now being accepted.

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Loss ratio	65%	13.8%
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EXTREME
HEAT

Internet

Continued from page 1

While the former must learn to recognize and address risks as they move ahead with their business, the latter need to find new ways of looking at risk, brokers and insurers say.

The first group of companies is often created by "computer geniuses with good business sense who have a great idea and look for venture capital," said Emily Freeman, San Francisco-based national practice leader for Marsh USA Inc.

They are generally "consumed with business" and typically don't have a risk manager. The risk management function is often turned over to their accountants, lawyers or insurance brokers, as they focus on the "day-to-day struggle" for business survival.

Geoffrey Allen, New York-based managing director at Willis Media-TEC, a unit of Willis Corroon Group Ltd., said these individuals "are usually operating under a lot of time pressure and resource pressure, and the desire is to quickly as possible identify the issues and come up with a solution, so speed of delivery is an essential requirement."

"It poses a threat because of the pressure and the speed with which they have to operate, and the fact that oftentimes you're not dealing with individuals with a risk management background," though they are good at what they do, Mr. Allen said.

Sometimes these companies go into hypergrowth mode, "where everything is happening so fast, it's difficult to slow down, and sometimes, with risk, you need to slow down and evaluate what you have on the ground, and make sure what you're doing from a risk management perspective reduces your vulnerability to loss," said Ms. Freeman.

Meanwhile, "dot com" companies "typically have very little meaningful coverage" that deals directly with their liability exposures in cyberspace, said Ms. Freeman, whose firm's Net Secure program covers electronic commerce risks. "Many companies simply have office packages that protect them" so they can get required insurance certificates to show their landlords, she said.

Reliance National Insurance Co. in New York, which offers coverage to e-commerce companies, has seen these companies' general lack of risk management practices. Greg Gamble, vp-excess and surplus division at Reliance National, said, "As an underwriter, we've seen quite a few submissions for insurance where, when we ask them to provide details about how they're securing their electronic business environment, their answers fall short of what is necessary to buy insurance for it, which means they don't have the appropriate policy, techniques and procedures in place."

There is a need to develop new tools and address these virtual companies' needs using the techniques they are most familiar with, said Ms. Freeman.

The other type of e-commerce company, said Ms. Freeman, is the venture that starts out as a traditional business and has plants or stores but realizes "they need to reach out and embrace this technology to maintain their competitive edge." These companies typically have someone filling the risk management role.

The challenge for these companies may be to change the old ways of doing things. Traditional companies tend to see risks in terms of physical assets, things such as fire, windstorm and products that do not work, said Ms. Freeman. "They're having trouble shifting gears" and understanding "how much they need to be involved from the risk management end in dealing with these (e-commerce) risks head on," said Ms. Freeman.

While these companies have risk management resources, "oftentimes

the movement onto the Web is a quick reaction to market forces" that suddenly create new demands on the risk manager, said Mr. Allen.

It could involve dealing with wholly different risks, such as the security of electronic transmissions, that "may be relatively new exposure areas to a risk management department which is quite expert in their traditional areas," he said.

But, Ms. Freeman said, "I think many of them are slowly coming around and understanding and wanting to know" how to deal with Internet-related risks. "I think there's considerably more awareness than there was a year ago."

Whether new or established, all Internet companies face a combination of new and unanticipated risks, as well as risks that may have a different emphasis from that for a wholly traditional brick-and-mortar company.

For instance, one new potential risk is related to "meta tags," said Laura

Johnson, product and account development manager at Media/Professional Insurance Agency Inc. in Kansas City, Mo.

"Meta tags" are words embedded in Internet programming language. Search engines use the tags as part of their confidential formulas for identifying site matches.

In an effort to be listed first by a search engine, a company could embed in its meta tag the name of a prestigious competitor, improving its own chances of being called up first. But this creates a trademark issue, because that company is using the trademark to the potential detriment of the company that holds it.

Another issue that has trademark and copyright implications is related to framing technology, when a computer user is on a site that draws in other Web sites into its frame. These are among the new risks insurers are now grappling with, said Ms. Johnson.

As Internet companies develop new ways of doing things, "they can cause other exposures that were unanticipated," said Ms. Johnson, whose firm's CyberLiability Plus insurance policy covers cyber-related risks.

"The liability is evolving," said Mark Pruner, president of Rye, N.Y.-based Web Counsel Inc., a Web site-based marketing company. "New liabilities are being created as new businesses are being created, and new risks, and the question then becomes, does insurance written to cover traditional types of business modes cover these new risks?"

Business models are changing so fast, people "are not thinking, in many cases, about the liability, and even if they are thinking about the liability in the technology field, people don't think these risks are, or should be, covered by insurance," said Mr. Pruner.

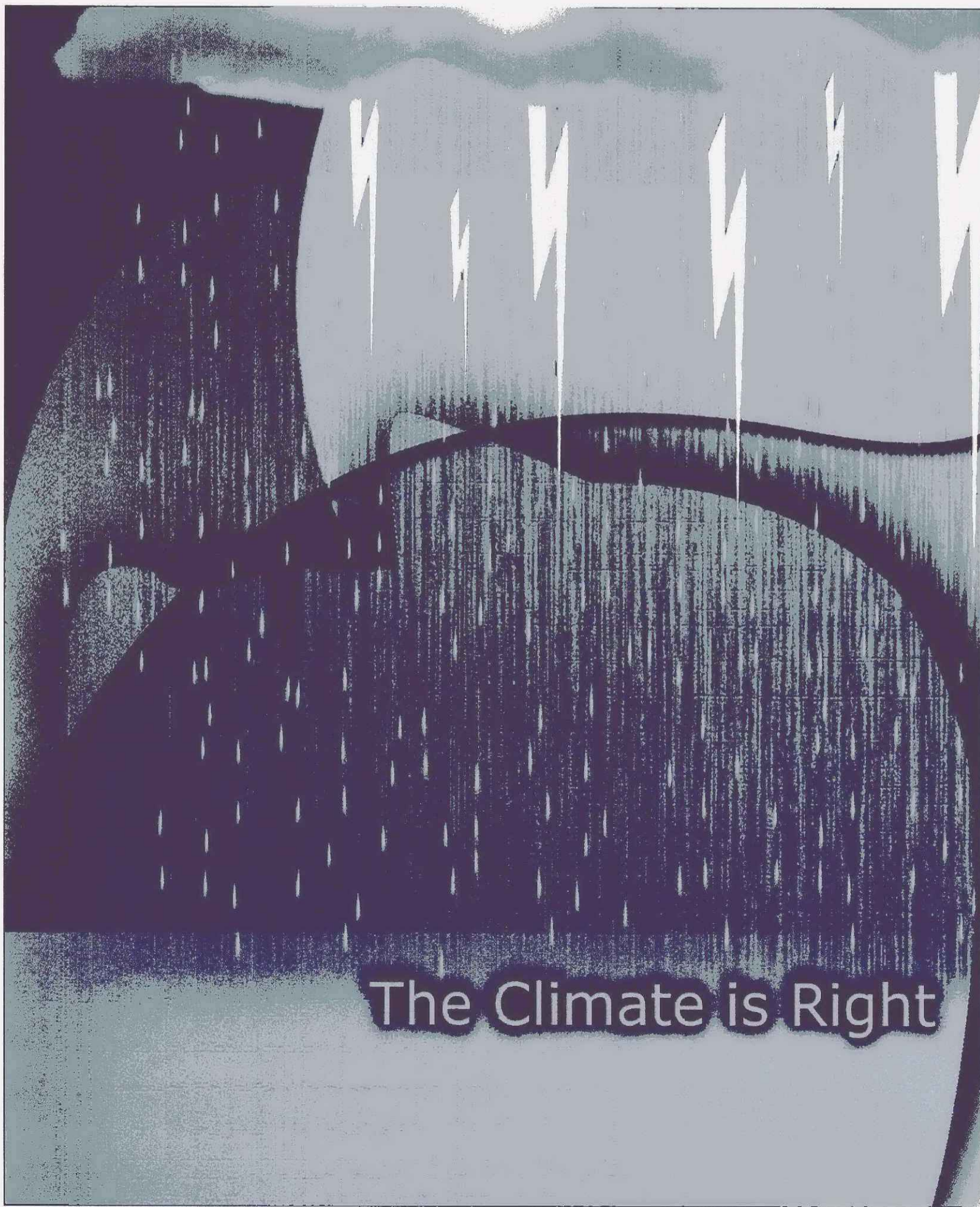
In many cases, long-recognized risks have a new emphasis.

The perils of e-commerce include risks faced by any company dealing with the Internet. These include computer viruses; theft and destruction of data; unauthorized use of data; defamation; intellectual property infringement; privacy and advertising liabilities; and repudiation, which deals with verifying the identity of the person doing the transaction, say observers.

But the traditional risks take on more critical importance when the entire, or a significant portion, of the business, is dependent on Internet use.

"Clearly, any business in 1999 has issues surrounding the integrity of their data, but if you're an online company, that is your life's blood, and the risk management efforts that you employ to protect the integrity of the information... are that much more central to your operation and your ability to maintain and to continue to grow," said Reliance's Mr.

Continued on next page



The Climate is Right

Continued from previous page

Gamble. If a programming error brings down a Web site, "the magnitude of that loss is far different for the virtual companies than companies that still do only a small percentage" of their sales on the Internet, said Ms. Freeman.

In addition to its impact both financially and on customer relationships, there are also potential legal liabilities if, for instance, a client cannot trade his stock over the Internet, said John Dorf, senior manager at Ernst & Young in New York.

Insuring e-commerce business is "probably closer to the publishing business than anything else, in that you're putting something out over the airwaves" in the same way a magazine or newspaper provides information, said Richard C. Reynell, senior vp at Becher + Carlson Risk Management Inc. in Atlanta.

"The only difference is there are

ways you can talk back to an Internet site...consequently, you've got a doorway open to your company you've got to protect," said Mr. Reynell.

"At the beginning of the Internet, people were basically throwing up their brochures," so there were concerns about content exposure, including libel, slander, defamation, invasion of privacy and standard media exposures, said Ms. Johnson.

But once people began providing services and transacting business, "it moved beyond the typical content exposure to E&O exposures and security exposures," said Ms. Johnson.

When insurers evaluate an e-commerce risk, "they need to look at what is the business model employed on the site, meaning is it just informational, telling you what my company does?"

"Do they conduct transactions? Is it interactive? Do they provide a service like Internet access? Do they accept

advertising banners from other companies? Who are they targeting? Is it business to business, or business to consumer?"

"Do they collect information about people who visit their site? If they collect information, if they're going to give that information to another party, do they ask the permission from the user first?" Ms. Johnson asked. For instance, is medical information given on an interactive physicians' site shared with others?

"You have to look at each e-commerce business and understand what their key risk issues are," said Willis' Mr. Allen. "You can't fall into the trap of thinking each e-commerce business is the same. They have a lot of similar ingredients, but the emphasis is going to change. You certainly don't want to emphasize the wrong or the less important part of their risk profile."

Some e-commerce companies, for instance, "may have more content

that they are offering as part of their business model, which gives them a larger media exposure."

"Some may have a business model which is dependent upon the security of the information and the privacy of the transaction which flows through the e-commerce business, and for those models, security becomes a paramount concern," Mr. Allen said.

Another issue is the speed at which these companies can change. Overnight, some Internet companies may metamorphose into other businesses with different and significant risk issues, said Mr. Allen.

A company may add, for instance, additional Web functions, such as a bulletin board or a chat room, or run an online sweepstakes to attract interest, he said.

One of the challenges also facing insurers is the lack of judicial precedent. "Normally, we tend to look at the historical litigation patterns to determine rates and coverage, and

that doesn't exist because the Internet and its adoption by business is still relatively in its infancy," and the issue of exposure is still emerging, said Ms. Johnson.

Ronald A. Johnson, a systems architect with Zurich Technical Risk Services in San Francisco, a unit of Zurich U.S., said, "In terms of the coverages developed, it's really a work in progress, because many of these companies are so unique, and the exposures are discovered almost daily."

"What the companies are trying to do is try to fit the old product around the new exposure," said Becher + Carlson's Mr. Reynell. "In that we have not seen any claims of any severity coming out of any of this yet, it's difficult to develop a product," he said. "We won't know what kinds of insurance is required until we witness more problems in the industry."

The situation is comparable to the one that had existed in the environmental arena, but only to a certain extent, said Web Counsel's Mr. Pruner. There, "you had a change in the business environment, but when the companies wrote the insurance, they certainly were aware that most companies had bad environmental practices at the time."

"Here, you've got a situation where companies are doing things that had never been done before, so it's not like an insurance company that ignored or really didn't think about the risk of how the waste was being disposed of. An Internet search engine is a business that, as a practical matter, didn't exist before the Internet came along," Mr. Pruner said.

Insurers are proceeding cautiously, said Reliance's Mr. Gamble. "Because this is new, insurance companies are being very careful to make sure they adequately understand the exposures and how the insured is addressing the exposures in terms of information security risk management."

Insurance is a "very reactive industry, and I think it's difficult for insurance companies to keep pace with the speed of Internet transaction technology" in general, said Eric Meyer, vp at Alexandria, Va.-based USI Southeast, a division of USI Insurance Services Corp.

"I would put, unfortunately, the insurance industry about two years behind any Internet development. It takes about two full years for the insurance industry to understand the technology, begin negotiations for exploring how to insure and actually being able to develop the products to insure it."

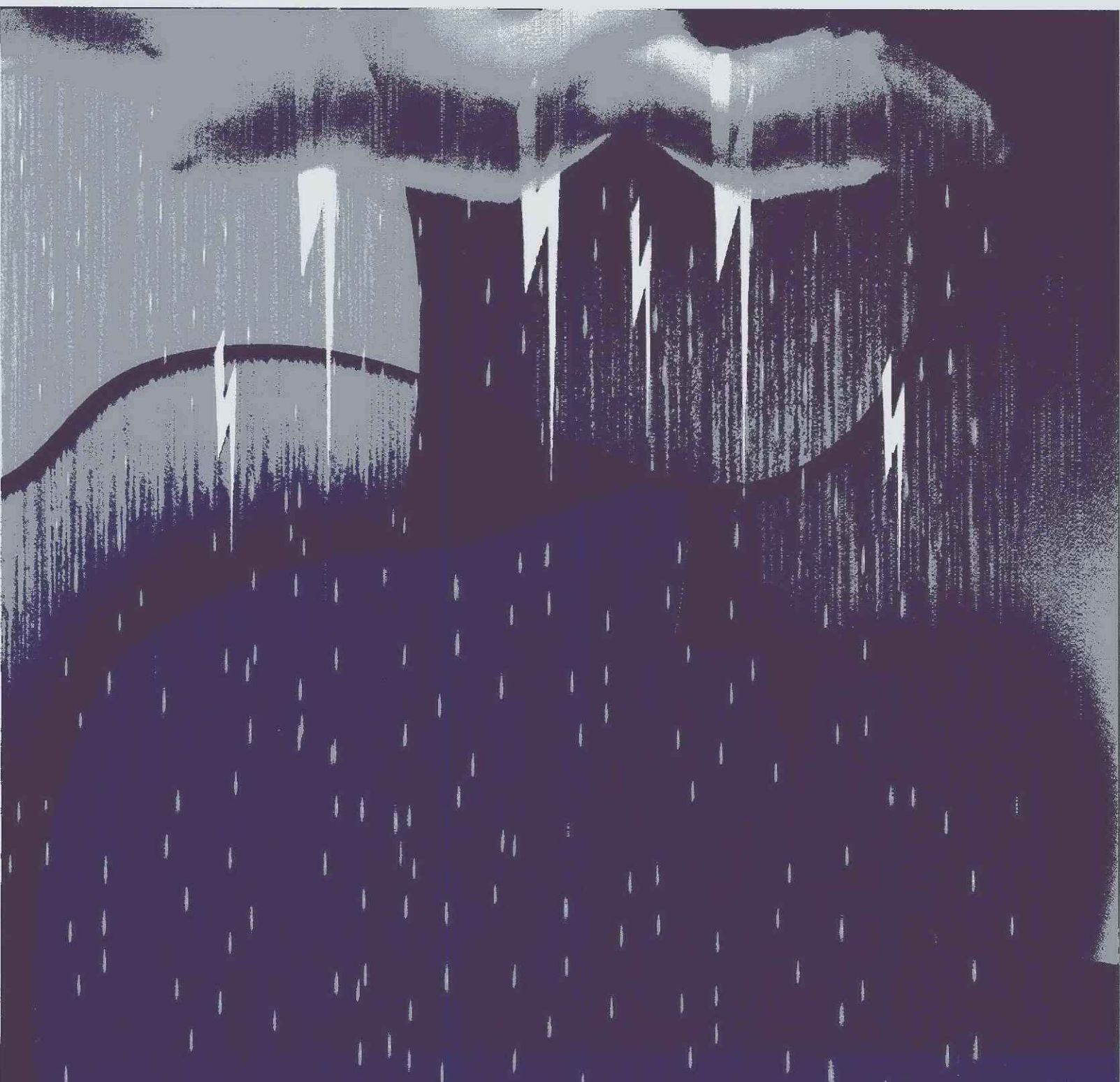
Mr. Meyer said he has always loved the phrase "the Internet minute." But the insurance industry works on an insurance year. "It is ponderously slow to evaluate new risks and to design methods for insuring them. There are some products out there," but they are designed for Internet developments that are three to five years old, he said.

According to Mr. Allen, however, that lag time is being reduced.

"It's been clear that the Web was going to be a force now for several years, and I think we're now just seeing in the past six months more thoughtful responses" by insurers, he said.

While insurance products do lag somewhat behind, "I think the insurers are seeing the importance of the Web and are working hard to respond to it. I don't think it's really different, if you will, than the way the (employment liability) or environmental market developed. It takes a while for the outlines of the exposure to clarify" and then for the responses to a changing set of risk requirements to develop.

But the products are still relatively nascent, he added, and "each product has to be looked at with extreme caution because of the complexity of the exposures."



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Large brokers eyeing independent agencies in Ohio

By **CHRISTOPHER SERRES**
Crain News Service

MAYFIELD HEIGHTS, Ohio—The telephone calls used to come three or four times a year. Then they started coming three times a month.

Now the phone is ringing so often that Ned Hyland, president of the commercial insurance agency Todd Associates Inc. of Mayfield Heights, is annoyed.

"I'm trying to kill these calls on the front end, but they're so persistent," Mr. Hyland said.

Like many independent insurance agencies in the Cleveland area, Todd Associates has become the unwitting acquisition target of firms many times its size. After going through years of mergers and internal management

changes, large national brokers—including Willis Corroon Corp. of Nashville, Tenn., Aon Risk Services Inc. of Chicago and Acordia Inc. of Indianapolis—are hunting for local acquisitions.

"Now that the megamergers are over, it makes sense that the next logical step is for larger firms like us to start consolidating those beneath us," said John Chaney, chief executive of Willis' Cleveland office. What remains to be seen is whether the big boys can find willing sellers.

Firms such as Todd Associates and Fedeli Group Inc. of Independence, Ohio, have voiced their opposition to joining larger firms. Their primary concern is that national agencies have gone through so many management changes that they haven't been able to de-

velop strong relationships with local clients.

"There is a perception that the national agencies have been so wrapped up in their own problems that they haven't been able to grow (locally)," said Larry Marsh, president and founder of Marsh, Berry & Co., an insurance advisory firm based in Concord, Ohio. "And after all, who wants to join a stagnant organization?"

Acordia is a prime example. The company had been scaling back its Cleveland operations ever since its previous owner, health insurer Anthem Group of Indianapolis, sold the company in September 1997 and effectively turned it into a private firm. Acordia has changed its president in Cleveland three times since 1996, and its payroll has shrunk to 60 from 75.

Keith Burkhardt, Acordia's latest top executive in Cleveland, acknowledged that the changes have been a distraction.

"When you're bought or sold, the first thing you start thinking about is, 'What's going to happen to my job?'" said Mr. Burkhardt, who took over as president and chief operating officer of Acordia's Cleveland office last November. "One of my goals was to get people thinking outwardly rather than inwardly."

Part of that process means looking for acquisitions. Last April, Mr. Burkhardt hired international accounting firm KPMG L.L.P. to begin searching Cleveland's commercial insurance market for acquisition opportunities. The ideal candidate would boast at least \$1 million in annual revenues, 25%

to 30% annual profit growth and a diverse book of business, said Randy Buhlig, who organized the search as senior manager of insurance advisory services at KPMG.

But finding companies that meet such criteria hasn't been easy. Mr. Buhlig said he had hoped at least one deal would be in the works by the end of the third quarter; now he doesn't expect a deal until the fourth quarter or early next year.

"We're finding that many of the most desirable firms simply don't want to sell," said Mr. Buhlig, who is calling on 70 local insurance agencies from a list given to him by Mr. Burkhardt.

The reluctance of local agencies to sell to their national competitors comes as no surprise to Mr. Hyland of Todd Associates.

There is still too much uncertainty about the ownership structure of the national agencies doing business in Cleveland, Mr. Hyland said. In addition to Acordia's sale, Willis was bought last year by private investment firm Kohlberg Kravis Roberts & Co. of New York.

"We don't want to join a company where we have to worry every day about whether we're going to be sold," he said.

At least one other firm, The Fedeli Group, already has accessed talent from the national agencies without selling. Fedeli's president and CEO, Umberto Fedeli, estimates he has hired eight to 10 insurance professionals from the Cleveland offices of national insurance agencies over the past five years. Those hires include Michael Cancelliere, who left his position as chief executive officer at Acordia in 1996 to run Fedeli Group's workers compensation practice.

"Why join them if we can hire them?" quipped Mr. Fedeli.

Such comments haven't deterred Michael LaRocca, president and CEO of Aon's Cleveland office, which employs 85.

Mr. LaRocca said he has begun to make personal calls to executives at independent brokers throughout Northeast Ohio. His hope is to acquire either a large agency or a smaller one with expertise in a certain industry, such as sports and entertainment.

"I wouldn't describe my search as intense, but I'm getting more encouragement from the head office (to make acquisitions) than I've ever gotten before," Mr. LaRocca said.

Mr. Chaney of Willis has more precise parameters. He said he ideally would like to acquire an agency with \$125,000 to \$150,000 in fee income per employee, and clients that averaged at least \$25 million in revenues per year.

"We're not looking for anyone with small accounts," he said.

But if a deal between a national giant and a local concern is in the making, then it hasn't crossed the desk of Mr. Marsh, whose firm often represents small to midsize insurance agencies in mergers and acquisitions.

"If one of the really large independents really wanted to sell—if they opened the door just a crack—then you can bet the (national) agencies would flood them" with offers, Mr. Marsh said. "Chances are, if a large deal hasn't happened by now, then it won't happen."

Chris Serres is a reporter for Crain's Cleveland Business, a sister publication of Business Insurance.

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Alabama's 11 HMOs post 1998 loss of nearly \$51 million

By MARK TAYLOR
Crain News Service

The general financial downturn affecting managed care organizations nationwide is giving Alabama HMOs a tough row to hoe.

All five of Alabama's provider-owned HMOs lost money last year, according to a company that tracks managed care plans in the Southeast. In fact, the other six HMOs operating in the state lost money, too.

The state's 11 HMOs lost about \$50.7 million on total 1998 premium revenues of \$785 million, according to Harkey & Associates, a Nashville, Tenn.-based information and health care publishing company that tracks HMOs in 13 Southeastern states.

Of the 11, the two health plans

that lost the most money were provider-owned.

PrimeHealth Cos. in Mobile, which operates a commercial and a Medicaid HMO with a combined

was founded by the three hospitals of the university, in Mobile.

Health Partners Southeast in Birmingham, a commercial and Medicare HMO with 106,000 en-

'We offered aggressive benefits with too many out-of-network possibilities, and we sold it too low. The moral of our story is bigger is not better and probably is worse,' says Brad Rollow.

rollment of 81,000, lost \$20.8 million last year on premium revenues of \$108.6 million, according to Harkey & Associates. The University of South Alabama Foundation operates PrimeHealth, which

rollees, lost \$20 million last year on premium revenues of \$109 million, according to Harkey & Associates. Baptist Health System in Birmingham operates Health Partners.

Harkey & Associates founder John Harkey Jr. said Alabama HMOs have performed so dismally because they've been caught in the general financial downturn affecting the managed care industry. That, coupled with the dominance of Blue Cross & Blue Shield of Alabama, a non-HMO, has made Alabama a tough place for HMOs to do business.

"Alabama is not a state with heavy managed care penetration," said Mr. Harkey. "Only 15% of the state's 1.8 million insured lives are covered by an HMO. The state's largest commercial HMO—United HealthCare of Alabama—covers only 125,000 lives."

Viva Health, with 41,000 enrollees, offers a Medicare risk and commercial HMO product. The University of Alabama-Birmingham owns the 4-year-old plan and also operates 851-bed University of Alabama Hospital.

The HMO has yet to make a profit. Last year, it lost \$5.6 million on 1998 revenues of \$34 million.

Brad Rollow, president and chief executive officer of Viva Health, said his firm is on the right path after several down years.

"We're doing better now," said Mr. Rollow. "We got ourselves in trouble because we grew too fast."

What hurt the HMO, he said, was a point-of-service product the health system launched in 1997 and has since stopped selling.

"We offered aggressive benefits with too many out-of-network possibilities, and we sold it too

low. The moral of our story is bigger is not better and probably is worse," he said.

Mr. Rollow, who is hoping to break even within six months, said Viva Health was placed on the state's critical list in January but was taken off in July.

The state Insurance Department places insurers on its critical list when they lose 50% of their reserves. The designation results in closer monitoring by state regulators.

Mr. Harkey said the state's provider-owned HMOs have usually been undercapitalized. He said most entered the market during an up cycle and were unprepared financially to face the downturn afflicting managed care for the past few years.

Alabama's other provider-owned HMOs are:

- CACH HMO, owned by 195-bed Children's Hospital of Alabama in Birmingham. The 38,000-enrollee plan lost \$52,000 on \$16.7 million in revenues last year.

- Health Advantage Plans, a joint venture between two Birmingham health systems, Tenet Healthcare Corp.-owned Brookwood Development Corp. and Eastern Health Systems' Eastside Ventures. The 13,000-enrollee plan lost \$1.4 million last year on 1998 revenues of \$3.7 million. Tenet is shutting the plan down next March.

Mark Taylor is a reporter at Modern Healthcare, a sister publication of Business Insurance.

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Oxford cancels plan for high-tech firms

By JUDITH MESSINA
Crain News Service

NEW YORK—Small high-tech companies in New York City are scrambling to find new health insurance after Oxford Health Plans Inc. canceled a policy with the Emerging Industries Alliance for non-payment of premiums.

The EIA, an umbrella organization for technology trade groups, has hired a new broker and administrator, but members haven't been able to get the low rates and broad coverage the original plan provided. At least one of EIA's member groups, the New York Software Industry Assn., has gone out on its own to look for coverage.

"There are not that many options," says Alice O'Rourke, executive director of the New York New Media Assn., another EIA member association.

The Emerging Industries Alliance was formed in 1997 to help raise the profile of small high-tech companies. One of its goals was to help small firms attract and retain employees by enabling them to offer affordable health insurance.

Two years ago, the association struck a deal with Benefit Concepts, a broker and plan administrator in Long Island. Benefit Concepts negotiated a contract with Oxford to provide group health insurance to employees of the companies in EIA's member groups.

The plan grew rapidly and soon covered more than 400 people. But Benefit Concepts was unable to keep accurate records, say EIA officials. Disagreements arose over policy cancellations, and members complained that it was difficult to

get information from the administrator.

Sources say the state Department of Insurance is investigating the plan's administrator; the department said it doesn't comment on pending investigations.

Benefit Concepts principal Perry Della Giustina says problems developed when Oxford transferred administration of the plan to an office in New Hampshire and continued charging for policies that had been canceled. In addition, he says, some members were not paying their premiums.

"EIA jumped in prematurely," adds Mr. Della Giustina. He says Benefit Concepts has opened its books to auditors hired by EIA.

EIA says it spent four months, from April to August, straightening out the records but, in the end, could not resolve a premium shortfall of about \$100,000. Oxford decided to terminate the plan as of Aug. 31.

While EIA has been able to help members move into other plans without a disruption in coverage, many are paying significantly more.

Brian Fisher, chief financial officer of new media start-up Templar Studios Inc., said that under the EIA group plan, his employees were paying \$215 a month for medical and dental coverage that allowed them to go to non-plan doctors for a reasonable fee. Now, they're paying \$268 and a much higher fee to use non-plan doctors.

Judith Messina is a reporter at Crain's New York Business, a sister publication of Business Insurance.

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Continued from page 3

not contain cost-saving reforms, according to his press aides.

That is good news, said Mr. Wilder, who lobbied other employers to oppose S.B. 320. Mr. Wilder also is chairman for the Sacramento, Calif.-based Californians For Compensation Reform.

Yet Mr. Wilder and insurers say the issue will come around again during the next legislative session.

In its current form, the bill proposes to increase most types of indemnity benefits. For example, maximum total temporary disability and partial temporary disability benefits would increase from \$490 weekly to \$546 in 2000 and to \$602 in 2001.

Even though the governor said he will veto the current bill, CCR still is encouraging employers to send letters to the governor supporting his posi-

tion. "We are getting our troops motivated to support his veto," said Lori Kammerer, CCR's managing director. The governor has until Oct. 10 to take action on the bill.

Members of the Alliance of American Insurers oppose S.B. 320 because

The issue of workers compensation benefit increases is expected to return in the next legislative session.

it falls far short of providing the full system reform necessary to offset increased benefit costs, said Peter M. Gorman, Alliance associate vp and regional manager in San Francisco.

For one thing, Mr. Gorman said, it would make California's workers

comp system even more complex by only partially repealing a legal presumption that a treating physician's injury diagnosis is always correct, Mr. Gorman said. Insurers and businesses seek a full repeal, he said.

Critics of the treating-physician presumption system want it changed so that benefits are granted based on objective medical criteria rather than on subjective doctor opinions.

In other action of interest to employers, California's legislators held over for next session a bill that would eliminate confidentiality agreements in the settlement of lawsuits involving environmental hazards, product defects or financial fraud (BI, Sept. 7).

In addition, legislators held over A.B. 1380, which would raise the state's \$250,000 cap on non-economic damages in medical malpractice cases. Also held over for next session is A.B. 858, which seeks to ban mandatory arbitration clauses in employment contracts. **BI**

Rollovers

Continued from page 3

not to do that, he said. "When someone does leave, it's important to make a concerted effort to remind people that this is retirement money. Also, some employers are directing employees to an IRA provider," Mr. McCarthy said.

Plan participants also need to be aware of the effects of the substantial tax hit if they choose to cash out, according to Mr. McCarthy. Workers who cash out face an automatic 20% withholding and additional income taxes on the funds, he noted.

He said the 20% withholding tax causes some confusion for employees.

"Unfortunately, sometimes it can be a detriment because people hear that 20% figure, and sometimes plan participants think that maybe that's a tax rate when really all it is, is a rate of withholding. They don't realize that it's going to count as regular income. There's also an additional 10% penalty tax, and then they are subject to state income tax as well."

Besides avoiding the withholding and taxes, workers who roll over relatively small savings into an IRA or new employer's plan can reap big rewards later.

"Even the small amounts do make a difference. Even that \$6,000 rollover that you have from an employer can

amount to a significant amount of money when it comes time for retirement," he said.

The survey showed that the number of employees rolling retirement savings into an IRA is up to 37% from 31% in 1993. Mr. McCarthy attributes that increase to a number of reasons.

"People are seeing a lot of advertising from mutual fund companies and brokerage houses that are really showing the perceived advantages that the IRAs have. It's also just another opportunity for IRA providers to get the word out that an IRA is a good place to save," he said.

Although the number of plan participants turning to IRAs has increased, the percentage of participants rolling over cash payouts into a qualified retirement plan has increased just 1%, to 6% in 1998 from 5% in 1993.

"The statistics show that IRA providers have done a good job, but you see the rollovers to new employers are pretty stagnant. Maybe that shows that people really aren't aware of all the benefits of their employer plan," Mr. McCarthy said.

The Hewitt 401(k) Distribution Rollover Analysis represents more than 193,000 defined contribution plan distributions nationwide in 1998.

The Hewitt survey is not available, but a summary can be viewed at www.hewitt.com.

Health costs hit hard

Trend is asking employees to pay more

By DAVID BARKHOLZ
Crain News Service

John Tovey is looking for answers to the mounting costs of employee health insurance.

Mr. Tovey is the director of human resources at Independent Engineering Laboratories Inc., a laboratory that tests fuel pumps in Ann Arbor, Mich. He said his company cannot afford another 15%-plus increase in premiums when its health insurance renewal comes due in April.

Consequently, Mr. Tovey has brought in an independent broker, Custom Benefits Insurance Group Inc. of Walled Lake, Mich. Mr. Tovey said he asked Custom Benefits to shop for a deal that will keep full coverage for IEL's 45 employees at savings over next year's anticipated rates.

"We're preparing now for next year," he said. "We have to."

Businesses everywhere are dealing with similar dilemmas. Although they are choking on new premium increases for health plans, they are concerned about changing plans or insurers because they either don't know where to turn for help or fear employee turnover if they alter plans too much.

The latter point is particularly troublesome because a tight local labor market makes retaining and recruiting qualified employees a priority for businesses, said Timothy Hite, a sales consultant for the Reaume Co., an employee benefits consulting company in Troy, Mich. "The (year) 2000 renewals are going to cause a lot of soul-searching," Mr. Hite said.

Experts in health insurance say the key to surviving the increases is to explore options beyond the type of plan traditionally made available to employees of large companies in the Detroit area, wherein employers pay for 100% of their workers' health care.

The trend in the industry is for employers to require employees to pay for part of their health insurance, Mr. Hite said. Other companies are increasing copayments and deductibles; some are even settling on base health plans and allowing employees to voluntarily "buy up," or pay for more-comprehensive coverage, he said.

"Until the past couple years, health

care was just an assumed benefit," Mr. Hite said. "But with rates increasing the way they have, the thinking has generally turned that the employees are going to have to pay for something."

For example, Blue Cross & Blue Shield of Michigan, the state's largest health plan, with 4.6 million members, has announced plans to raise rates for small businesses in the Detroit area by an average of 19.4% in the fourth quarter.

Mr. Hite has seen the dramatic impact on employers of the increases in the past two years, fueled largely by double-digit hikes in the cost and use of prescription drugs.

A typical preferred provider organization option in 1997 cost about \$230 per month for an unmarried employee and \$544 for family coverage, Mr. Hite said. Today, those costs are \$291 and \$689, respectively.

Mr. Hite said employees will accept more cost sharing if they are convinced that their employers' well-being is jeopardized by rising costs or that top-dollar health care coverage is costing them other benefits.

Employers should consider employee meetings, for example, to provide information about the importance of using generic drugs, as opposed to pricey, heavily advertised, brand-name drugs, said Richard Cole, Blue Cross senior vp-strategic planning and corporate communications.

A popular employer strategy to combat brand-name pharmaceutical use is to put in a higher copayment for brand-name prescriptions than for their generic equivalents, he said.

Mr. Tovey said he isn't sure yet how Independent Engineering Laboratories will fight rising premiums. Custom Benefits is going to look at every option, including possibly changing the company's insurer.

One way or another, though, employees must know the battle has been joined, Mr. Tovey said. "Unfortunately, many small businesses find themselves in the same spot that we're in," he said.

David Barkholz is a reporter for Crain's Detroit Business, a sister publication of Business Insurance.

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Oregon

Continued from page 2 representing Mr. Greenfield.

But RRG advocates disagree with that interpretation.

"The court order is broad enough to protect every RRG in that line of business," said Donald Breakstone, chairman of the government affairs committee of the National Risk Retention Assn. and senior vp and general counsel in Chicago for Vermont-domiciled Attorneys Liability Assurance Inc., a Risk Retention Group.

Other RRG supporters say Oregon regulators' refusal to apply the ruling to other RRGs in the same situation has no precedent.

"I have never seen a state so narrowly attempt to apply a court decision or order. Other groups could be forced to litigate—at great cost—an issue that is so clearly un-

der the umbrella of the court decision," said Jon Harkavy, an NRRA member and vp-general counsel in the Arlington, Va., office of Risk Services L.L.C., a consulting and captive management firm.

Others say Oregon regulators are, in fact, incorrectly reading Judge Stewart's decision.

"The judgment clearly applies to all RRGs as a category," said Phil Olsson, NRRA general counsel and a principal with Olsson Frank & Weeda P.C. in Washington.

The Oregon controversy involves the relationship between those sections of the Risk Retention Act that pre-empt state laws that discriminate against RRGs and other sections that protect from pre-emption state laws and rules that require employers in certain industries to demonstrate financial responsibility.

Under Oregon law, insurers must be authorized by the Depart-

ment of Consumer and Business Services to do business in the state. In addition, an insurer must be a member of the Oregon Insurance

automobile dealers must be registered with the state before they can sell vehicle service contracts. In order to meet the registration

'Singling out all RRGs for exclusion in favor of domestic insurers is not an objective or neutral standard, but, instead, constitutes discrimination as a class,' the judge wrote.

Guaranty Assn., which pays claims for policyholders if an insurer becomes insolvent. Under the Risk Retention Act, RRGs cannot be members of state guaranty associations and, as a result, cannot become authorized insurers in Oregon.

Under another Oregon statute,

requirements, the dealer must meet mandated "financial stability" requirements. A dealer can meet that requirement either by showing it has a net worth of at least \$100 million or by purchasing a reimbursement policy from an authorized insurer.

In 1996, the Oregon Department of Justice said RRGs could not offer reimbursement policies to dealers selling service contracts because the RRGs were not authorized insurers.

NWIC sued Mr. Greenfield, saying the Oregon requirements violated the Risk Retention Act, which allows RRGs to operate throughout the country after being licensed in one state. NWIC is licensed in 1984 in the Cayman Islands under a sunset provision in the original 1981 Risk Retention Act. Under the act, an RRG could be set up in the Cayman Islands or Bermuda and operate in the United States if it also meets the surplus and capital requirements of one domestic state. NWIC meets Pennsylvania's requirements. That provision has since expired, and RRGs now must be licensed in a domestic state, but those RRGs that took advantage of the earlier

provision can continue to operate.

Oregon regulators said the "financial responsibility" provision of the Risk Retention Act saved from federal pre-emption its statute requiring auto dealers to buy policies from authorized insurers. Under that provision, states are not pre-empted from specifying acceptable means of demonstrating financial responsibility.

But in her ruling, Judge Stewart noted that the Risk Retention Act exempts RRGs from any state law or order that discriminates against them.

"It is difficult to imagine how a law which categorically prohibits obligors of service contracts from purchasing their reimbursement insurance policies from RRGs can be characterized as a law which does not discriminate against RRGs," Judge Stewart said.

While the Risk Retention Act permits a state to specify a means to demonstrate financial responsibility, those means cannot discriminate against RRGs, she said.

For example, a state could require auto dealers to buy reimbursement policies from insurers with a certain amount of policyholder surplus. Or, it could require a dealer to purchase a certain level of coverage, Judge Stewart said.

However, "singling out all RRGs for exclusion in favor of domestic insurers is not an objective or neutral standard, but, instead, constitutes discrimination as a class," she said.

National Warranty Insurance Co., RRG (A Risk Retention Group) vs. Mike Greenfield, Director, Department of Consumer and Business Affairs of the State of Oregon, U.S. District Court for the District of Oregon, No. CV-97-1654-ST.

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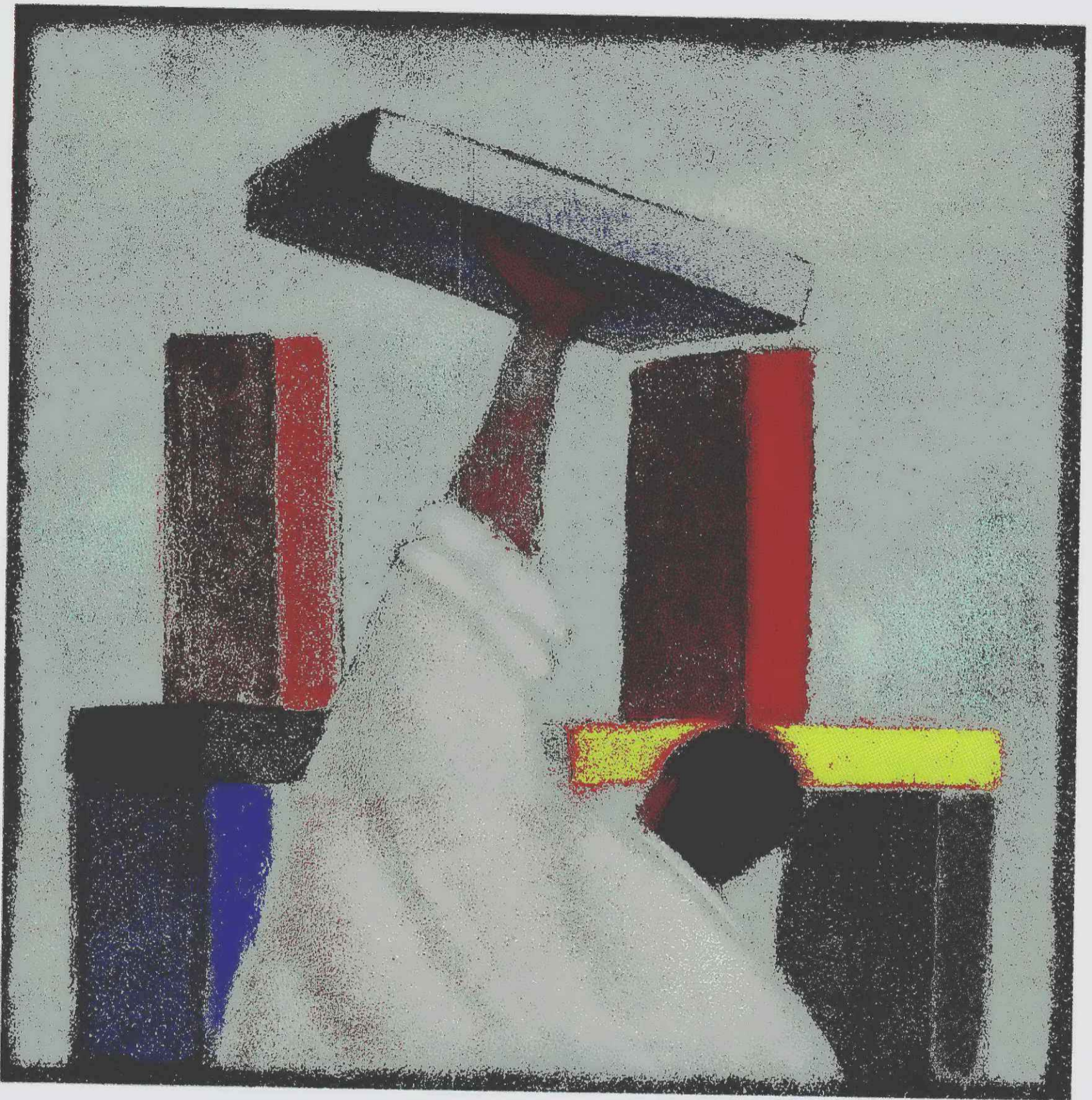
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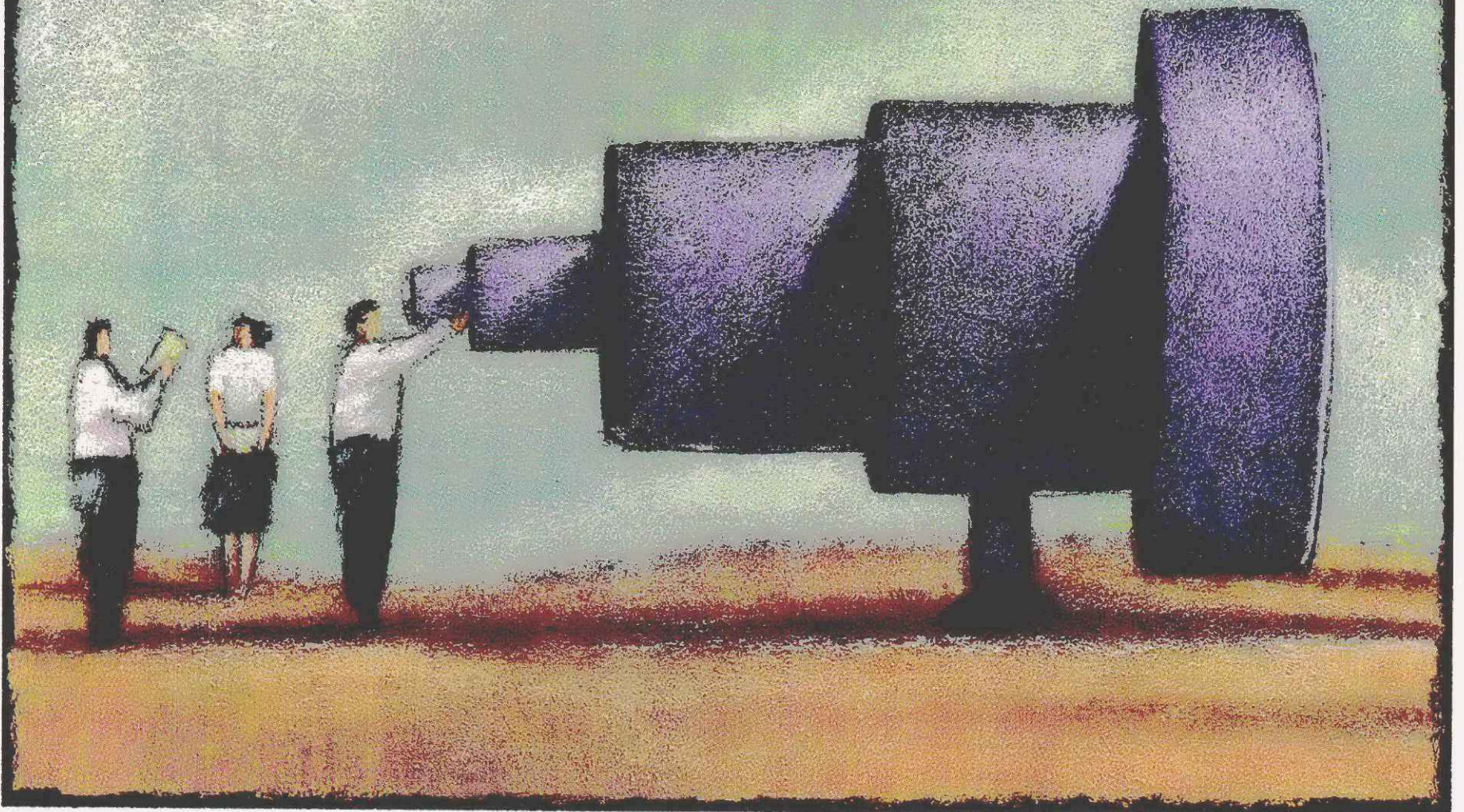
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RS: Reader Service, SS: Starch Study

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INTERNATIONAL

Global Briefs

Brazilian government-owned reinsurer **Instituto Resseguros Brasil** will be floated at \$520 million real (\$276.7 million) when it is privatized, rather than the \$460 million real (\$244.8 million) previously asked, according to a statement from the Brazilian government. The price increase is a result of debt reduction, said the government, but a few days later, all the IRB directors representing private insurance companies protested the move and resigned from the board. Local media sources report that the IRB privatization, originally scheduled for Oct. 14, has been postponed until next year. . . . U.K.-based loss adjuster **Crawford-THG** has opened a Tokyo liaison office for Japanese clients. The new office is headed by Richard Solomon, Crawford's regional managing director for Asia Pacific. . . . Citing concerns over the risk profile of the syndicate's business, Lloyd's of London's regulatory division confirmed it will require **Chartwell Managing Agents Ltd.**'s syndicate 270 to boost its capital backing by 10% for the 2000 year of account. Lloyd's regulators also have advised **Duncanson & Holt Syndicate Management Ltd.** that Lloyd's is considering a risk-based loading on syndicates 55, 957 and 1999. In addition, DP Mann Ltd. syndicate 435 has been given a 5% risk-based loading for the 2000 year of account. . . . Lloyd's syndicates 861 and 1209, managed by **Brockbank Syndicate Management Ltd.**, have ceased writing engineering business, including extended warranties. The agency earlier had forecast it would underwrite £17.5 million (\$28.3 million) in engineering business premiums next year. . . . **PXRE Managing Agency Ltd.** is taking over from **Amlin P.L.C.** the management of Lloyd's first captive syndicate. The transfer of **SmithKline Beecham's** syndicate is expected to be complete by the end of this year, though it is subject to Lloyd's approval. Most of the Amlin team responsible for bringing in SB's captive syndicate at the beginning of this year moved to **PXRE** several months ago. . . . Thomas Kraiser has been appointed a member of the Enlarged Group Executive Board at Zurich, Switzerland-based **Zurich Financial Services Group**. Mr. Kraiser, who is head of the Corporate Customer Division in the group's Zurich head office, previously was chief executive officer of **Enterprise Risk**, a Zurich U.S. unit. . . . Swedish insurer **Skandia Insurance Co. Ltd.** has purchased almost 10% of the shares in Norwegian insurer **Storebrand A/S**. Under Norwegian law, the maximum any one investor can hold in a Norwegian financial institution is 10% of the stock. **Skandia**, **Storebrand** and Finnish insurer **Pohjola Group** currently are merging their property/casualty operations; the merger recently received the green light from European Union officials. . . . European insurer alliance **Eureko** has bought a 25% stake in Cologne, Germany-based **Gothaer Credit Versicherung AG**. In addition, it has completed the formalities for its co-offer, with **BIG Bank GDANSKI**, for Polish insurer **PZU SA**. . . . George Nixon, a director of **Willis Corroon Group Ltd.**, has been appointed chairman-elect of the **British Insurance Brokers' Assn.** He will succeed **Simon Bolam**, the current BIBA chairman, next July.

Generali makes hostile bid for INA

INA's life business may attract other potential buyers

By SARAH GODDARD

MILAN, Italy—No sooner had Italian bank **Sanpaolo IMI** and insurer **Istituto Nazionale delle Assicurazioni S.p.A.** announced they were considering an alliance than Trieste-based insurance giant **Assicurazioni Generali S.p.A.** jumped in last week with an offer for **INA**.

The unsolicited offer for **INA** comes less than four months after **Antoine Bernheim** was ousted as **Generali's** chairman amid speculation that **Generali** was planning to slow down its acquisition activity (*BI*, May 24).

Mr. Bernheim was dismissed at

the end of April and replaced with **Alfonso Desiata**, the former chairman of Milan-based life insurer **Alleanza Assicurazioni S.p.A.**, a majority-owned subsidiary of **Generali**.

INA is the second-largest insurer in Italy after **Generali**, which, overall, is the third-largest insurer in Europe.

Generali's offer of 0.83 euros (86 cents) cash plus 0.07 ordinary **Generali** shares per **INA** share put an end to market speculation that Italy's largest insurer would not bid for **INA** because of a large overlap in business. But

even after the details of **Generali's** proposal were presented, analysts suggested that other suitors for **INA** are waiting in the wings.

The Italian life market, in which **INA** is a major player, with about a 12% market share, is particularly attractive because it is the fastest-growing in Europe. Premiums in

1998 rose about 40% from the previous year, totaling 51.5 trillion lira (\$314.5 million). In the same period, **Generali** posted gross premiums of 12.59 trillion lira (\$76.9 million), of which 5.96 trillion lira (\$36.4 million) came

from non-life business. There is considerable overlap between **INA** and **Alleanza's** life business in Italy.

"**INA** has a business which could potentially be very valuable," said **Nick Bunker**, director of insurance research at London-based **HSBC Securities**. "It has gone a long way already, but it still has got a long way to go," he said, referring to **INA's** reorganization since it was floated by the Italian government in 1994. "(The deal) will take a while, and it will be hotly contested. There could potentially be others interested," he said, possibly including **Allianz A.G. Holdings**, the German insurer that **Generali** found itself bidding against in

See **Generali** on next page



GIO directors face shareholder suit

Class alleges losses weren't disclosed; members say they'd have sold to AMP

By MATTHEW MACDERMOTT

SYDNEY, Australia—The directors of **GIO Australia Holdings Ltd.** and their financial advisers are facing a class-ac-



tion suit from shareholders angered by what they allege is the company's non-disclosure of large reinsurance losses.

Although **GIO's** directors and the company's advisers have liability coverage, none would name the insurers writing the risks.

GIO, a Sydney, Australia-based non-life insurer, announced in August that its reinsurance division, **GIO Re**, incurred losses of \$759 million Australian (\$498.5 million) for the 1998-99 fiscal year. The losses from **GIO Re**, which will now be sold or run off, were the major factor in **GIO's** overall 1998-99 loss of \$743 million Australian (\$488.0 million).

The class action stems not from the size of the losses but from the shareholders' claim that the impending losses were not foreshown in detailed documents released by **GIO** last year during its defense of a hostile takeover from Australian composite insurer **AMP Ltd.** of Sydney (*BI*, Aug. 31, 1998; Sept. 21, 1998). **AMP** ultimately achieved 57% control of **GIO** in January.

The class action, coordinated by Melbourne law firm **Maurice Blackburn Cashman** and supported by the Australian Shareholders' Assn., is being conducted on behalf of the 43% of **GIO** shareholders who, on the advice of the **GIO** board at the time, rejected the **AMP** offer.

The 43% of **GIO** shareholders who rejected the **AMP** takeover amount to 68,000 shareholders holding 200 million **GIO** shares.

Tony McLean, Australian Shareholders' Assn. executive officer in Sydney, said **GIO** shareholders who rejected **AMP's** offer are "aggrieved by the apparent lack of transparency" by the **GIO** board during the takeover.

See **GIO** on next page

Nissan Fire ordered to pay Weavers pool

By CAROLYN ALDRED

LONDON—A recent High Court ruling on the defunct **Weavers pool**, formerly one of the leading London underwriters of U.S. casualty risks, could speed up reinsurance collection by other insolvent pools, lawyers say.

Mr. Justice Moore-Bick ruled in *Kingscroft Insurance Co. Ltd. and 11 others vs. The Nissan Fire & Marine Insurance Co. Ltd.* that **Nissan** could not avoid paying reinsurance claims from the **Weavers pool** by arguing that it was unaware of the existence of certain participants in the pool and the existence of the pool's excess-of-loss reinsurance program.

The judgment means the administrators of the insolvent insurers that formed part of the **Weavers pool** will be entitled to collect "tens of millions of dollars" from **Nissan**, confirmed **George Clarke**, head of the legal department at **KWELM**.

KWELM is an acronym for **Kingscroft Insurance Co. Ltd.**, **Walbrook Insurance Co. Ltd.**, **El Paso Insurance Co. Ltd.**, **Lime Street Insurance Co. Ltd.** and

Mutual Reinsurance Co., former **Weavers pool** members that were placed into a joint scheme of arrangement in 1993.

It also should allow **KWELM** to pursue collection from at least a dozen other reinsurers that were using similar arguments to avoid paying claims, said **Chris Hughes**, scheme administrator for **KWELM** and senior insolvency partner at **PricewaterhouseCoopers** in London.

Since **KWELM** was put into a scheme of arrangement in 1993, its administrators have collected more than \$1 billion from about 220 reinsurers, according to Mr. Hughes.

According to the **KWELM** annual report to creditors published in August, liabilities and provisions at year-end 1998 totaled \$8.77 billion, while the companies' assets totaled \$2.87 billion, leaving a net deficiency of \$5.9 billion.

The judgment likely will affect settlements in other pool arrangements in the London market, lawyers agree.

The *Kingscroft* decision on the issue of who the **Weavers pool** was writing for "was eagerly

See **Weavers** on page 56

German brokers change with times

By DON LEWIS KIRK

FRANKFURT, Germany—As new legal concerns prompt German companies to pay greater heed to risk management, brokers are broadening their range of services to help clients adjust to the new climate.

George Nixon is a director of **Willis Corroon Group Ltd.** and a member of the supervisory board of Frankfurt-based broker **Jaspers Wuppesahl GmbH & Co. KG**. Speaking at a recent conference on trends and developments among brokers, Mr. Nixon told attendees that buyers' attitudes toward risk have shifted to the protection of assets for share-

holders.

Brokers need to help clients "put into place a risk manage-

Recent changes in corporate law have provided brokers with new consulting possibilities.

ment program, including insurance protection, that protects the whole global enterprise, so that the owner/shareholders' assets are not exposed," Mr. Nixon said.

For example, pollution is one risk a broker can point out to a client, said **Norbert Golumbeck**, risk manager for the **Bitburg**, Germany-based brewery **Bitburger Getraeke Verwaltungsgesellschaft GmbH**. "Our broker made us aware of potential pollution problems in the brewery process. We normally distribute waste on fields. Our broker made us aware of possible repercussion under Germany's new environmental liability law," Mr. Golumbeck said.

In fact, the new liabilities stemming from strict environmental laws are the area in which German brokers have been most active, Mr. Nixon said. "These

projects take many forms, but environmental concerns grow almost daily. And our experts can help clients cope with legislation and regulations and provide training to our clients' staff," he said.

Also, recent legal changes in Germany have opened up new consulting possibilities. In April 1997, the federal Supreme Court ruled that corporate supervisory boards must monitor management for errors and omissions. In a historic ruling, the court decided that supervisory boards can no longer treat illegal acts committed by management as internal corporate matters.

See **Germany** on page 56

INTERNATIONAL

Generali

Continued from previous page
last year's fight for French insurer Assurances Generales de France.

After a protracted battle for control of AGF, Generali and Allianz eventually reached an agreement in January last year giving Allianz ownership of AGF. Generali instead walked off with 80% of the shares in German insurer Aachenener & Munchener Beteiligungs A.G. and in three French AGF subsidiaries, GPA-Vie, GPA-LARD and Proxima.

Since then, Generali has set up a cooperation deal with German bank Commerzbank A.G. to distribute AMB products through its branch network in a bancassur-

ance arrangement.

Following the announcement of the Generali bid, rating agency Moody's Investors Service Ltd. in London reiterated an earlier statement that Generali "faces a challenge in making acquisitions... while maintaining a conservative financial structure."

INA's fragmented shareholder base—the Italian Treasury is its largest investor, holding 9.91% of shares, while Sanpaolo IMI controls 5.75%—has led to speculation over the summer that it could be a target for a takeover, particularly since acquisition activity was sparked in Italy by Olivetti S.p.A.'s takeover of Telecom Italia S.p.A. earlier in the year.

Analysts contend that the Sanpaolo talks ironically were de-

signed to stop Generali from making a hostile bid, and INA's chairman has stated the Generali bid does not fit INA management's plans to create a bancassurance group. INA's board officially rejected Generali's bid last week.

If the bid is successful, Generali expects the deal to be finalized by the end of this year. The offer, which effectively values each INA share at 3.04 euros (\$3.15), represents a 17.7% premium on the INA share price on Sept. 13, the day before the bid was launched, and a 28.4% premium on INA's average share price over the previous six months.

In a statement, Generali said the combined outfit would have premium income of 80 trillion lira (\$483.4 million) for 1999, and that

costs could be reduced by forming industry-specific groups and eliminating duplication.

Rating agency Standard & Poor's Corp. in London affirmed its AA rating for INA after the Sanpaolo talks were disclosed.

Meanwhile, a week earlier, an executive from Generali dismissed rumors that AXA Group of France was in talks to acquire the Italian company.

Such a deal would be "very, very unlikely," said Benito Pagnanelli, deputy general manager of Assicurazioni Generali S.p.A. of Trieste, Italy. "We're not looking to be bought," he said.

In Italian, the word for "rumor" means "noise," so speculation of AXA buying Generali "is just noise," Mr. Pagnanelli said. **BI**

GIO

Continued from previous page

"If they (GIO shareholders) had been given an accurate picture of the difficulties being experienced by GIO's reinsurance division, very few of them would have heeded the board's advice to reject AMP's offer," he said.

So far, more than 4,500 GIO shareholders have contacted Maurice Blackburn Cashman about joining the action; that figure is expected to rise due to the ASA publicly urging GIO shareholders to participate. It is the first time the ASA has recommended shareholders join a class action.

Mr. McLean said it is difficult to predict the total number of GIO shareholders who will join the action, and the total claim amount will depend on the number of shareholders and the value of their shareholdings in GIO.

If all 68,000 GIO shareholders who rejected AMP's offer join the action, the total claim amount is expected to be about \$500 million Australian (\$328.4 million). The shareholders who rejected AMP's offer are mainly small, individual investors.

Mr. McLean said the class action represents the best opportunity for GIO shareholders to recover their

losses.

GIO shareholders who rejected the AMP offer of \$5.35 Australian (\$3.51) a share have since seen the value of their shares drop to \$2.50 Australian (\$1.64) per share. At the release of its huge reinsurance losses GIO also announced that shareholders would not receive a dividend for the 1998-99 fiscal year.

The class-action lawsuit is the best opportunity for GIO shareholders to recover their losses, says Tony McLean.

Mr. McLean said the action aims to "uncover exactly what the GIO directors knew about the reinsurance division's likely losses" at the time they urged shareholders not to sell.

The central piece of evidence in the action will be GIO's Part B documents, lodged in response to the AMP takeover.

In the Part B, prepared by GIO directors in conjunction with external financial advisers Grant Samuel & Associates Pty. Ltd. of Sydney, GIO forecast a \$250 mil-

lion Australian (\$164.2 million) profit for the 1998-99 fiscal year, including a \$69 million Australian (\$45.3 million) profit for GIO Re.

The profit forecasts were made despite GIO recording an overall loss of \$26.6 million Australian (\$17.5 million), and a reinsurance loss of \$189 million Australian (\$124.1 million), for the 1997-98 fiscal year.

The class action against GIO directors and Grant Samuel will seek damages for misleading and deceptive conduct under Australia's Trade Practices Act. Formal class proceedings have been lodged with the Australian Federal Court, but no hearing dates have yet been set.

A spokesperson for GIO said the insurer had not received formal notification of the action. She said while the action is relevant to GIO, the company is not a defendant; only the directors at the time of the takeover and Grant Samuel have been targeted for damages.

None of the GIO directors during last year's AMP takeover still is on the GIO board.

The GIO board at the time of the takeover was Chief Executive Nick Steffey, now chief executive of Reinsurance Australia Corp. Ltd.; Chairman David Mortimer; and Directors Ronald Ashton, Andrew Kaldor, Lloyd Lange, David

O'Halloran, Ian Pollard, Marina Darling, and Bruce Hogan. Ms. Darling and Mr. Hogan resigned from the board in the first week of September; the vacancies have not yet been filled. The other board members were replaced with AMP directors when AMP took control of GIO in January.

The GIO spokesperson said the GIO board has D&O insurance, but it is not written by GIO or AMP. She would not name the board's insurers.

A spokesperson for Grant Samuel said the financial advisory firm will defend the class action. He said the company holds professional indemnity insurance, but he would not reveal details.

Meanwhile, GIO is facing potential fines from Australia's corporate watchdog, the Australian Securities & Investments Commission, over the reporting of its reinsurance losses.

In a statement, ASIC said it is investigating GIO's statements during the AMP takeover, GIO's financial position and accounts at the time, and whether the decisions made by GIO were "reasonable in the circumstances."

ASIC said its inquiry will "not be a simple or quick matter" as the issues surrounding GIO's reporting "are complex, and there is a great deal of material to consider." **BI**

Maritime unit goes to Lloyd's

By SARAH GODDARD

LONDON—Fallout from the merger earlier this year of the Institute of London Underwriters and the London International Insurance & Reinsurance Market Assn. to form the International Underwriting Assn. appears to be benefiting Lloyd's of London.

Last week, for example, CNA Maritime Insurance Co. Ltd. moved its London company market business from its underwriting rooms in the ILU building, which it had vacated in June, to a "box" at Lloyd's—a group of desks on the open plan trading floor where underwriters sit.

The move follows a decision early this year by U.K. multiline insurer CGU P.L.C. to move its marine underwriting operations into Lloyd's. Unlike CGU, however, CNA Maritime will not be transferring the business into a Lloyd's syndicate.

Starting last week, CNA Maritime began conducting its business from a box on the third gallery of Lloyd's headquarters on Lime Street in London. For four hours a day, hull, cargo and excess-of-loss business is being conducted from the box, though brokers still can visit the CNA Maritime underwriting team at the company's main underwriting office around the corner from Lloyd's.

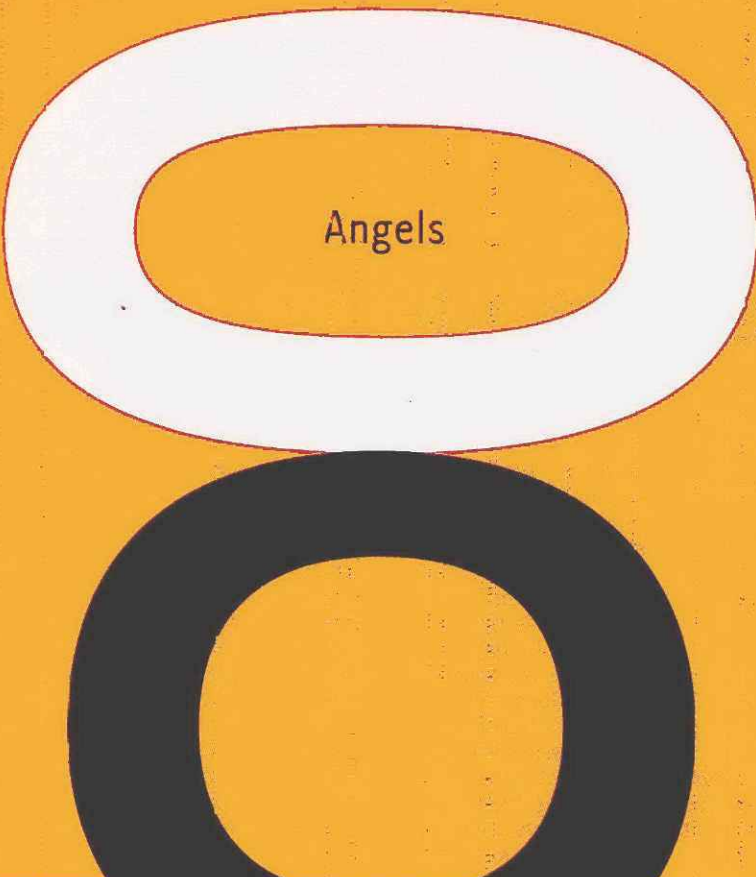
"Although we shall remain a member of the International Underwriting Assn. of London, basing some of our underwriters at Lloyd's has been planned for some time following our decision to vacate our underwriting rooms in the ILU building at the end of June," CNA Maritime Managing Director Nigel Jenkins said in a statement.

Traditionally, the ILU has been the heart of the insurance company marine market business in London.

Mr. Jenkins continued, "In line with the decisions made by a number of other companies, we see the Lloyd's building developing into an increasingly strong focal point for marine insurance in the London market."

CNA Maritime's box is adjacent to that of CNA Insurance Co. (Europe) Ltd., which set up business in Lloyd's in July. That, said Mr. Jenkins, will allow CNA to cross-sell marine and non-marine products and develop joint products between the two operations.

CNA also has a Lloyd's-based underwriting operation, CNA Underwriting Agencies Ltd. During the summer, active underwriter Richard McCarthy and deputy underwriter Paul Witzgenfeld resigned from the company's syndicate 1229. They were replaced by Ken Noden and David Ridpath as acting underwriters.



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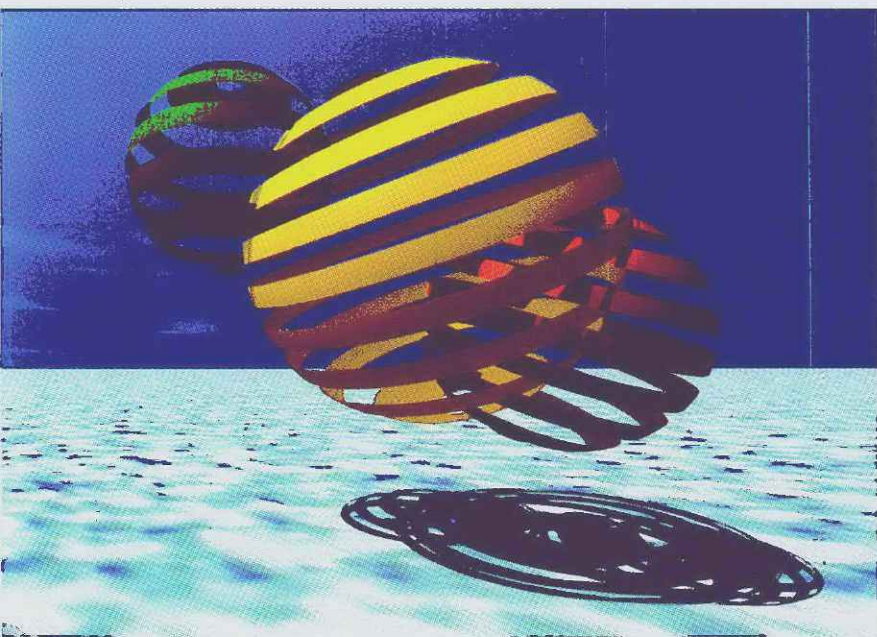
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■ **Captives 101: The Benchmark Course**

- Nicholas Dove, President, Skandia International Risk Management
- D. Hugh Rosenbaum, Principal, Tillinghast-Towers Perrin

OR ■ **Basics of Employee Benefits for Captives Owners**

- John Woyke, Esq., Principal, Towers Perrin
- P. Bruce Wright, Esq., Partner, LeBoeuf, Lamb, Green & MacRae

Keynote Address: David Wasserman, President, Centre Solutions

■ **Group Captives**

- George Chaffee, President, Skandia International Risk Management Ltd. (VT),
- Michael Ducey, Assistant Vice President and Managing Director, Bermuda Operations, Liberty Mutual Insurance Group
- Robert S. Wilkinson, Executive Vice President for Plan Operations, Health Services Medical Corporation, A Univera Company
- Moderator: Gaelen W. Cole, Marketing Director, Fireman's Fund Insurance Company

OR ■ **The Capital Market Landscape**

- Joe Kavanagh, Vice President, Marsh & McLennan Securities Corporation
- Additional panelists to be announced
- Moderator: Thomas Wronski, Director, Insurance & Risk Management, Fidelity Investments

■ **New Ways to Better Use Your Captive**

- James D. Cameron, Esq., Partner, Baker & McKenzie
- Mitchell J. Cole, Principal, Towers Perrin
- Moderator: Michael Maglaras, Principal, Michael Maglaras & Co.

OR ■ **Capital Markets vs. Reinsurance**

- John Berger, CEO, Chubb Re
- John Kiernan, Senior Vice President, Lehman Re
- Moderator: D. Hugh Rosenbaum, Principal, Tillinghast-Towers Perrin

Reception at the Spa Terrace

Tuesday, November 16, 1999

■ **Rent-a-Captives and Segregated Cell Facilities**

- Philip J. Harvey, President, Philip J. Harvey & Company, Inc.
- Philip J. Stevens, ARM, Vice President, Aon Group Inc., Alternative Markets Organization
- William Watson, Executive Vice President, Reliance National
- Moderator: Nicholas Dove, President, Skandia International Risk Management

OR ■ **Improving Financial Performance**

- Patrick C. Jensen, FCAS, Senior Manager, Deloitte & Touche LLP
- Jan Lommele, Principal, Deloitte & Touche LLP
- John M. Lummis, Senior Vice President and Chief Financial Officer, RenaissanceRe Holdings Ltd.
- Moderator: Mitchell J. Cole, Principal, Towers Perrin

■ **New Reinsurance Products for Captives**

- R. Lincoln Trimble, Vice President, Chubb Atlantic
- Michael Woodroffe, President, Meadowbrook International
- Moderator: Robert J. Rosser, Senior Vice President, Skandia International Risk Management

OR ■ **Expanding Captive Horizons to Employee Benefits**

- Nancy Bern, Senior Vice President, John Hancock
- Richard M. Inserra, Assistant Treasurer, Union Carbide Corporation
- Gary Matson, Director, Global Benefits, HJ Heinz
- Moderator: Mitchell J. Cole, Principal, Towers Perrin

■ **Shutdowns and Windups: Has Your Captive Run Its Course?**

- Sanford Bragman, Vice President Risk Management, Tenet HealthSystems
- James M. Dineen, Principal, The Knowledge Guild, Inc.
- Moderator: Robert J. Rosser, Senior Vice President, Skandia International Risk Management

OR ■ **Integrated Risk Financing/Enterprise Risk Management/Basket Aggregates**

- Michel Courrier, Director of Risk Management, Alcatel
- P. Richard Hackenburg, President & CEO, XL America, Inc.
- Brian Kawamoto, Director, Enterprise Risk, Swiss Re New Markets
- Moderator: Kathryn J. McIntyre, Publisher and Editorial Director, Business Insurance

■ **Using a Captive in Mergers and Acquisitions — A Healthcare Perspective**

- C. Richard Cornelius, Vice President Insurance Services, VHA Inc.
- Corbette Doyle, Chief Executive Officer of Healthcare, Aon Healthcare Alliance
- Moderator: Michael Maglaras, Principal, Michael Maglaras & Co.

OR ■ **Getting Ready for a Merger or Acquisition**

- Peter Gentile, CEO, Gerling Global
- Ken Krenicky, Vice President, Risk Management, Rhone-Poulenc Rorer Inc.
- Gary Peruse, Senior Vice President, Risk Management, Ogden Corporation
- Moderator: Kathryn J. McIntyre, Publisher and Editorial Director, Business Insurance

Reception, Dinner and Entertainment at the Pavilion

Wednesday, November 17, 1999

■ **Captive Case Studies Reception, Dinner and Entertainment at the Pavilion**

- Janet Evans, Corporate Risk Manager, Snow Summit Ski Corporation
- Barry Port, President, Public Utility Mutual Insurance Company
- Philip Thomas, Director of Risk Management, Bass
- Moderator: D. Hugh Rosenbaum, Principal, Tillinghast-Towers Perrin

Germany

Continued from page 53

And, in May 1998, German lawmakers passed the KonTraG laws, a series of amendments to national corporate law that call for managing boards to establish risk management plans as a part of corporate governance (BI, Sept. 6; March 29).

New legal concerns have proved a boon to brokers, said one broker executive.

"Demand for protection against manager liability grows as more plaintiffs in Germany are willing to sue," said Rolf Cyrus, director of Aon Jauch & Heubener's branch in Frankfurt.

The resulting boom in D&O insurance and KonTraG-related risk assessment has been a welcome development for German brokers. "Corporate governance is placing greater demands on boards of companies to fully understand and manage the risks faced by the business—not only the insurable risks but all the risks inherent in the business," Mr. Nixon said.

"Brokers, of course, are ideally situated to help with both," he said.

Brokers are seeking to help clients develop systems to monitor not only insurable risks but also business risks, to provide supervisory boards an "early warning" of potentially large exposures, said Christian

Dahms, chief executive officer of Germany's largest brokerage, Hamburg-based Aon Jauch & Heubener.

"The majority of corporate risks cannot be insured, and we are expanding expertise to help clients identify those risks," Mr. Dahms said. He was referring to balance-sheet risks that may be covered through alternative risk transfer,

'Our own analysis gives us knowledge of what we can insure and what we can't,' says one risk manager.

large deductibles or other means.

It's not yet clear whether clients will demand these services, but one risk manager suggests that companies themselves need to develop their own business risk solutions.

"If a company is not doing this already, it's not doing its job," said Lothar Riedle, risk manager of Vebe A.G., a giant German energy, chemicals, oil and logistics conglomerate. "Brokers would like the business, and they can contribute, but large companies, in particular, already have these controls in place."

Other German companies, such as Trienekens Entsorgung GmbH, a

Viersen-based recycling company, see cooperation with brokers on a limited scale.

"Our own analysis gives us knowledge of what we can insure and what we can't," said risk manager and captive director Hans-Josef Dohmen. "With that knowledge, we can better transfer risk." But Mr. Dohmen admitted, "Sometimes, the company is too close to the risk to really judge it properly."

To analyze risk, a new breed of broker is emerging, Willis' Mr. Nixon said. "We are getting involved in activities such as mergers, acquisitions and management buyouts, when it is most important to do due diligence in order to be clear on what you are buying or merging with. The risk management and insurance issues are part of this but are not always properly addressed."

As an example, Mr. Nixon cited Willis' assistance in a recent major merger, though he declined to name the companies involved. The broker, he said, was able to identify a potentially deal-breaking risk.

"We were also able to provide a solution to enable the deal to go forward, and the chief executive of that business confirmed that, without our work, the deal could not have gone through," Mr. Nixon said.

Although brokers are striving to differentiate themselves through services, price continues to drive the market, said Ralf Geck von Kaenel,

director of retail business at Aon Jauch & Heubener.

Germany's insurance market has been very soft for four years, considerably diminishing brokerage commissions. Despite an increase in quality and variety of service, German brokers agree Germany's ultra-soft market makes it difficult to convince clients they should pay more for broker services, Mr. Geck said.

"Nothing beats cheap insurance, and we find clients hesitate paying additional service costs and the soft market is supporting that trend," he said.

As a result, German brokers are intensifying efforts to shift to more fee-

based compensation from clients, rather than commissions paid by insurers. "When it comes to remuneration, the insurance broker is in a strange position that becomes ever stranger in this changing role," Mr. Nixon said. "We are acting for the client but have typically been remunerated by the insurer to whom we introduce the business."

Increasingly, however, brokers are succeeding in getting fees from clients for more complex services, Mr. Nixon said. "Brokers do add real value to clients, and they should be paid by the client for the job that they do. Our role has been undervalued." **BI**

Weavers

Continued from page 53

awaited, since it arises in relation to a number of pools that operated in the 1970s and 1980s," noted Nigel Brook, a partner at London-based law firm Clyde & Co. "The judge's conclusion on this issue in particular is phrased in terms that are applicable to pools generally and does not turn on the specific knowledge of Nissan," Mr. Brook said.

The judgment is "very significant and could have an impact on other pools," agreed Mark Everiss, a partner at London law firm D.J. Freeman.

"This judgment represents a further landmark in the Weavers saga," wrote Nick Bradley, a partner at law firm Lawrence Graham in London. Mr. Bradley noted that Nissan is "one of a long line of reinsurers who have crawled over Weavers' records, and many will have monitored closely their challenge to the structure of the Weavers' pool and the manner in which Weavers was administered."

In a commentary sent to clients, Mr. Bradley wrote that the decision addresses several issues relating to pools, including the retention obligation of pool underwriters, the manner in which pools operate and the status of underwriting companies that are not "stamp companies."

The ruling also provides a "significant guide to the manner in which the commercial court will apply rules of (contract) construction," according to Mr. Bradley.

Holman Fenwick & Willan, Nissan's law firm, said Nissan will appeal.

Mr. Justice Moore-Bick gave Nissan leave to appeal on all issues on the grounds that "the case raises questions of interest and importance to the insurance market and some questions of principle in the law of contract generally," according to a statement from Holman Fenwick & Willan.

H.S. Weavers (Underwriting) Agencies Ltd. acted as an underwriting agent in London from 1963 to 1990, establishing itself as one of the leading London underwriters of U.S. property and liability risks by writing for a pool of insurance companies. From 1963 to 1974, Weavers maintained separate underwriting agency agreements with each of the pool companies, known as "stamp companies" because their names appeared on the underwriting stamp used to accept incoming business, according to the judgment.

From 1971 on, several companies joined the pool as reinsurers of the stamp companies, with Weavers accepting, on behalf of the reinsuring member, a proportion of each risk written by a stamp company.

"However, for practical purposes the reinsuring members were treated in the same way as other members of the pool," the judge noted. Premium collection and claims accounting for the reinsurers was handled as if they were stamp companies in the pool.

The U.K. Insurance Companies Act 1974 led to a restructuring of the Weaver pool because some participants based overseas were not authorized to do insurance business in the United Kingdom but wanted to continue their participation in the pool.

"The solution to the problem which Weavers adopted was to stop accepting business for those companies under their existing agency agreements and to arrange for each of them, and new members in a like position, to enter into a whole account quota-share reinsurance treaty with one or more of the stamp companies," the judge explained.

"Weavers' need for additional capacity to enable it to develop its business, together with the enthusiasm of insurance companies to obtain a share in what was increasingly seen as an attractive underwriting account, enabled the pool to grow by the recruitment of additional members. Inevitably, therefore, its composition changed from time to time as new companies became members and... existing members left," noted the judge. Change of this kind "was a characteristic which the Weavers pool shared with other similar underwriting pools, many of which were active during this period, both in the London market and elsewhere," he added.

In 1975, Nissan agreed to participate in two facility quota-share treaties under which it would provide proportional reinsurance to companies for which Weavers underwrote.

Nissan claimed it was entitled to avoid claims under both treaties on the grounds of misrepresentation and non-disclosure concerning the involvement of the whole account quota-share participants and the existence of the pool's excess-of-loss program. Nissan also claimed that the stamp companies and whole account quota-share cedents repudiated both treaties by failing to comply with a contractual obligation to retain 50% of the risks ceded.

In addition, Nissan contended that six of the 11 claimants, none of which was a member of the Weavers pool in January 1976, never were parties to the original treaties.

The judge also concluded that it would be standard market practice for a pool writing umbrella liability insurance to have an excess-of-loss reinsurance program and that the retention obligation should be applied to the pool as a whole without excluding non-proportional reinsurance.

On the issue of new members to the pool, the judge concluded that "the parties to the agreement intended that, if there were changes in the composition of the pool during the currency of the (facility quota-share) treaties, the new members should become reinsureds as soon as Weavers began to underwrite on their behalf. Any other conclusion would significantly undermine the commercial purpose of the treaties, which depended for their efficacy on treating the Weavers pool, for these purposes, as a single commercial entity." **BI**

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Moderator: Donna Galer, executive vice president, Zurich-American Insurance Group.

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United

Continued from page 3

and benefits are contained in the U.S. collective bargaining agreement."

United flight attendants, at the time of the recent tribunal, could fly up through their 27th week of pregnancy if they had obtained a doctor's permission. Now, Mr. Colosi said, this has been increased to 31 weeks by United and discussions with pilot and flight attendant unions.

In addition, Mr. Colosi said many U.S. collective bargaining agreements have scope clauses, which limit work alternatives that a pregnant flight attendant may perform. He noted the scope clause, which was last modified in 1972, mandates that flight attendants must perform tasks directly related to the flight attendant position.

For example, one such related position might be working at a flight attendant training center. Mr. Colosi said. To qualify for such alternative assignment at United, an attendant

must first volunteer for the assignment and meet established criteria dictated by the nature of the job.

Another option for some United flight attendants not able to fly for the full number of weeks of their pregnancy is to transfer to a vacant position such as a customer service or ticket agent position, he said. Flight attendants are selected and trained for such positions.

As part of the agreement, United flight attendants voluntarily may use accrued paid sick time off during the last nine weeks of their pregnancy, not exceeding 1,000 hours.

Many flight attendants go on a seven-week unpaid medical leave and collect unemployment before giving birth. This arrangement, said Mr. Colosi, enables the flight attendant to keep insurance, medical and travel benefits as well as being guaranteed a return to her job and retention of seniority.

United flight attendants also are able to take a 90-day leave after delivery, which may be extended an additional 90 days as personal or medical leave.

Joanna Broadbent, an assistant in the employment department of law firm Lovell White Durrant in London, said employees domiciled at London's Heathrow Airport would be entitled to the various maternity laws that apply to people ordinarily employed in the United Kingdom.

These protections go well beyond the scope of maternity benefits, encompassing unfair dismissal and discrimination laws, said Ellen Temperton, partner in the employment department at law firm Baker & McKenzie in London.

Current U.K. law permits 14 weeks of maternity leave, of which six weeks are paid at 90% of normal pay. The remaining leave is paid at a flat rate of about £60 (\$97) per week. Total leave will increase to 18 weeks on Dec. 15, said Ms. Broadbent. The United Kingdom also provides for a 13-week unpaid parental leave that may be taken by either the mother or the father.

Ms. Broadbent said the Employment Relations Act of 1999 will relax factors that determine whether an individual is considered "ordinarily

employed" in the United Kingdom. This change likely will become effective in October.

"A contract may say you're based somewhere else, but if in practice you work out of London, in the future, you'll be covered by the statutory protection," said Ms. Broadbent.

Sam Whitaker, an employment law attorney for London-based law firm Freshfields, sees parallels with the latest United Airlines tribunal and another tribunal involving Saudi Arabian Airlines within the past year.

"Clearly, foreign corporations will no longer be able to assume that their U.K. employees will not have U.K. employment rights merely because they work for or are paid by a non-U.K.-based corporation," said Mr. Whitaker.

In addition, the benefits afforded by U.K. law "are replicated across Europe in similar forms," Baker & McKenzie's Ms. Temperton said.

This may increase an employer's difficulty in providing equitable benefits to workers with like job descriptions who work in different

countries, she said.

"The introduction of the euro will facilitate comparisons by employees employed in one country by a multinational with employees based in another country," Ms. Temperton said. These comparisons will not just be monetary, but also could examine benefits packages.

"I still think it's possible for that company to say distinctions should be drawn because social, economic and legal requirements vary considerably from country to country."

Elliot Goldman, an equity partner at Wildman, Harrold, Allen & Dixon in Chicago, said this decision seems "consistent with an underlying difference in work culture between Europe and the U.S. and, for that matter, other parts of the world."

"Some people look at (the U.S.) system and say it's too demanding of people and not deferential enough to workers' needs," he said.

But, he said, there are differences in the economies, productivity levels and unemployment rates of the United States and other countries, too. **BI**

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REQUEST FOR PROPOSALS

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Sub-total30,866
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Educational Institutions972

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Former Winston Hill chief convicted

HOUSTON—The former owner of a fraudulent Bahamas insurance company has been convicted on charges of swindling U.S. policyholders of tens of millions of dollars by writing an array of worthless policies.

A federal jury earlier this month convicted George L.J. Wilson, former owner and president of Winston Hill Assurance Co. Ltd., on multiple conspiracy, mail fraud and money laundering charges.

Mr. Wilson, who has also been a prominent Bahamas political figure, faces maximum sentences ranging from five years to 20 years for each of the 18 counts on which he was found guilty. Mr. Wilson was released on bond while awaiting sentencing, which is scheduled for Dec. 20.

Prosecutors charged that Mr. Wilson and Norwood Rolle, a Bahamas lawyer and accountant, conspired to create phony financial statements showing millions of dollars of non-existent assets in order to attract business to Winston Hill. The "assets" included \$63.4 million supposedly on deposit with Gulf Union Bank in Nassau, Bahamas, at year-end 1989, when, in fact, Winston Hill's account at the bank contained only \$11,000 at that time (BI, Jan. 18).

Operating through an underwriting office in Houston, Winston Hill took in more than \$50 million in premiums between 1989 and 1992, including \$34 million written in California alone. Its business ranged from auto liability to health coverage for multiple employer welfare arrangements. Winston Hill declared bankruptcy in 1992 and has left about \$15 million in unpaid claims, prosecutors say.

Mr. Wilson was arrested last year when he arrived at Miami International Airport on a business trip. Mr. Rolle, who acted as Winston Hill's accountant, still is wanted on fraud charges and remains in the Bahamas, where he is working for the Elliott B. Lockhart Law Firm, according to a report in The Nassau Guardian newspaper.

Mr. Wilson's lawyers have filed motions for a new trial and a post-verdict judgment of acquittal. If these fail, Mr. Wilson will appeal the conviction, said Jim Lavine of Zimmerman & Lavine in Houston.

"We believe the evidence was wholly insufficient to sustain a verdict of guilty," Mr. Lavine said. "We were quite surprised at the verdict."

Mr. Rolle could not be reached.

Court rejects arguments on reinsurance

LITTLE ROCK, Ark.—A federal appeals court ruling that failed to address the restrictions an insurer faced while trying to recover damages for its reinsurer could lead to higher insurance costs, an industry association maintains.

Last month's ruling by the 8th U.S. Circuit Court of Appeals came in a legal malpractice lawsuit that New York-based Reliance National Indemnity Co. filed against attorney Alston Jen-

nings Jr. and his firm, Wright, Lindsey & Jennings L.L.P. of Little Rock, Ark. Reliance had used the Jennings firm to represent a trucking company policyholder, Eastern Express, in a wrongful death case.

According to court papers, the driver of a passenger vehicle was killed in a 1991 accident with an Eastern truck, but witnesses told police the trucker was not at fault. A police report attributed at least partial blame to a third driver but none to the trucker. The dead driver's family still sued Eastern but indicated it would settle for \$50,000. Mr. Jennings was uninterested in the offer, and Reliance did not offer to settle, court papers said.

During a 1994 jury trial, the investigating officer faulted the trucker, and Mr. Jennings was unable to produce the eye-witnesses. A jury awarded the family \$2.5 million, but Reliance and the family later settled for \$1.5 million. Reliance ceded all but \$262,500, or 17.5%, of the loss to reinsurers.

In its legal malpractice lawsuit, Reliance sought to recover the entire \$1.5 million of damages. It argued it should not be limited to seeking recovery for only its 17.5% retention, because Reliance's reinsurance contracts required it to pay the reinsurers the bulk of any legal malpractice recovery. A federal district court rejected Reliance's argument. A federal jury later found Reliance was 97% at fault for the underlying damage award.

In affirming the lower court's decision, a three-judge panel of the 8th Circuit on Aug. 10 ruled that Reliance's objection to the amount of damages it was limited to seeking was moot.

"This was a disappointing ruling because it threatens the fundamental nature of the reinsurance agreement that requires insurers to attempt to recover on reinsurance paid," said Mike Koziol, senior director and counsel for the National Assn. of Independent Insurers of Des Plaines, Ill. "This may increase the sums reinsurers pay out under their agreements," which could boost insurance costs "for the public at large."

Program emphasized early intervention

HARTFORD, Conn.—Aetna U.S. Healthcare has combined the features of its managed health care plans with those of its managed disability plan to create a program called HealthWorks.



According to a release from Hartford, Conn.-based Aetna U.S. Healthcare, HealthWorks is a new benefits program designed to improve employee health and productivity while reducing absenteeism due to illnesses or disabling events. It was created, the release says, to better manage high-cost chronic conditions—such as asthma, diabetes, heart disease and lower-back pain—that can seriously harm an employee's health and productivity and increase benefit costs.

Return-to-work planning is begun before disabling injuries occur, when members are in disease management programs or they are pre-certified for the treatment of existing medical conditions. The early-warning system, the company says, enables disability nurse case managers to educate at-risk members and

to provide disease management intervention when a disabling event is imminent.

The company release says that once a disability occurs, a clinical team coordinates case management. This team includes trained disability nurses, vocational rehabilitation specialists and on-staff medical directors. Nurses educate employees in managing their conditions at home and at work, and they collaborate with the employee's physician and employer to assess opportunities for transitional work duties.

HealthWorks is now available to employers in the Northeast and the Mid-Atlantic states that use Aetna U.S. Healthcare's HMO and managed disability products. The program is scheduled to be available nationally in 2000.

For information, contact Richard Babcock, product manager at Aetna U.S. Healthcare, 860-273-3439 or babcock@aetna.com.

Comings & Goings: Industry

New York-based American International Underwriters, the international property/casualty unit of American International Group Inc., has named **Joseph Smetana** chairman of AIU's commercial lines division. He previously was vp-foreign general insurance for AIG. . . **Urs Nussbaum** has been named head of the Global & National Unit at Swiss Reinsurance America Corp. in Armonk, N.Y. . . ESG Re Ltd. of Hamilton, Bermuda, has named **Steven Debrovner** chief executive of ESG's reinsurance operations; he previously was chief underwriting and marketing officer. Also at ESG, Chairman **John C. Head III** has been named chief executive officer. Mr. Head, who will remain chairman of ESG, replaces outgoing CEO **Wolfgang Wand**, who has resigned. ESG also has named **Edward A. Tilly** deputy chairman.

Information in brief

Marsh & McLennan Securities Corp. completed a \$50 million insurance-linked swap transaction last week for an unnamed insurer. The swap, conducted between multiple investors and the insurer, involved earthquake risks in the New Madrid region. The New Madrid Seismic Zone spans seven central U.S. states. Although it functions much like a catastrophe bond, a swap is less expensive and less time-consuming, said Sean F. Mooney, senior vp of Guy Carpenter & Co. Inc., a reinsurance arm of Marsh & McLennan Cos. . . **Frontier Insurance Group Inc.**, based in Rock Hill, N.Y., has opened a Midwest regional office of the United Capitol Insurance Co. in Chicago. . . Fort Wayne, Ind.-based **Lincoln Financial Group's** reinsurance unit signed an agreement last week to buy Alden Risk Management Services, an employer medical stop-loss provider. ARMS is owned by Miami-based John Alden Life Insurance Co., a subsidiary of Fortis Inc. The \$41.5 million cash deal, which also includes some group life and accidental death and dismemberment business, is expected to close before year end. . . **Pinnacol Assurance** is the new name adopted last week by the former Colorado Compensation Insurance Authority, a competitive state fund. Service enhancements include online capabilities for policyholders and brokers to report injuries and monitor claims. The quasi-public insurer, which is the state's insurer of last resort, currently writes workers comp coverage for about 49,000 employers, which is nearly 38% of the market, according to the company. **BI**

Hurricane

Continued from page 1

Dallas-based restaurant chain had been monitoring Floyd's path for several days prior to landfall, and it is also watching Hurricane Gert, which was gathering strength in the Atlantic behind Floyd last week.

A few of the 50 Pizza Inn restaurants in Floyd's path through North and South Carolina experienced power outages, but no structural damage to Pizza Inns had been reported as of Thursday morning, Ms. Owen said.

All Pizza Inn stores are insured for any property damages, and the restaurants also have business interruption insurance, which Ms. Owen expects will kick in for the restaurants left without electricity.

State Farm Mutual Automobile Insurance Co.'s preliminary estimate of losses from Floyd in the area from Florida to Delaware included 26,000 homeowners claims worth about \$55 million and 5,000 automobile claims worth about \$12 million. The estimates do not include flood claims covered by the National Flood Insurance Program.

As of last Friday morning, Liberty Mutual Insurance Co. in Boston had received just over 1,000 initial reports of personal insurance claims due to Floyd, a spokeswoman said. The volume was increasing in the insurer's Southern and Mid-Atlantic regions. By this week, "we expect that number

may double or triple," the spokeswoman said, adding that the insurer did not have any estimates of its Floyd losses yet. She said the insurer had mobilized catastrophe claims teams in Florida and the Mid-Atlantic.

As a result of Hurricane Andrew, the Factory Mutual companies put teams of engineers in the field to help customers identify what could be done to keep their roofs intact in the face of the hurricane, said Mike Burke, vp and chief engineer of Factory Mutual Insurance Co. in Johnston, R.I. He said the engineers showed policyholders where to secure the coverings. "It's a tiny weak point" that can prove to be costly, he said.

Since Andrew, 80% of all the deficiencies that the engineers identified have been corrected, he said.

The payoff came during Hurricane Georges, which hit Puerto Rico in September 1998. Customers that followed the engineers' advice suffered losses that were only 20% to 25% of that suffered by "all industry that didn't follow our advice," Mr. Burke said.

As Floyd approached, the insurer sent out faxes to policyholders identifying specific emergency actions that needed to be undertaken. In addition, resident engineers either called or visited plants to make sure proper precautions were being taken. Factory Mutual also updated its World Wide Web site to show the hurricane's path and to identify necessary emergency actions.

"After Hurricane Andrew, we got very serious with all of our customers about addressing all of hurricanes' preventable loss. We wanted to get them to recognize that it wasn't bad luck, that there are engineering solutions," said Mr. Burke.

Bahamas hit first

While the U.S. coast was not hit as hard as feared, the Bahamas were the first to be struck by Floyd as it moved westward.

Due to communication and transportation difficulties in the Bahamas, though, complete damage estimates were not available as of late last week.

Robert Barnett, catastrophe coordinator for McLarens Toplis N.A. Inc. in Los Angeles, said the adjuster has "a lot of hotel-type accounts" in the Bahamas, but no claims had been reported by the end of last week. "We may yet get something down there," Mr. Barnett said.

Drew Maenza, director of marketing for Crawford & Co. in Atlanta, said 40 adjusters have been sent to the Bahamas to survey the damage and to adjust claims after Hurricane Floyd hit there early last week.

According to the adjusters, who took an aerial view of the damages last Thursday, the small island of Abaco and the islands surrounding it received the full force of the storm, which included 15-foot storm surges and wind gusts of 190 mph, Mr. Maenza said. Many homes, hotels, marinas and at least 25 ferryboats

were damaged, he said, but no damage estimates were available.

Mr. Maenza said that, according to a report from a Crawford adjuster in Freeport, Grand Bahama, "the storm was over the island for 15 hours, causing trees to uproot and sea walls to disintegrate, which caused flooding."

As of last Friday, Freeport Airport remained closed due to the flooding, Mr. Maenza noted.

New Providence also sustained a mixture of structural and flood-related damage, Mr. Maenza said. The resort of Paradise Island in Nassau, including the Atlantis Hotel, sustained flooding damage.

Sandals Resorts, which operates several Caribbean resorts, reimbursed 560 vacationing guests at the Sandals Royal Bahamian Resort & Spa in Nassau with complimentary replacement vacation packages. The hotelier uses a self-insured hurricane guarantee.

John Lynch, executive vp-sales for Unique Vacations, who represents Miami-based Sandals Resorts, said this is the second time the two-year old guarantee has been paid. "Once the resort gets hurricane-force winds, it trips (the guarantee)," he said.

The resort sustained some water damage in fewer than 20 of its 406 rooms, and a few trees were toppled, but Mr. Lynch said there was no structural damage.

Although the resort is remaining open, it is encouraging new vacationers not to arrive until next week, he said, and it is even chartering planes

to take current vacationers off the island.

Florida 'dodges a bullet'

After barreling through the Bahamas, Hurricane Floyd seemed poised to inflict tremendous damage on John F. Kennedy Space Center in Cape Canaveral, Fla. With the storm bearing down on the complex, four rockets were secured to towers on the launch pad, and space shuttles were placed in hangars able to withstand winds of 110 to 120 mph. The highest sustained wind at the Space Center was 91 mph, registered early Wednesday morning.

A statement on the Web site of the National Aeronautics and Space Administration called damage from the storm "institutional in nature," citing downed signs, felled trees, water intrusion from blowing rain and minor equipment damage.

The 34-mile-wide complex is situated on the tip of the Atlantic, just nine feet above sea level. Threats of hurricane-force winds and tidal surges are mitigated by shuttering and sandbagging, said a NASA spokesman based at the Kennedy Space Center.

"We get these scares a couple of times a year, and we secure the buildings and we live and hope," he said earlier last week, noting that if Floyd came ashore at high tide, the complex would have a flooding problem.

In some cases, Florida's pre-

See Hurricane on next page

Benefits

Continued from previous page
have exempted small employers from mental health care parity laws, California's current measure would not. Also, other states have included escape clauses exempting health plans from the mandate if parity results in cost increases above certain levels. The California measure lacks such a provision.

In addition, the list of mental disorders covered under the California bill is broader than those in bills approved in many other states.

Under the California measure, health plans could not impose higher cost-sharing requirements, such as deductibles and copayments, for the treatment of severe mental illnesses, including:

- Schizophrenia.
- Schizoaffective disorder.

- Major depressive disorder.
- Bipolar disorder.
- Panic disorder.
- Obsessive-compulsive disorder.
- Autism.
- Anorexia nervosa.
- Bulimia nervosa.

The list of mental disorders covered by the California bill is broader than those in bills approved in many other states.

In addition, equitable coverage would have to be provided for a child with a mental disorder—other than a primary substance abuse disorder—that results in behavior inappropriate to the child's age.

The bill also would prohibit

plans from imposing limits on the number of inpatient days or outpatient sessions for the treatment of mental disorders that are different from coverage for other physical conditions.

For larger employers using managed care plans, the cost impact of the mental health care mandate should be negligible, said Kathy Sternbach, a principal in the San Francisco office of William M. Mercer Inc.

That is because managed care helps ensure that the treatment provided is necessary and appropriate, Ms. Sternbach said.

In fact, the bill says health care plans can use managed care techniques, such as utilization review and case management, to control costs.

In addition, plans can require enrollees in specific geographic areas to obtain mental health care services from networks. **BI**

D&O

Continued from page 3

lated to Owens Corning's financial disclosures and alleged misrepresentation and that the asbestos exclusion did not apply, Mr. Smith said.

The case was then sent back to the trial court level, and in January Judge Katz ruled that Owens Corning is entitled to coverage. In March, he rejected another National Union argument on allocation of the loss: The insurer contended that at least part of the settlement should not be covered because one of the defendants in the shareholder suit was Owens Corning itself, which was not a named insured under the D&O policy.

Judge Katz ruled instead that the National Union must cover the whole settlement.

In a final order in the coverage case this month, the judge also awarded Owens Corning prejudg-

ment interest from the date of the 1995 settlement and attorneys' fees for both the underlying shareholder suit and the coverage litigation.

The judge rejected National Union's contention that he could not award court costs without a showing of malice or bad faith by the insurer.

While National Union also urged the court not to enter a final judgment without a hearing on the "reasonableness" of the shareholder settlement, Judge Katz dismissed this argument.

National Union "acknowledged that it received information from (Owens Corning) regarding the *Lavalle* suit in October 1991. (National Union) does not dispute that it received regular correspondence and notice from (Owens Corning) regarding settlement negotiations and ultimate resolution of the underlying litigation. The *Lavalle* trial court conducted a fairness hearing only after notice was provided to the parties and National Union was again

advised of those proceedings. (National Union) did not respond or object to the settlement," Judge Katz noted.

"This court will not further explore that issue as the parties had an opportunity to object, did not, and after a hearing the trial court approved the settlement," he concluded.

The \$12.8 million award to Owens Corning includes \$8.9 million in settlement and defense costs, including coverage of the \$10 million settlement and \$1.4 million in defense expenses less the company's \$2.5 million deductible. Also included are prejudgment interest of roughly \$3.5 million and \$467,519 in attorneys' fees attributable to the coverage case.

Owens Corning Fiberglas Corp. vs. National Union Fire Insurance Co. of Pittsburgh, Pa.; U.S. District Court for the Northern District of Ohio, Western Division; Case No. 3:95cv7700.

Colorado rules on allocation

DENVER—The Colorado Supreme Court has adopted a pro-rata method of allocating insurance coverage from multiple policies in an environmental action, making it harder for policyholders to obtain an "all sums" allocation.

Under pro rata allocation, all of the insurers on a risk must contribute proportionately to a claim. Under the all sums allocation, each insurer could be called on to pay all of a claim, explained Adam H. Fleischer, an attorney with Bates Meckler Bulgher & Tilson who represented Wallis & Cos., the London under-

writers involved in the case.

In its Sept. 13 ruling in *Public Service Co. vs. Wallis & Cos.*, Colorado's high court found that "in cases of continuous, progressive and indivisible environmental damage, where it would be unreasonable to expect juries to allocate actual damages to specific policy periods, we hold that liability must be allocated proportionately among insurance policies according both to time-on-the-risk and to the degree of risk assumed."

"We do not believe that these policy provisions can reasonably be

read to mean that one single-year policy out of dozens of triggered policies must indemnify the insured's liability for the total amount of pollution caused by events over a period of decades," the court said.

The case stemmed from a suit filed by PSC seeking coverage for the cleanup of two Denver-area sites: the Barter Yard and the Lowry Landfill. PSC sued all of the insurers that had issued liability insurance policies to it between 1966 and 1980. All of the insurers except Wallis settled with PSC before trial.

—By Joanne Wojcik Kochaniec

Airline insured for landing mishap

GERONA, Spain—The hard landing last week of a Britannia Airways Ltd. jet comes a couple months after the airline changed lead insurers for its liability and hull coverage and negotiated a premium reduction.

Some passengers were injured slightly, and the 757 jet's fuselage tore open in a couple areas during the incident.

At its July 1 renewal, Britannia switched to Lloyd's syn-



PHOTO: AFP

This Boeing 757 landed hard last week in Gerona, Spain, slightly injuring 55 people who were aboard.

dicare 270, managed by Chartwell Managing Agents Ltd., as its lead insurer. Gerard Knowles is the lead underwriter. Marsh Ltd. in London placed the coverage. Lloyd's syndicates managed by ACE Ltd. previously led the coverage, according to market sources.

The airline purchased liability limits "in line with normal industry practices," a source said. Airlines increasingly have been purchasing \$1.25 billion to \$1.5 billion of liability limits in recent years.

Britannia has one of the lowest loss ratios among commercial airlines, according to information *Business Insurance* obtained. It had an 11% five-year loss ratio as of July 1998.

The flight, carrying a vacation charter group of 236 from Cardiff, Wales, to Gerona, Spain, skidded off a runway into a field after landing during a heavy rainstorm last Tuesday. Of 55 passengers injured slightly, all but one had been released from the hospital by late last week, a Britannia spokeswoman said. She said the passenger who remained hospitalized had breathing difficulties before the landing.

The fuselage of the six-year-old Boeing 757 ripped open in a couple areas but overall remained intact, the spokeswoman said. She and market sources said they did not know whether the jet was repairable. **BI**

Updates

Aetna to sell some Texas units

RICHARDSON, Texas—Aetna U.S. Healthcare is selling its NYLCare Texas commercial operations to Blue Cross & Blue Shield of Texas for \$500 million in cash, the companies announced last week.

The transaction was required under terms of a settlement reached by Aetna with the U.S. Justice Department to permit its acquisition of Prudential HealthCare.

Included in the deal are NYLCare Health Plans of the Gulf Coast and NYLCare Health Plans of the Southwest. The plans collectively include 531,000 health maintenance organization/point-of-service plan members and 20,000 preferred provider organization members.

Aetna U.S. Healthcare will retain approximately 105,000 members of the NYLCare 65 Texas Medicare plan through a reinsurance and administrative services agreement.

If the transaction receives regulatory approval, as is required, it will close in the first quarter of 2000.

After the divestiture, Aetna U.S. Healthcare will be the second-largest managed care firm in Texas, with about 2.4 million members statewide, including 1.1 million HMO enrollees. BC/BS of Texas, which owns Blue Cross & Blue Shield of Illinois, will become the largest managed care plan in the state, with nearly 2.7 million members.

Comp data public, judge rules

PHOENIX—An Arizona judge ruled recently that the state's public record law requires the Arizona Industrial Commission to release its database of employer-specific workers compensation information to a company that sells such information.

The decision, which followed a Sept. 7 bench trial, removes a temporary restraining order issued in June at the request of the National Assn. of Independent Insurers. The NAI's injunction request was prompted by the efforts of DataLister Inc. of Lakeland, Fla., to obtain proof-of-coverage information on individual employers. The information includes their identity, location, policy expiration date and insurer.

The NAI sued the Arizona commission, arguing that the data was proprietary and confidential. The insurer association also said that allowing DataLister to sell the data, primarily to prospecting agents, would create unfair competition.

Arizona Superior Court Judge William J. Schaffer III, however, said in a statement, "It seems to me that disseminating this information will foster competition, not restrict it, and that is fair and in the best interest of the state."

The judge's decision clears the way for DataLister to add Arizona employers' records to its database, bringing to 27 the number of states contributing, for a total of more than 3.5 million employer records.

"We are delighted to see the court confirm the public nature of this important data," said C. Charles Murray, DataLister's senior vp.

The NAI is reviewing the decision and considering appealing it, according to Sam Sorich, an NAI vp based in Sacramento, Calif.

Briefly noted

Brera Capital Partners L.P. plans to buy claims specialist **GAB Robins** from SGS Societe Generale de Surveillance Holding S.A. for an undisclosed amount. The acquisition by the private equity firm will allow GAB Robins to pursue broader opportunities and expand its core strengths in loss adjustment, third-party administration and medical cost containment services, Brera officials said in a release. Brera representatives, however, declined to provide specific plans for expanding GAB Robins' services. The sale is expected to be completed in the fourth quarter of this year. . . . A Stanislaus County Superior Court judge in Modesto, Calif., last week **overturned an award of \$290 million in punitive damages** against Ford Motor Co., ruling that because the jury had discussed a juror's dream and a TV show during deliberations, it had injected issues not presented as evidence in the trial. Judge Roger Beauchesne ordered a new trial on the punitive damages, a Ford spokesman said. The judge, however, upheld the jury's finding that a defective roof on a Ford Bronco was responsible for the deaths of three people when it overturned on a freeway in June 1993. He reduced a \$5 million award to surviving family members by \$469,000. The spokesman said Ford is likely to appeal. . . . **American Home Products Corp.** has settled a case involving its diet pills for less than 10% of the \$23.4 million verdict awarded to Deborah Lovett by a Texas jury in August. The Madison, N.J.-based drugmaker agreed to withdraw all its appeals in exchange for the settlement and ending the suit. Texas law would have required a significant reduction in the \$20 million of punitive damages awarded to Ms. Lovett. . . . The full U.S. House of Representatives is expected to begin debating a measure that would allow interstate class-action lawsuits to be moved **from state to federal court** by either defendants or plaintiffs under certain circumstances (*BI*, July 26). Proponents of the measure, which has considerable business support, say the change is necessary to rein in "forum shopping," whereby plaintiffs attorneys attempt to have national class-action suits tried in state courts with reputations as being predisposed to plaintiffs. . . . ServiceMaster Co. will appeal a **verdict of more than \$136 million** awarded last week by a jury in a Georgia state court. The verdict consisted of \$1.3 million in compensatory damages and \$135 million in punitive damages. The case involved a former ServiceMaster salesman, Ray Martin, who sued for unpaid commissions after the Downers Grove, Ill.-based company fired him. . . . Santa Ana, Calif.-based **PacifiCare Health Systems Inc.** said Robert B. Stearns, its executive vp and chief financial officer, has resigned after about a year with the managed care company. A PacifiCare spokeswoman said the company and Mr. Stearns had different visions for the company. Separately, the spokeswoman said PacifiCare has been restructured into three divisions: Health Plans, Specialty Products and a Seniors division.

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