

SUPREME COURT FRAUD RULING RAISES DISCLOSURE QUESTIONS FOR SOME ADVISERS / PAGE 3

ECONOMIC DOWNTURN COULD PROLONG SOFT MARKET / PAGE 3

LIABILITY INSURANCE BUYERS STICK WITH SAME LIMIT LEVELS DESPITE FALLING RATES / PAGE 3



In Brief

XL downgraded to A on SCA losses

A.M. Best Co. Inc. and Fitch Ratings Ltd. have downgraded the financial strength rating of Bermuda-based XL Capital Ltd.'s property/casualty and reinsurance units to A from A+. The downgrades follow XL's announcement that it will record a fourth-quarter charge of up to \$1.7 billion, much of it stemming from investments in Security Capital Assurance Ltd. Fitch also downgraded its ratings of SCA and its financial guarantee units, including XL Capital Assurance Inc., to A from AAA. Both were units of XL that were spun off in public offerings. XL retains a 46% stake in SCA.

Firm takes stake in Beecher Carlson

New York-based global investment firm Old Lane L.P.,

See **IN BRIEF** page 22

SPOTLIGHT

EMERGING MARKETS: LATIN AMERICA

Brazil, Mexico lead demand for more sophisticated risk management services in region; Panama Canal expansion provides opportunities for multi-nationals; insurers try affinity



strategies to grow business in Latin America; company says captive broker gives it inside edge. **Page 10**

Gaps in data slow retiree Rx subsidies

Administrative hassles hold up payments

By **JOANNE WOJCIK**

Employers that provide prescription drug coverage for their retirees are finding that the application process for the Medicare Retiree Drug Subsidy is a lot harder than they expected.

Prescription drug benefit options available to employers under the Medicare Modernization Act of 2003:

- Receive a tax-free subsidy of 28% of eligible prescription drug expenses for employers that offer drug benefit plans equal to the Medicare Part D drug benefit.
- Supplement Medicare D coverage.
- Contract with a commercial prescription drug plan or Medicare Advantage Plan, which would receive capitated payments from the federal government that could be used to reduce premiums.
- Create an employer-owned PDP, where the employer receives the capitated payments directly from the federal government.

Because of administrative snafus such as not having Social Security numbers for all plan members—something the Centers for Medicare & Medicaid Services requires for payment—some employers are now scrambling to meet a March 31 deadline for final reconciliation. If they are unable to confirm eligibility of all of their plan members, they will not be paid for them, or worse, they may have to pay back any interim pay-

ments they've already received on behalf of those retirees.

Because of these hassles and a variety of other reasons, some employers that provide prescription drug benefits to Medicare-eligible retirees are now considering alternatives to the RDS, retiree health benefits experts report (see story page 20).

Under the Medicare Modernization Act of 2003 employers have several options (see box).

Most employers opt to take the tax-free subsidy, because it gives them the most control and doesn't require any plan changes to be made, according to Rick McGill, a principal responsible for medical consulting services in the Atlanta office of Hewitt Associates Inc.

"Financially, an employer has sole discretion over what they do with the subsidy. It's also tax-free. And from the retiree perspective, it's non-disruptive," he said.

Moreover, commercial prescription drug plans, in which Medicare drug benefits would be offered by vendors, such as prescription benefit managers were few and far between in early 2005, which was when Part D regulations were promulgated, and when employers began developing their benefit strategies for 2006, according to Mike Morfe, senior vp at Aon Consulting in Somerset, N.J.

But the RDS application process has turned out to be "very labor-intensive for plan sponsors," said Stephen Parahus, a

See **SUBSIDY** page 20

Lawmakers OK FMLA expansion

Military family members would get new leave

By **JERRY GEISEL**

WASHINGTON—Legislation on its way to President Bush will expand Family and Medical Leave Act coverage for family members of employees called for military service.

The expansion, included in a broader Department of Defense spending measure, is the first for the 1993 law, which requires employers to allow employees to take up to 12 weeks of unpaid, job-protected leave in a year after the birth or adoption of a child, to care for sick child, parent or spouse or when an employee has a serious illness. While on leave, employers must continue to provide health insurance coverage to employees the

same as if the employee continued to work.

The legislation, H.R. 4986, which received final congressional approval last week, is expected to be signed by President Bush.

The legislation will expand the FMLA in two ways for military families.

Under the first expansion, employees will be allowed to take up to 12 weeks of leave when a spouse, child or parent is on active duty in the armed forces or is called up for active duty. Leave could be for any "exigency," as defined by regulations to be drafted by the Labor Department, the federal agency that enforces the FMLA.

See **FMLA** page 21

Defense plans at odds in Gen Re finite trial

Two defendants seek to separate from others

By **DOUGLAS McLEOD**

HARTFORD, Conn.—Elizabeth Monrad and Christian M. Milton sit at opposite ends of a row of tables in a Hartford federal courtroom, a separation that reflects their defense positions: As a trial over their parts in an allegedly fraudulent 2000 reinsurance deal progresses, their lawyers are increasingly battling each other as well as the prosecution.

Lawyers for Ms. Monrad, General Re Corp.'s former chief financial officer, and Mr. Milton, a former AIG reinsurance vp, renewed efforts last week to sever their cases from those of three other defendants, arguing that their defenses are mutually antagonistic.

Ms. Monrad contends that she

accounted for \$500 million loss portfolio deal with AIG properly as a deposit transaction, told AIG that Gen Re would account for it that way and had no reason to believe AIG would account for it differently.

Mr. Milton, on the other hand, argues that he believed the deal transferred sufficient risk for AIG to account for it as reinsurance, and that he was deceived on that point by Gen Re officials, including John Houldsworth, former chief executive officer of Gen Re's Cologne Re Dublin unit, who began testifying for the government last week.

"I think these are irreconcilable defenses, and I think that will con-

See **GEN RE** page 22



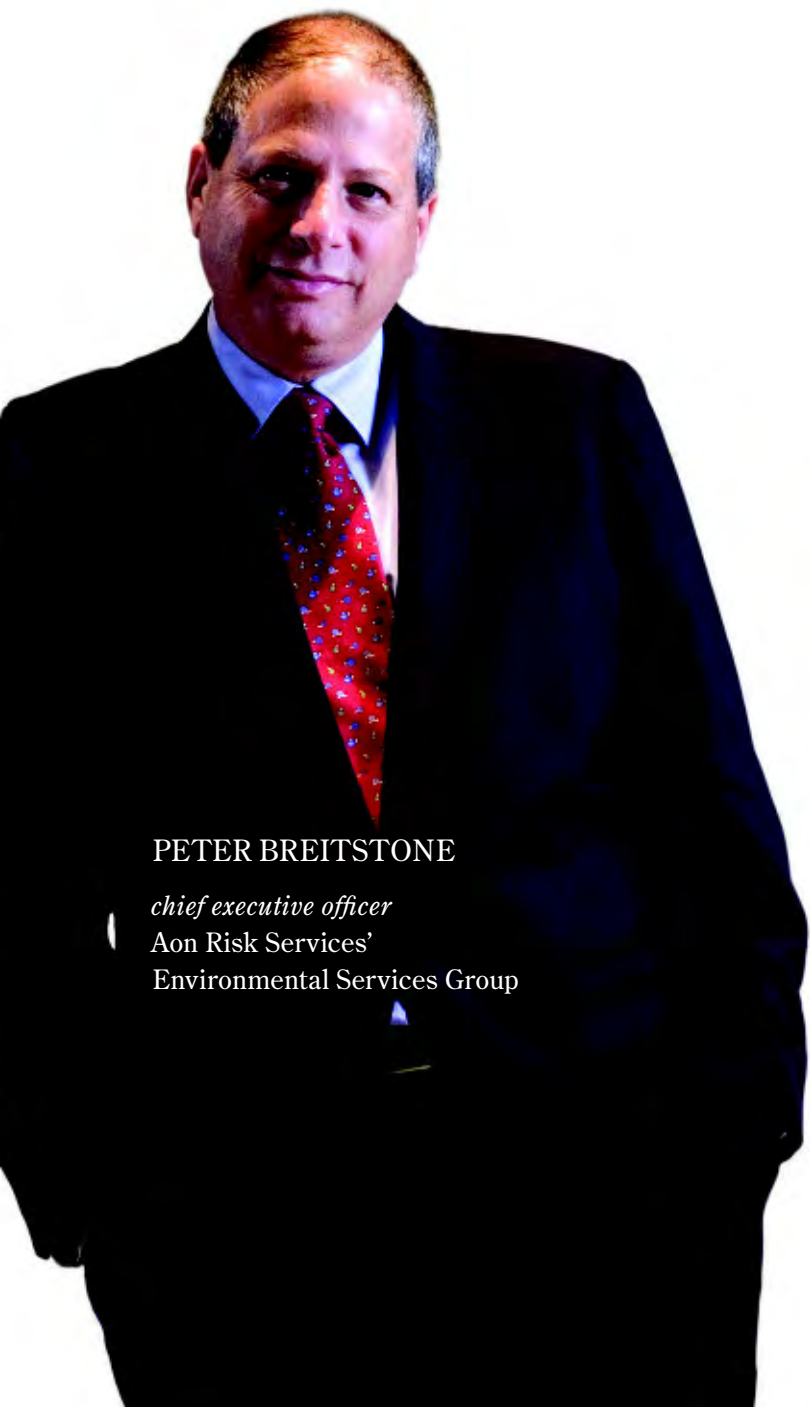
ONLINE: Daily reports, other resources available at www.businessinsurance.com/GenReTrial

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Are you ready to discuss the opportunities created by climate change?

Ask Aon.



PETER BREITSTONE

chief executive officer
Aon Risk Services'
Environmental Services Group

While there may be debate about causes of climate change, there is little dispute that global warming is happening. As the physical, financial, regulatory and legal risks associated with climate change evolve, are you ready to capture the developing opportunities?

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Go to www.aon.com/ask and get ready for change.



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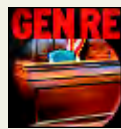
AON RISK SERVICES

On the Web

GEN RE/AIG TRIAL

Complete Gen Re/AIG trial coverage online

The criminal fraud trial of five former executives of Gen Re and



American International Group got under way Jan. 7 in federal court in Hartford, Conn.

The case centers on a finite reinsurance deal between Gen Re and AIG that prosecutors allege was a sham transaction. *Business Insurance* is following this trial closely and will update readers on the latest developments, witnesses and evidence presented at www.BusinessInsurance.com/GenReTrial.

QUESTIONS & ANSWERS

Podcast interview explores Latin America

Business Insurance's page 12 interview with Eugenio Paschoal, Willis Group Holdings Ltd.'s chief executive officer for Latin America, is offered in its entirety online at www.BusinessInsurance.com/Qanda.

EMERGING RISK STRATEGIES

New John Hampton column now online

In the latest Emerging Risk Strategies column, John J. Hampton, professor of business at St. Peter's College in New Jersey, discusses the drivers of enterprise risk management and logical starting places for implementing ERM. To read this and all of his archived columns online, visit www.BusinessInsurance.com/ERM.

THIS WEEK IN BI

New podcast takes you behind the BI headlines

"This Week in *Business Insurance*" is a new weekly podcast that reviews the headlines in each new issue of and interviews reporters for in-depth insights on the top stories of the week. Listen to these audio reports online at www.BusinessInsurance.com/thisweek to stay informed.

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Recession could drive rates down further

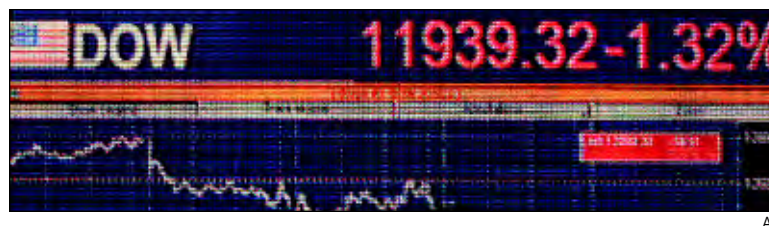
Insurers would have to deal with lower prices, demand in economic downturn

By MARK A. HOFMANN

As concerns about a possible recession rise, industry observers say such economic conditions would prove trying to insurers, while risk managers may continue to enjoy soft market conditions.

Because of "the coincidence of the soft market with the recession," risk managers could "probably be able to get some lowering of rates," said Steven N. Weisbart, vp and chief economist for the insurance industry-backed Insurance Information Institute in New York.

Insurers, on the other hand, would have to deal with diminished demand for their products at a time when claims could rise. And some of the projected increase in claims



Fears of a recession increased in recent weeks as stock markets plummeted.

would be due to outright fraud (see story, page 21).

But analysts also caution that the insurance underwriting cycle and the business cycle don't always coincide.

"The insurance cycle is not necessarily the same as the economic cycle," said Mark Lane, principal and equity research analyst with

William Blair & Co. in Chicago.

Of course, the economy is not in a recession yet, despite fears of pending downturn fueled in part by an erratic equities market in recent weeks. A recession is generally defined as occurring when the economy experiences at least two consecutive quarters of negative economic growth. There has not

been even a single quarter of economic contraction in years.

The current turmoil in the equities markets—driven by the subprime mortgage crisis and other credit-related concerns—probably won't have a significant direct impact on insurers, say analysts.

"I don't think it will have a major impact," said Cliff Gallant, an analyst with Keefe, Bruyette & Woods Inc. in New York. The subprime losses could cause more claims for some professional liability coverages like directors and officers liability, he said. But in general, "I think the capital position of the industry is relatively strong. We continue to look for modest price softening,

See **RECESSION** page 21

High court fraud ruling raises disclosure issues

Stoneridge limits liabilities of third parties

By DAVE LENCKUS

While the U.S. Supreme Court has limited the potential liability of third parties in securities fraud lawsuits, business partners and advisers that suspect they inadvertently facilitated fraud at another company face some tough challenges, legal experts said.

Those companies have to weigh the odds that their activities—even if not designed to help another company defraud its investors—were relied on by those investors and then balance the potential risks and rewards of publicly disclosing those activities, attorneys said.

Making such disclosures could prevent the company from being drawn into another company's securities fraud litigation, some experts said.

But raising questions about another company's actions could trigger a securities fraud case and pull the whistleblower into the middle of it, other experts said.

"That may well be the law of unintended consequences," said plaintiffs attorney Barbara J. Hart, a partner with Labaton Sucharow L.L.P. in New York.

In its Jan. 15 decision in *Stoneridge Investment Partners L.L.C. vs. Scientific-Atlanta Inc.; Motorola Inc.*, the high court limited the cases when defrauded investors can recover from third parties—even those that knowingly facilitated another company's fraud—to those in which the investors relied on the defendants' actions (*BI*, Jan. 21).

Separately, last week the Supreme Court without explanation refused to hear a case involving similar claims by Enron Corp. investors.

Attorneys distinguish between

the third-party liability risks faced by a company's business partners and suppliers—such as those involved in the *Stoneridge* case—and lawyers, accountants and auditors—who can be integral players in the preparation of a company's financial statements and related notes.

In the *Stoneridge* case, investors of St. Louis-based Charter Communications Inc. sued two of the company's suppliers for allegedly participating in a financial fraud scheme. The investors argued that the deal did not result in a true revenue increase for Charter but facilitated

an accounting manipulation that allowed it to boost sagging revenues in 2000. When discovered, that manipulation and others forced Charter to restate years of earnings and triggered a dramatic drop in its share price.

While the suppliers dodged liability because Charter's investors could not show they relied on the transaction, a comparable scenario with an important distinction could trip up other third parties that discover they inadvertently facilitated fraud, attorneys said.

For example, if a stock issuer publicly announces the transaction and its financial impact, "then, I think, (the suppliers) are at risk, unless they put out some corrective statement," said insurer attorney Arthur J. Washington, a partner at Mendes & Mount L.P. in New York.

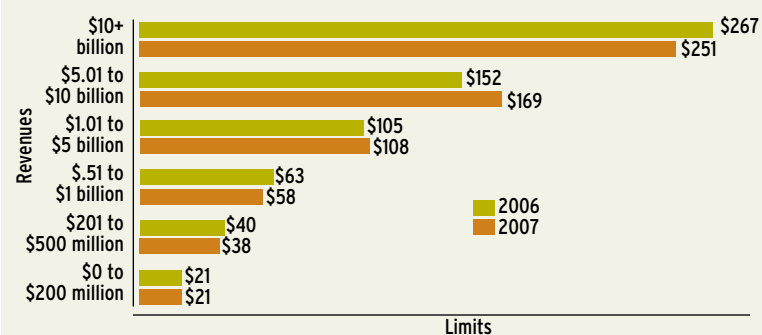
Also, if the suppliers issue a public statement about the transaction, "then they'd get tagged" by the investors, he said.

The suppliers have "got to put two and two together and may—and I emphasize may—be under a

See **STONERIDGE** page 18

LIABILITY LIMITS PURCHASING TRENDS

Participants' average limits purchased by company revenue size. In millions of dollars.



Source: Marsh Inc.

Buyers keep same limits as liability rates slide

Risk managers buying 'more on budget' than on potential for loss

By SALLY ROBERTS

Despite continued price declines in the cost of liability coverage, insurance buyers, in general, are not buying more coverage, according to a new Marsh Inc. global study of its clients.

The average limit purchased by the more than 7,000 worldwide Marsh clients surveyed was \$47 million in 2007, the same as it was in 2006, Marsh found. This comes despite the average price per \$1 million of coverage falling 5.3% to \$10,084 in 2007.

Marsh studied 7,265 clients from 58 countries for its "Limits of Liability 2007" report, which presents a range of information to help companies decide how much excess liability insurance they need.

"While limit purchasing might have historically followed pricing, we're not seeing it followed to the same extent as when prices went up," said George G. Pallis, managing director of Marsh's national casualty practice in Morristown,

N.J. "People were much more reactive to the increase in pricing by reducing their limits than they've been to increasing their limits when pricing is down."

"It appears to be that people are buying more on budget than on need," Mr. Pallis said. They have X amount of dollars to spend and want to know how much that buys them rather than looking at what the potential catastrophe is and how that can affect their organization, he added.

While Mr. Pallis noted that it's difficult to determine the appropriate limits until a large loss occurs, risk managers should look at their company's operations, their potential exposures, any past losses and answer some what-if scenarios.

And in terms of potential exposures, while products liability and motor vehicle accident cases continue to dominate the largest jury verdicts awarded in the United States, insurance buyers should keep in mind other emerging risks, including those associated with the ever-increasing global economy, Mr. Pallis said. Last year's concerns over products manufactured in China, from toys to pet food to tooth-

See **LIMITS** page 19

Securities class action risk expected to rise, study finds

Lawsuit filings will increase, hit more small cap companies, according to Corporate Library analysis

By DAVE LENCKUS

Corporate America should expect a robust year for securities class action filings in 2008, with filings likely climbing back to a 10-year norm of 194, according to a research company.

A two-year lull in filings that ended in mid-2007 was an anomaly, and companies with small market capitalizations—which once faced very little risk of securities fraud lawsuits—will be more frequent targets for disgruntled investors this year, predicts the Corporate Library, an independent corporate governance research and analysis firm based in Portland, Maine.

Investors also will increasingly

seek to recover losses from financial institutions, which have seen just the “tip of the iceberg” of additional claims, and high tech companies, said Ric Marshall, chief analyst and a co-founder of Corporate Library. The frequency of claims against pharmaceutical companies also will continue at about the same strong pace, he said.

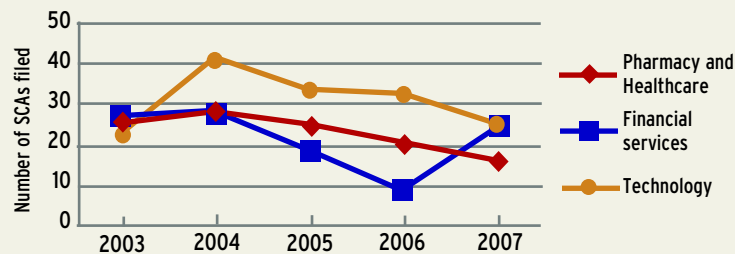
Mr. Marshall made his predictions in discussing the research firm’s report, “Predicting Securities Litigation—2007 Year-End Report,” which was released this week.

Both the 2008 and 2007 projections were derived using a predictive tool—which analyzes 35 factors—that Corporate Library has developed.

Mr. Marshall said he would give

HIGH-RISK INDUSTRIES

Within Corporate Library's database, companies in four industries faced the greatest risk of investor lawsuits since 2003



Source: The Corporate Library

the Corporate Library a “B” grade for its 2007 predictions on the lawsuit risk that the 3,047 companies

in its database faced. One hundred companies in the database were sued, while 169 companies overall

were sued last year.

Mr. Marshall explained that the predictive tool last year did not adequately anticipate the jump in claims against small-cap companies. That heightened risk has been factored into the tool for 2008, he said.

The database currently includes 3,290 companies.

A comparison of the 2008 and 2007 findings show some striking differences that portend mostly bad news for corporations.

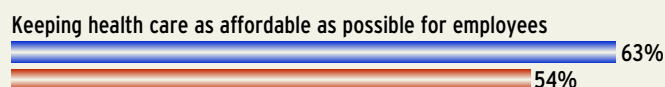
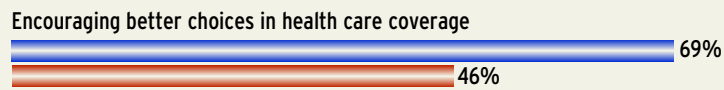
For example, 27.1% of the companies face a high risk of being sued this year, compared with 17.5% last year. Similarly, 47.1% are rated moderate risks this year, compared

See **SECURITIES** page 6

MEASURE OF SUCCESS

Impact of health plans in 2007 compared to 2005.

Encouraging better use of health care



Traditional plan sponsors ABHP sponsors

Source: Towers Perrin

Study examines success of consumer-driven plans

Towers Perrin finds plans aid workers' health

By JOANNE WOJCIK

Employers that help their employees understand how to manage the risk inherent in high-deductible health plans linked with health savings accounts are likely to have better experience than those that don't, a survey by Towers Perrin shows.

Success with such account-based health plans, Towers Perrin's term for what is generally known as a consumer-driven health plan, also depends on an organization's overall climate, including such factors as trust in management and a sense that the employer cares about its employees' well-being, according to the survey conducted during 2007 by the Stamford, Conn.-based risk management and benefits consultant.

“Strategic, thoughtful change management initiatives, along with targeted, ongoing communication

and visible leadership can go a long way toward building trust and a healthy work environment,” states the survey, “Account-Based Health Plans: What Works—and Why.”

The survey, which was released last week, included responses from 150 employers offering the plans and about 500 plan participants. These responses were compared with those of 200 employers that do not offer such plans and 500 employees enrolled in traditional health plans.

Towers Perrin conducted the research project to identify what factors characterize successful account-based plans, said Jay Savan, a principal at Towers Perrin based in St. Louis.

“We felt there was a lot of information available on financial performance, but not much on attitudes and perceptions,” he said.

See **CDHP** page 19

\$458M Big Dig settlement reached

Civil suit pending against two other companies involved in project

By JEFFREY CASALE

BOSTON—A settlement of \$458 million has been reached in Boston's “Big Dig” project, and litigation is pending against two other companies involved with the project.

Massachusetts Attorney General Martha Coakley last week announced at a press conference that state and federal investigators reached an agreement with Big Dig project manager Bechtel/Parsons Brinckerhoff and 24 small design companies involved in the highway's construction.

However, Ms. Coakley added that a civil lawsuit is still pending against construction contractor Modern Continental Construction Co. and designer Gannett Fleming Inc.

Bechtel/Parsons Brinckerhoff agreed to the settlement to resolve



A \$458 million settlement was reached in the collapse of a highway tunnel on I-90 in Boston.

its criminal and civil liabilities in connection with the collapse of the I-90 Connector Tunnel ceiling and defects in the slurry walls of the Tip O'Neill tunnel.

The partial ceiling collapse resulted in the death of Milena Del Valle, a passenger in a vehicle, in July 2006. An investigation by the National Transportation Safety Board revealed that the epoxy adhesive used in the tunnel's construction failed, causing portions of 26-ton concrete panels to fall and crush the vehicle in which Ms. Del Valle was riding. Bechtel/Parsons Brinckerhoff, Gannett Fleming, Modern Continental and Powers Fasteners Inc. were all named liable parties according to the NTSB report (BI, July 16, 2007).

“We have always said that we take responsibility for our work,” a statement issued by San Francisco-based Bechtel/Parsons Brinckerhoff said. “We understand and acknowledge with this resolution that our

See **BIG DIG** page 19

Appeals court OKs stock fraud case after considering High Court ruling

By DAVE LENCKUS

CHICAGO—A federal appellate court has upheld its decision to allow a securities fraud case to proceed against Tellabs Inc. nearly seven months after the U.S. Supreme Court overturned the earlier ruling because of the appellate court's improper analysis of the claimants' allegations.

The closely watched case, *Tellabs Inc. et al. vs. Makor Issues & Rights Ltd. et al.*, has turned on a provision in the 1995 Private Securities Litigation Reform Act that requires claimants to allege detailed facts sufficient to establish “a strong inference” that the defendants acted with intent to commit fraud.

Overturing a 2004 district court decision that dismissed the case, the

7th U.S. Circuit Court of Appeals ruled in January 2006 that the case could proceed because a reasonable person could infer that the defendants acted with fraudulent intent. The 7th Circuit did not consider inferences that it could have made from the facts in the case that Naperville, Ill.-based Tellabs and other defendants had acted innocently in misleading investors about the company's sales prospects.

Courts in other circuits had considered inferences of culpability and innocence but balanced them in different ways when they determined whether to dismiss a case. That inconsistency prompted the Supreme Court to review the *Tellabs* case (BI, Jan. 15, 2007).

The Supreme Court ruled plain-

tiffs' allegations should survive only if—after considering all plausible fraudulent and innocent inferences that a court could draw from defendants' activity—a reasonable person would find the plaintiffs' arguments “at least as compelling” as any opposing inferences that person could draw (BI, July 2, 2007).

In reconsidering the case on remand from the Supreme Court, the 7th Circuit on Jan. 17 analyzed both how the corporation and its former chief executive officer and other senior management could have been misled into issuing misleading statements to investors and the likelihood of that occurring.

The appellate panel concluded that management far more likely intentionally misled investors.

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Sidecar formations dwindle due to softening market

Arrangements are expected to make a comeback when the need for capacity arises

By JUDY GREENWALD

Sidecars' heyday is over, at least for now, observers say.

The softening market has made them unnecessary at present, but they are expected to make a comeback when the market hardens, and if there is a major catastrophe, they say.

For now, some sidecars will continue to be formed, but on a smaller scale than their predecessors, and only in certain niche segments, some observers say.

Sidecars are special-purpose vehicles, often capitalized by hedge funds, which provide capacity to existing reinsurers by assuming risk, typically through quota-share reinsurance contracts that may have a duration of two years or less. The sidecar assumes a percentage of premiums in return for assuming the risk, which is generally property catastrophe reinsurance.

Sidecar formations took off after the hurricane losses in 2005, when they provided much needed capital. Twenty sidecars were formed in 2006, representing \$4.5 billion in capital, according to Oldwick, N.J.-based A.M. Best Co. Inc. But by 2007, with a mild catastrophe season and a softening market, only eight were formed, representing \$1.87 billion in capital, according to Best.

A further decline in formations is expected this year, barring major catastrophes, observers say. A complete picture of which sidecars are being unwound will not emerge

until companies report their fourth-quarter results, said Mark Rouck, senior director with Fitch Ratings Ltd. in Chicago.

"You see a lot of sidecars not being renewed, or renewed with smaller limits," said Emmanuel Modu, managing director of structured finance for Best in Oldwick. He pointed to Concord Re Ltd., which had a collateralized quota-share reinsurance treaty with Lexington Insurance Co., a subsidiary of New York-based American International Group Inc., and was terminated largely as scheduled on Dec. 31, 2007.

In addition, it was announced earlier this month that Bermuda-based White Mountains Insurance Group Ltd. unit White Mountains Re is acquiring sidecar Helicon Reinsurance Co. Ltd. The sidecar had provided quota-share retrocessional coverage to White Mountains Re in 2006 and 2007, and was then put in runoff.

Meanwhile, XL Re, a unit of Bermuda-based XL Capital Ltd., entered into a quota-share reinsurance treaty with a new sidecar, Bermuda-based Cyrus Reinsurance II Ltd., which put about \$136 million into a trust to support its coverage. In contrast, its predecessor, Cyrus Reinsurance Ltd., deposited \$525 million into a trust following its 2005 formation.

"Sidecars by design are temporary vehicles," said Steven K. Bolland, president of New York-based reinsurance intermediary Gill & Roeser Inc. "The main reason for setting them

up is the sponsoring entity...doesn't want to raise permanent capital but wants to take advantage of a short-term situation. Sidecars are a very good solution to a short-term problem; therefore I think what you will see is sidecars moving in and out of the market, depending on the status of the market at that specific time."

Right now, though, "there is sufficient capacity and therefore the need for sidecars has diminished significantly," Mr. Bolland said.

Sidecars are "nothing more" than special quota-share programs that "were created at a time when there was increasing demand for capacity. That spigot has been turned off," said John N. Gilbert, chairman of reinsurance intermediary Holborn Corp. in New York.

"We think there'll be fewer sidecars because it's just more difficult to achieve the necessary internal rate of return, which is basically what equity investors are looking for," said Beat Holliger, managing director at Munich Re Capital Markets in New York.

"It just does not make economic sense," given the current environment, said Albert Selius, head of asset-backed and insurance-linked securities trading at Swiss Reinsurance Co. in New York.

But, Mr. Bolland said, "it only takes one or two large losses during the course of the year, when suddenly additional capacity would be required," and the sidecars would become very popular again.

John L. Ward, chief executive officer of Cincinnati-based Cincinnatus Partners L.L.C., an advisory firm that specializes in the insurance industry, said, "when the market outlook changes, which it undoubtedly will at some point in the future, sidecars will be the structure of choice, and will rebound at the appropriate time."

"I don't think they're a thing of the past," said attorney Charles G.R. Collis, of Bermuda-based Conyers Dill & Pearman, who advises insurance industry clients on corporate and regulatory matters. "They have their time and their place."

Meanwhile, sidecar formations will continue, but in a somewhat different form, said Ed Torres, New York-based senior vp at Benfield Advisory Inc., a unit of the Benfield Group. "The sidecars of 2006 and 2007 were largely made up of whole account, quota-share deals for reinsurance companies," which may have encompassed European, Japanese, U.S. and/or Australian catastrophe risk.

Going forward, there will be an opportunity for "more select portfolios to be put into a sidecar," Mr. Torres said. There may be certain niches within the market where investors can find the returns they are seeking and there is still a need for excess capacity, he said.

For instance, he mentioned Starbound Reinsurance II Ltd., which Bermuda-based RenaissanceRe Holdings Ltd. launched last year to provide an additional \$375 million in reinsurance capacity for the Florida homeowners market (*BI*, June 11, 2007).

There may continue to be good opportunities for sidecars where there is a "pinpoint need for capital with unusual high return potential," said Mr. Ward.

James Brender, a director at rating agency Standard & Poor's Corp. in New York, said, "Nothing's actually happened yet, but we've gotten inquiries about possible ways to bring capital" into different lines of business, including casualty, with sidecars.

Big Dig: Settlement reached, some litigation pending

CONTINUED FROM PAGE 4

performance did not meet our commitment to the public or our own expectations. Above all, we deeply regret the tragic death of Milena Del Valle in the I-90 tunnel."

The majority of the \$458 million will be held in a new state Central Artery/Tunnel Project Repair and Maintenance Trust Fund to provide for future nonroutine repairs and maintenance of the Big Dig, Ms. Coakley said in a statement. The project's owner controlled insurance program will cover \$40 million of the payout.

Further, the agreement does not release Bechtel/Parsons Brinckerhoff from liability for any future catastrophic events that occur with-

in the next 10 years. Any event that causes more than \$50 million in damages will be Bechtel/Parsons Brinckerhoff's responsibility, with a cap of \$100 million, according to a statement released by Ms. Coakley.

"It is critically important that federal and state tax dollars needed to fund important public works projects, like the Big Dig, are safeguarded against waste, fraud and corruption," U.S. Attorney Michael J. Sullivan, who assisted Ms. Coakley with the investigation, said in a statement. "Our work is not done. We will dedicate the resources and time necessary to complete a comprehensive review and investigation of the Big Dig Project. I can assure you that there will be no stone unturned."

Securities: Litigation filings expected to climb this year

CONTINUED FROM PAGE 4

with 35.1% last year. And the number of companies classified as low risk this year fell by nearly half to 21.2% from 41% in 2007.

But the percentage of very high risk companies dropped by nearly one-third to 4.5% from 6.4%.

Among the risk factors that show that a company is at a heightened risk of facing a securities fraud lawsuit, "the most powerful indicator" is excessive compensation for the chief executive officer.

Other powerful indicators include:

- The ages, tenures, over-commitments and lack of independence of

company directors.

- 60% or greater ownership of traded stock by institutional investors.

- Conducting business within the high-tech, pharmaceutical, health care and financial services industries.

- A market cap of at least \$400 million, though small-cap companies' risk is growing.

- An annual trading volume of between 2 billion and 25 billion shares.

Copies of "Predicting Securities Litigation—2007 Year-End Report" are available for \$250 and can be ordered online at www.thecorporatelibrary.com.

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Business Insurance OPINIONS

Slipshod treatment mars FMLA measure

WHILE WE SUPPORT legislation that expands benefits under the Family and Medical Leave Act for family members of employees called up for military service or on active duty, we are disappointed in the careless way the measure was put together.

As we report on page 1, the FMLA expansion—included in a broader Department of Defense spending bill that received final congressional approval last week—will more than double the amount of leave family members can take to care for a close family member injured during the course of military service.

In addition, family members would be eligible for up to 12 weeks of FMLA leave when a relative is called up for military service.

We have no problem with the expansion of the FMLA. Employees called up or who enlist deserve, along with their families, support and this legislation, in a very modest way, does just that.

We have no problem with the expansion of the FMLA.

What we do have a problem with—and this isn't the first time this has happened in the employee benefits arena—is the way the legislation was passed.

Given that this expansion will affect hundreds of thousands of employees and their families—to say nothing of their employers—one would have thought some care would have gone into the drafting of the legislation.

That, unfortunately, was not the case. Indeed, something basic, yet essential for implementation and administration, was left out: the provisions' effective date.

Additionally, while we fully understand why legislation can't always be detail rich—that is what regulations are for—this measure gives way too much discretion to regulators.

Legislators have a duty to their constituents to get it right when looking at the big picture and working out the details. In approving FMLA expansion, federal legislators passed only one of those tests. We hope they do better the next time.

Catastrophe backstop still a flawed concept

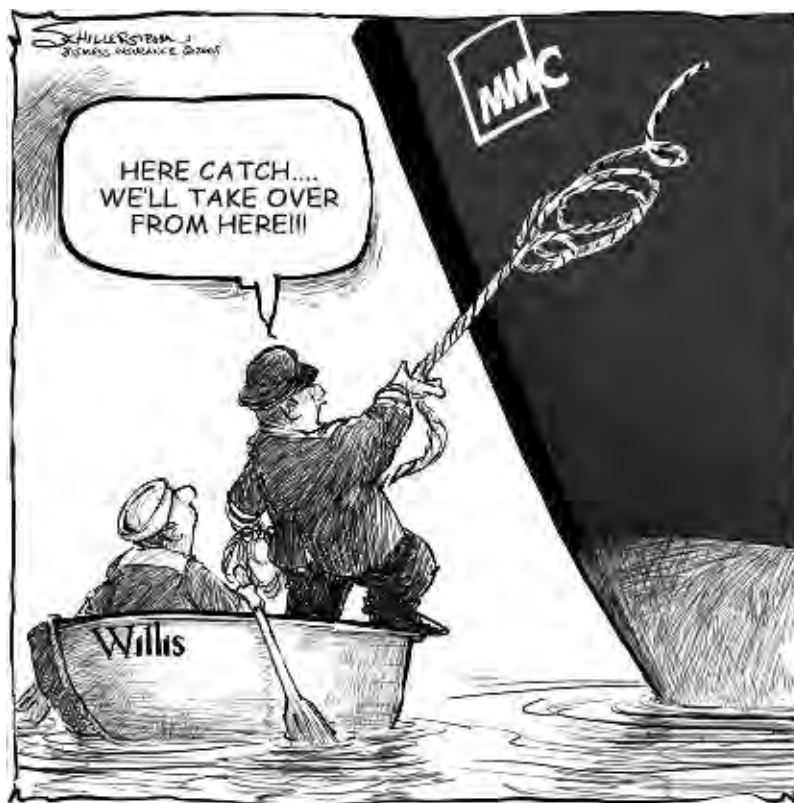
A FUNNY THING happened at last week's Republican presidential debate in Boca Raton, Fla. Two of the would-be standard bearers of the party generally associated with free enterprise came out in favor of some sort of national catastrophe insurance backstop to pay for losses associated with hurricanes.

That general idea, which won the endorsement of former New York Mayor Rudolph Giuliani and former Massachusetts Gov. Mitt Romney, enjoys widespread support in some coastal areas, and understandably so. As we've noted before, no one wants to pay the high property insurance rates underwriters will demand to cover a home or business that happens to be in harm's way. And as we've noted before, just because there's support for an idea doesn't make it a good one.

There's no evidence of market failure regarding catastrophe insurance. Unlike terrorism risk—which defies quantification—hurricane exposure can be easily quantified based on more than a century's worth of data. Insurers write coverage in hurricane-exposed areas, provided that they can charge actuarially sound premiums.

To make the government a player in a market that hasn't failed is bad public policy, period. While it's politically attractive, it's also economically dubious. Political pressure will keep rates artificially low, and when disaster strikes, the taxpayers will be left to make up the difference.

A far better approach is for government efforts to focus on mitigating the risk, not subsidizing it.



BI beats list

In an effort to ensure continuing timely coverage of risk management, insurance and benefit-related news, Business Insurance has formalized a list of its reporters' assigned beats. This list is not intended to be exclusive but rather to represent core subject areas of importance to BI readers. BI welcomes ideas and tips from readers on these and other areas. Following is a list of the beats and the principal reporters for each:

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Sally Roberts.

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Joanne Wojcik.

Benefits—retirement savings/pensions:

Jerry Geisel.

Canada—risk management and benefits:

Gloria Gonzalez.

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Judy Greenwald.

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Federal regulation/legislation—benefits:

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Federal regulation/legislation—risk management:

Mark A. Hofmann.

Health care industry operations:

Gloria Gonzalez.

Industry Focus:

Rodd Zolkos, Meg Fletcher.

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Latin American markets:

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Property/casualty industry operations:

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Property loss control/cat risks:

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Regulation of insurance:

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Reinsurance:

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Runoffs/receiverships:

Douglas McLeod.

Safety/ergonomics:

Meg Fletcher.

Surplus lines/insurance wholesalers:

Roberto Cenicerros.

Tort reform:

Mark A. Hofmann.

Work/life benefits and employee assistance programs:

Sally Roberts.

Workers compensation:

Roberto Cenicerros.

Online Poll at www.businessinsurance.com

How would an acquisition of Marsh & McLennan Cos. Inc. affect insurance buyers?



NEXT WEEK'S POLL: Is a federal backstop for natural catastrophe risks needed?

BI Online Poll tool sponsored by Wausau Insurance Cos.

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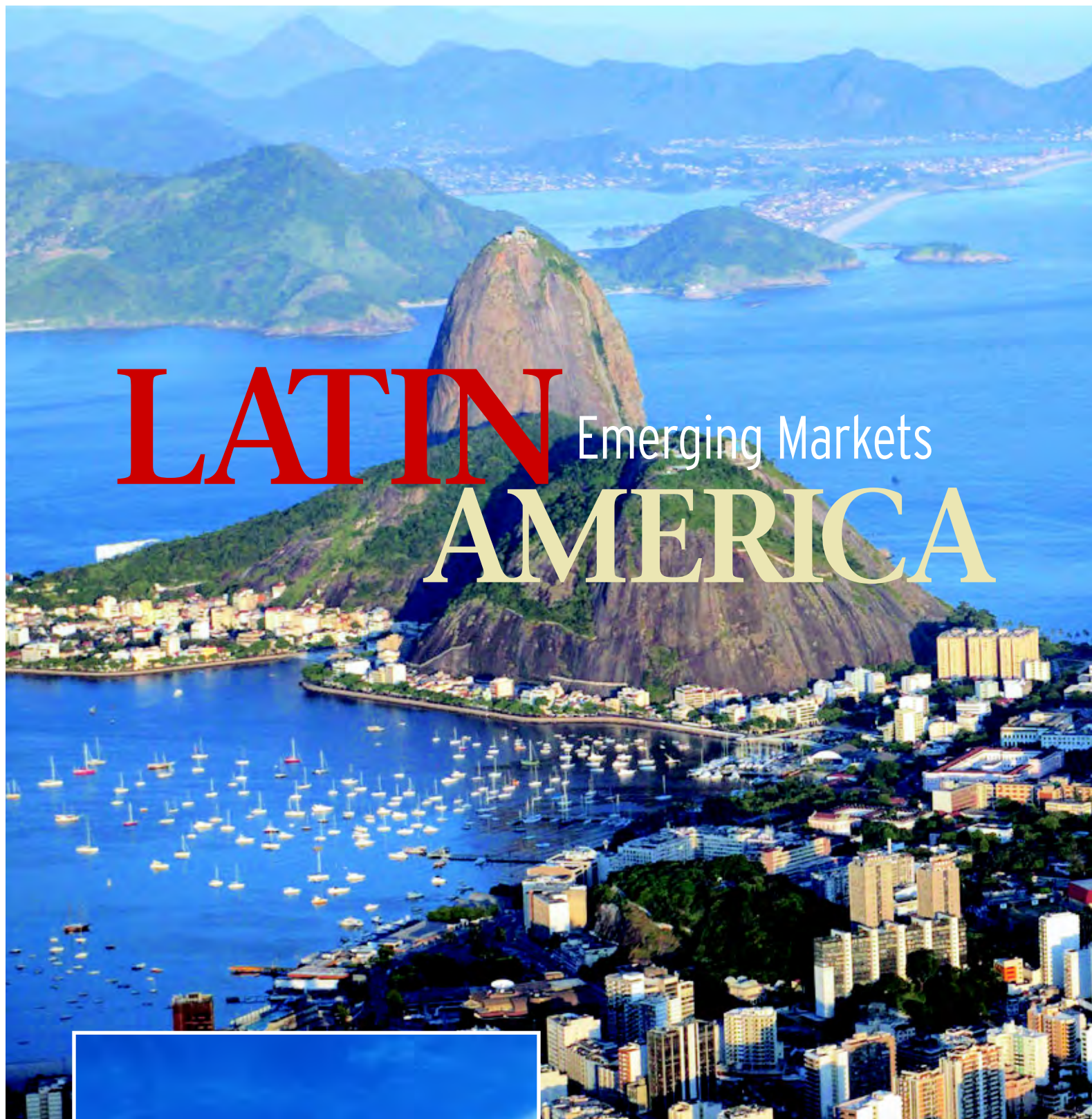
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LATIN AMERICA

Emerging Markets



GETTY IMAGES

Brazil, Mexico lead demand for risk financing services

By **ROBERTO CENICEROS**

Globalization, steady economic expansion and financial modernization are propelling Latin America's insurance markets to provide products and services once common only in more financially developed nations.

Brazil and Mexico, Latin America's two economic powerhouses, are particularly well-situated to continue prospering from globalization, which is driving growing demand for insurance services, observers say.

The two nations' massive populations of potential consumers dwarf the populations of surrounding countries. Foreign multinational companies, therefore, continue to expand their presence in Brazil, which has about 186 million residents, and in Mexico with 106 million residents.

Brazilian and Mexican conglomerates, in turn, have expanded abroad themselves. As they expand, they are increasingly demanding sophisticated financial and insurance services to help them

See **LATIN AMERICA** next page

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SPOTLIGHT

INSURANCE MARKET POISED FOR GROWTH

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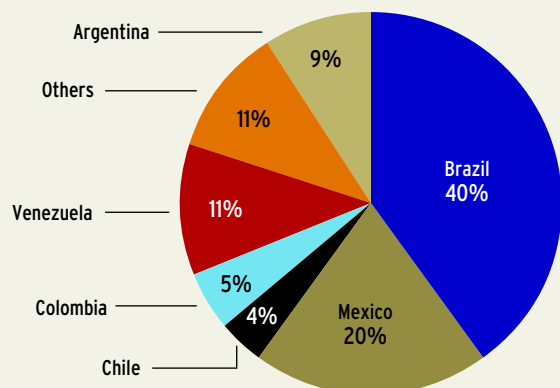
CAPTIVE BROKER GIVES COMPANY INSIDER'S EDGE

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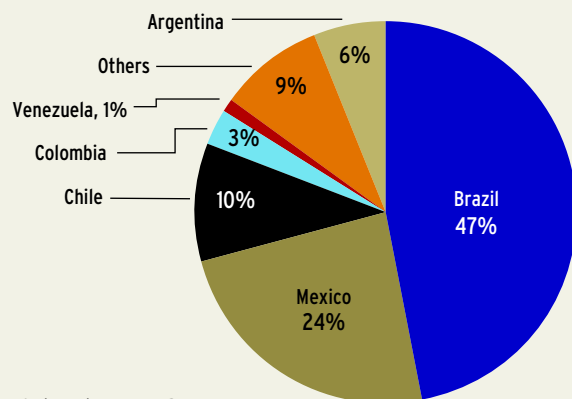
BREAKDOWN OF INSURANCE PREMIUMS

Latin America's 2006 nonlife and life premium volume is divided by country. About 2.4% of Latin America's gross domestic product was spent on insurance in 2006.

NONLIFE PREMIUM SPLIT



LIFE PREMIUM SPLIT



Source: Swiss Reinsurance Co.

Region's insurance market poised for 'strong' growth

Although Latin America's insurance market is growing, historically overall insurance penetration has been low in the region compared with developed nations, according to last year's "Latin America Insurance Market Review" by London-based reinsurance intermediary Benfield Group Ltd.

The region's gross written premiums amounted to only 2% of the worldwide total in 2005, Benfield noted about the latest data available. But Benfield also concluded that "the small size of (Latin America's insurance) market is counterbalanced by the potential for strong growth."

Benfield said insurance premiums in Latin America grew 22% in 2005 compared with 2004.

According to research by Zurich-based Swiss Reinsurance Co., Latin America spent about 2.4% of its gross domestic product on insurance during 2006. In contrast, the worldwide insurance spending average was 7.6% of the collective GDP.

Total premiums in Latin America reached \$71 billion in 2006, up from \$59 billion the prior year, Swiss Re's "FIDES 2007 Economics Research & Consulting" report indicated.

Latin America has benefited from high commodity prices,

availability of external credit and improved debt management practices within the region, according to New York-based Standard & Poor's Corp.'s "Sovereign Risk Indicators" report for 2007.

GDP for the region grew about 5.5% in 2006 and was expected to grow 4.6% in 2007, New York-based S&P reported.

Along with economic growth, insurance regulators in several countries such as Mexico and Brazil are implementing new practices that will help align their markets globally, observers noted.

For example, some regulators have been tightening solvency requirements and moving toward transparency, Swiss Re said.

For Mexico, its insurance regulator, the Comisión Nacional de Seguros y Fianzas, said it is preparing a plan to adopt Solvency II, the proposed pan-European risk-based capital standard for insurers, according to a CNSF spokeswoman.

While Mexico would adopt Solvency II, it would take into consideration its own market peculiarities, the spokeswoman said. CNSF plans to begin working on the plan this year with the goal of completing it by 2012.

—By Roberto Cenicerros

Development boom in Latin America could benefit U.S. bond insurers

Despite U.S. economic trouble, insurers still see opportunity in region

By ROBERTO CENICERROS

Latin America's ongoing economic expansion and infrastructure development projects could provide a bright spot for U.S. financial guarantee insurers, although their credit troubles at home must first be settled, observers said.

The projects within Latin Ameri-

ca provide opportunities for local insurers, pension funds and U.S. investors looking for cross-border investments, said Diana Adams, managing director for emerging markets and structured insurance in New York for Ambac Financial Group Inc.

Monoline bond insurers, in turn, could benefit from insuring those

investments, observers said. However, bond insurers currently face major problems in the United States due to the subprime crisis, wherein potential claims from this could deplete their capital.

Ambac, for instance, lost its triple-A rating this month when

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Latin America: Insurance market expands

CONTINUED FROM PREVIOUS PAGE

compete worldwide, observers say.

Brazil and Mexico, though, are not the only Latin American nations where hopes are high for insurance industry expansion. Latin America in general has experienced growth: total premiums in 2006 was \$71 billion, up from \$59 billion the previous year, Swiss Reinsurance Co. research reported (see related story).

"The expectation is very big for all of Latin America, due to more stable economic environments, good GDP growth and investments in utilities and other industries," says Marcos Aurelio Couto, president and chief executive officer for ACE Seguradora S.A., a São Paulo, Brazil-based unit of ACE Ltd.

In January 2007, ACE purchased an insurance company in Peru and recently opened an office in Panama, Mr. Couto said. The insurer also operates in Mexico, Puerto Rico, Argentina, Chile, Colombia and Ecuador, he added.

Although economic growth is currently moderating in Brazil and Mexico, the long-term outlook for their economies and insurance markets remains optimistic, observers say.

"All (economic) scenarios are good for Brazil for the next few years," said Jose Felipe Vieira De Castro, president of Aon Risk Services do Brazil Corretores de Seguros, a unit of Aon Corp. in São Paulo. "It will be a really big opportunity for brokers to increase their (share of Brazil's expanding economic) pie."

Aon Risk Services and Aon Consulting practices in Brazil will grow about 18% in 2008 and place about \$842 million in premiums, Mr. Vieira De Castro estimates. About 23% of Aon's Brazilian business currently derives from placing the Brazilian portion of worldwide coverage for multinational corporations based elsewhere, Mr. Vieira De Castro said.

Together, Brazil and Mexico represent about 65% of Aon's Latin American business, Mr. Vieira De Castro said.

In Mexico, businesses have begun to use risk management strategies developed in countries such as the United States, where the insurance and financial services markets matured earlier, said Ricardo Solis,

chief executive officer for Willis Agente de Seguros y Fianzas S.A., a Mexico City-based unit of Willis Group Ltd.

Globalization and Mexico's increasing integration into the world economy are driving "a change in the buying behavior of clients," Mr. Solis said.

Mexico's multinational companies want sophisticated financial risk consulting services, structured insurance programs, global insurance products such as directors and officers liability and errors and omissions coverage, Mr. Solis said.

Just a few years ago, the demand for commercial insurance in Mexico was mostly limited to property coverage, he said.

The shift is pressuring Mexico's insurance workforce to adapt.

"We need to (redefine) the way

Globalization and Mexico's increasing integration into the world economy are driving 'a change in the buying behavior of clients.'

Ricardo Solis,
Willis Agente de Seguros y Finanzas S.A.

we work," Mr. Solis said. "There is limited experience in the local market, (but)...we will slowly but surely build up the experience that we will have in the local market to satisfy the global demand."

Similarly in Brazil, European and U.S. entities are purchasing shares of local companies, said Eduardo Lucena, chief executive for brokerage Colemont Brasil Corretores de Seguro Ltda., a unit of Dallas-based Colemont Insurance Group Inc.

Growing demand for D&O coverage is being spurred by multinational companies purchasing local Brazilian entities, more mergers and acquisitions and a surge in initial public offerings among Brazilian companies, Mr. Lucena said.

The arrival of D&O coverage provides an example of how globalization is forcing Brazilian risk managers to increase their purchase

of more sophisticated risk financing arrangements, said Andres Ricardo Holownia, regional risk manager in São Paulo for truck manufacturer, Scania Latin America Ltda. Mr. Holownia is also incoming president of the Brazilian risk management association, Associação Brasileira de Gerência de Riscos.

During the first nine months of 2007, net written premiums for all lines in Brazil increased 17.7% over the same period in 2006 to reach nearly \$27 billion, according to Brazil's superintendent of private insurance, Superintendencia de Seguros Privados.

Observers in Brazil say their country's insurance regulators are increasingly aware that if their country's corporations are going to compete on a global level, they need access to insurance products that will put them on equal footing.

So far, though, insurers in Brazil have been stifled from introducing many insurance products, which are available in other nations, because of a reinsurance monopoly held since 1939 by the reinsurer Instituto de Resseguros do Brasil S.A., said Henrique Abreu de Oliveira, senior vp for client markets for Swiss Re Brasil Serviços e Participações S/C Ltda., a São Paulo-based unit of Swiss Reinsurance Co.

In early 2007, however, Brazil's lawmakers ended the monopoly held by the partially state-owned reinsurer and opened the market to foreign competition.

Because of that, Brazil's insurance industry is especially poised for growth, observers say. But much still depends on whether new regulations encourage competition or maintain practices protecting local insurers, the observers add.

Currently, bank-owned insurers dominate insurance sales in Brazil, said Pedro Purn, president of Zurich Brasil Seguros S.A. in São Paulo, a unit of Zurich Financial Services Group.

But opening Brazil's reinsurance market could help change that. The shift, for example, would help put ACE "in a position to play on equal footing with local companies," Mr. Couto says.

Insurers would be able to bring more capacity and insurance products to Brazil and increase its penetration by taking advantage of more competitive treaty arrangements, Mr. Couto said.

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Questions & Answers

Eugenio Paschoal is chief executive officer for Latin America for London-based Willis Group Holdings Ltd. Based in São Paulo, Brazil, Mr. Paschoal was promoted to CEO of Latin America in November, after heading up Willis Brazil and serving as a member of Willis' Latin America management team for the past 10 years. Recently, he spoke with Business Insurance Senior Editor Roberto Cenicerros about the growing importance of Latin America.



Latin America maturing

Q: Why is Latin America of growing importance to you and other global brokers and commercial insurers?

Latin America's economy is flourishing and creating tremendous opportunities for growth in various economic segments. For many years, Latin America has been (known) for high inflation rates and government instability. What we can see now is a much more mature economy, very much open to the global environment with very clear long-term objectives that are duly supported by private industry. We are very much dependent on foreign investments. But given the strength of the economy over the past few years, we (also) have very strong local business emerging in Latin America.

Q: Are there any particular industries that the global investors are focused on?

Global investors generally look into big, big business, basically infrastructure projects that have a lot of construction business. Among infrastructure projects you have energy (development).

Q: Is that business going to create opportunity for commercial insurers to provide coverage in the future?

Yes. This generates a lot of opportunity not only for the big (infrastructure) projects, but also for all the surrounding industries and suppliers for these big projects. That means commercial insurance foresees really big opportunity in the region.

Q: We hear a lot about growth in Mexico and Brazil—Latin America's largest economies. What about other South or Central American countries? Are their insurance markets also expected to continue growing?

Yes. Brazil and Mexico are the main markets in the region. But if you look at the other countries, we also have tremendous opportunities and the growth rate is also very impressive. We have seen very nice growth rates in Argentina, Chile, Peru and Colombia, for instance. Of course, we have a (political issue) in Venezuela, but there are still a lot of opportunities there.

Q: We hear insurance markets are modernizing in Latin America. What are some of the insurance products and services in demand there today?

The biggest demand we see today is for employee benefits and (personal lines) affinity business. Affinity business is becoming a very attractive market because the strength of the economy is generating major buying power for the lower classes that would not have accessed insurance before. This is a breakthrough market responsible for fantastic growth opportunities.

Q: Why are Latin America's middle-market companies becoming more attractive for commercial brokers and insurers?

It's a brand new source of revenue for us because we have always focused on large business. The middle market, until today, has been dominated by independent and small brokers. But the middle market is becoming more sophisticated when buying products. Small companies and middle-market companies are looking for professional broker advice that fits well with our search for opportunity to grow and meet their needs.

Q: How much of Willis' revenue flows from Latin America?

Latin America represents about 18% of Willis total international revenues for 2006, meaning somewhere around \$150 million.

Q: Do you have any concerns that Latin America's history of boom-and-bust economic cycles will once again tarnish enthusiasm for the region's insurance appetite?

The region has emerged strong enough to face crises. What we see today is a completely different environment in terms of the economy from what we have seen in the past. As an example, there is now fear of global recession. But I'm very sure that Latin America can hold its economic position because we have created a very strong internal market although we are also dependent on foreign investment. Because of this, I believe there is much more stability today than we had in the past.

Guarantee: Opportunity for insurers

CONTINUED FROM PAGE 10

New York-based Fitch Ratings downgraded the company to AA. Additionally, last week Ambac posted a \$3.3 billion loss for fourth-quarter 2007 after recording massive credit derivative write-downs.

Economic difficulties in the United States, however, are not likely to slow development in Latin America's major economies because its governments and international monetary institutions, such as the World Bank, are financing a substantial portion of infrastructure development, said Alfredo Coutino, senior economist for Latin America in Westchester, Pa., for Moody's Economy.com, a unit of Moody's Corp.

Worldwide economic expansion and demand for Latin America's commodities have driven the region's growth during the past few years, observers say.

Global investors have also been particularly interested in Brazil, Chile and Mexico because their economies have experienced gross domestic product growth of about 5% annually over the past four years, Mr. Coutino added.

Additionally, their governments are adopting practices aimed at smoothing the steep historical boom/bust cycles that the developing region has historically experienced, Mr. Coutino added.

To do that, Brazil and Mexico, for example, are investing huge sums in infrastructure spending to help reduce any negative economic occurrence should global demand for the countries' commodities moderate, Mr. Coutino said.

Mexico is planning to increase its investment in public projects by 45% in real terms over the next six years, "which is a huge amount of money," Mr. Coutino said. The money to finance the projects has come from the countries' oil revenues and fiscal reforms.

Brazil's government has said it will spend about \$250 billion during the next four years, and Chile has been saving copper revenues to invest in infrastructure during an economic downturn, Mr. Coutino added.

That spending could create additional opportunities for financial guarantee insurers that assure investors will receive their principal and interest payments for such projects.

Latin America is "important because everyone expects growth to be higher outside of the United States than it is (inside), and the emerging markets are growing so quickly and they are improving so much," Ms. Adams said.

The growth potential is significant for bond insurers, yet Latin America still accounts only for small part of their business, several insurers added.

At the end of 2007, about 5% to 10% of XL Capital Assurance Inc.'s business flowed from Latin America, said Wynne Morriss, managing director and head of origination for XLCA in New York.

With the bond insurers now facing difficulties, however, credit markets are essentially frozen and the



Economic expansion and infrastructure development in Latin America, particularly Mexico and Brazil, present U.S. financial guarantee insurers with an opportunity, but potential claims from the subprime mortgage crisis could deplete their capital.

"situation currently is too fluid" to predict whether it will affect their appetite for Latin American business, Mr. Morriss said. "Give it a couple of months," he added.

But international infrastructure development still remains a growth

'Whenever there is a large amount of infrastructure development that is needed and there is a need for massive amounts of funds, that is a good environment for us.'

Wynne Morriss,
XL Capital Assurance Inc.

area for bond insurers, although they are facing a "temporary slowdown for the time being," said Rob Haines, an insurance analyst at CreditSights in New York.

Among Latin American countries, only Mexico and Chile so far have obtained at least a BBB- sovereign credit rating from rating agencies.

Bond insurers typically demand a BBB- credit rating at a minimum before they will provide coverage, which is to help raise bond ratings to the AAA level required by institutional investors.

Aside from Chile and Mexico, bond insurers expect Brazil to obtain investment-grade status within a year or so, several observers said. Additionally, Colombia, Panama and Peru all have longer-term potential, at least for some specific projects, observers said.

Less than a decade ago, Brazil was a debtor nation that worried investors because of its potential to default on loans, observers said. But worldwide commodity demand and fiscal discipline have helped change that.

"The prospects for our business in Brazil over the medium term are quite good for us and our competition," Mr. Morriss said. "Whenever there is a large amount of infrastructure development that is needed and there is a need for massive amounts of funds, that is a good environment for us."

Interest in Chile and Mexico, the only two Latin American countries that currently have an investment-grade credit status, is substantial, said Olivier Garnier, managing director of infrastructure finance for the Americas, for New York-based bond insurer Financial Security Assurance Inc. Among other positive attributes, both have strong capital markets, Mr. Garnier said.

FSA Seguros Mexico S.A. de C.V., a Mexico City unit of FSA Inc., last September became the first licensed financial guarantee insurer authorized to conduct business in Mexico, Mr. Garnier said.

The Mexican government's transportation agency, the Secretaria de Comunicaciones y Transportes, said that the country needs \$5 billion annually for road construction and maintenance.

Mexico's government currently wants private contractors to build and operate so-called "greenfield roads," which would be operated by private contractors with the government paying for their construction.

Mexico is also selling established toll road concessions to parties interested in operating the roads. Because the toll roads have operated for several years, their risk can be measured and that makes them attractive for bond insurers, sources said.

Mexico also needs ports, airports, housing and degasification plants that convert liquefied natural gas into an appropriate form to generate electricity, Ambac's Ms. Adams said.

In contrast, Chile's infrastructure development is winding down and has nearly run its course on road concession contracts, which required the participation of financial guarantee insurers to back hundreds of millions of dollars in bonds, several sources said.



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The project to expand the Panama Canal will cost an estimated \$5.25 billion. Construction companies bidding on the project must specify how they will mitigate the risks involved and include details of proposed insurance arrangements.

Panama Canal expansion creates insurance opportunities

Securing coverage for mega-project's extensive risks should be obtainable, risk managers say

By RODRIGO AMARAL

Some of the world's largest construction companies and their insurers are braced for a flurry of activity as the consortiums bidding on the project to expand the Panama Canal assess the risks involved in the project.

The cost to build a third set of locks, which will double the canal's cargo volume capacity, is estimated at \$5.25 billion. The new locks are expected to be in operation in 2014.

The Panama Canal Authority has reported that more than 60 companies from 18 countries have expressed interest in taking part. They include some of the largest construction companies in Europe, the United States and South America.

Four consortiums formed by a total of 30 multinational companies from 13 different countries applied last November for the project's largest contract, to build the canal's two new locks, each estimated to cost \$1 billion.

The Balboa, Panama-based Panama Canal Authority has specified a strict timetable of requirements that have to be carried out and there will be little time to evaluate all the risks before the presentation of bids for the main projects, risk managers say.

"It will be a huge job, for which we are hiring consultants in addition to our own technical people," said David González Pérez, the director of risk management at Madrid, Spain-based Sacyr Vallehermoso S.A., which leads one of the consortiums.

The bids must specify how the construction companies will mitigate the risks involved and include details of proposed insurance arrangements. Agustín Martín—the Madrid-based director of Allianz

Global Corporate and Specialty in Spain, part of Allianz S.E.—said that he expects that once contracts are awarded, insurance premiums to cover construction will run to tens of million of dollars.

São Paulo, Brazil-based construction company, Construções e Comércio Camargo Corrêa S.A., is one of the companies that have already started to carry out risk assessment activities. By mid-January, the firm and its nine partners—which include three other Brazilian companies and multinationals from France, Germany and the United States—have started to discuss a risk matrix, said César Gazoni, Camargo Corrêa's director of South American and Central American countries.

"From the technological side, this is a simple project, but it brings two main difficulties," he said. "First is its sheer magnitude, which makes what should be simple much less simple. Secondly, you have a logistical problem. And there may also be some geological risks there."

Coverage concerns

Construction companies have complained that it is very hard to find good policies to cover risks involved in large scale projects. The problem is particularly acute when such projects are located on the coast or in the sea. But Mr. González and Mr. Gazoni don't anticipate problems when they look for a common ground with insurers about the expansion of the canal.

"This is one of the most important projects to reach the market in the past few years," Mr. González said. "So I do not believe there will be many difficulties in reaching agreements with insurers. There are many interests involved in the expansion of the canal and the pro-

ject will be very much under the spotlight."

"I just hope that the magnitude of the risks involved will not be such that it will be impossible to insure them," Mr. Gazoni said. He said that Camargo Corrêa has other projects under way in the region, some of them facing difficult conditions, and the company did not face

'This is one of the most important projects to reach the market in the past few years. So I do not believe there will be many difficulties in reaching agreements with insurers.'

César Gazoni,
Construções e Comércio Camargo Corrêa S.A.

problems when it bought its insurance.

"In Colombia, we have a contract worth \$500 million to build a hydroelectric plant in a region (that) is difficult to access. There we even have army protection against guerrilla attacks," he said. "But even in this case, we were able to negotiate an all-risks policy. It required a good deal of negotiation, but it was possible."

The general expectation among the experts is that political risk of the Colombian sort is not likely to be a factor in Panama, which has been politically stable since the early 1990s. It also helps that the citizens of Panama approved the expansion of the canal in a referendum held in October 2006, experts say.

Panama is also considered to be outside the path usually taken by

hurricanes that hit parts of Central America and the Caribbean every summer. "But there is some exposure to the risk of earthquakes," Mr. Martín said.

Mr. Martín is sure that the insurance market will be able to provide coverage for the project. "We are able to study the details of each case and to offer conditions that meet the characteristics of the project, the experience of the contractor, etc.," he said.

What each consortium will need from insurers will be defined in the next few months. Mr. González said that much will depend on the requirements of the Panama Canal Authority itself.

"The subjective analysis by the companies of the risks involved is important, but so is an accurate interpretation of the demands the client makes concerning the purchase of insurance coverage," he said. "An erroneous reading of the insurance chapters of the tender document can have serious consequences for the bid."

"The kinds of coverage that will be required will depend, as a general rule, on what is demanded in each contract," Mr. Martín said. But he added that coverages will also be up to the risk appetite shown by each contractor.

All these things will have to be decided by Camargo Corrêa, Sacyr Vallehermoso and their partners by August, when bids to build the new locks must be presented.

"We need to act fast. We have only (about six months) to assess the risks, negotiate with the insurers

and at least sign some pre-contracts," Mr. Gazoni said.

He pointed out that the proposed locks will be of a size not found anywhere else in the world. "The consortium needs to study the engineering project, and then validate concepts. The next step is to take responsibility for the project, which is when we will look for a lot of insurance. And insurance for something like this is a very important cost, one that cannot be simply estimated. We need very reliable figures," Mr. Gazoni said.

And then there is the challenge of coordinating the work of all the companies involved in each consortium. "One of the major difficulties is in the huge number of parts involved in the project," Mr. González said.

Camargo Corrêa and its partners, for instance, have divided the tasks and will work from four bases—São Paulo, Paris, New York and Panama City. One of the challenges will be to harmonize the perception of risks that each company has about the project.

"Of course, the nature of the risks involved is always the same, but the perception of them varies. Some companies are more daring than others. We will have to sit together, evaluate our different perceptions and build a consensus," Mr. Gazoni said.

The formation of partnerships is itself a tool to reduce the risk of bidding for a mammoth project like the expansion of the canal. The (tender process) alone requires considerable spending, and the three consortiums whose proposals will be discarded will have to absorb that cost.

"The client will pay from some of the bidding costs, but it barely reaches 10% of our (tender) budget," Mr. Gazoni said.

Earning commissions not an issue for in-house captive broker

In-house brokers use 'insider edge' to identify multinational firm's risks

By **ROBERTO CENICEROS**

A multinational conglomerate focusing on engineering, construction, and petrochemicals maintains its own in-house insurance brokerage that transfers the company's worldwide risks without regard for earning commissions.

In-house, "captive brokers" used to be common a few decades ago at large corporations in Brazil, where Odebrecht S.A. is headquartered. But Brazil's captive broker system mostly faded away due to competitive forces, observers say.

Odebrecht Administradora e Corretora De Seguros Ltda., the insurance subsidiary of Odebrecht Group, survives today as a captive broker because of its insider knowledge, said Marcelo Neves, director of the brokerage unit referred to as OCS, founded in 1978.

The insider edge helps OCS brokers better understand which risks should be retained and which should be transferred for optimal protection of Odebrecht shareholder net worth and group assets, Mr. Neves said.

OCS brokers are paid a salary rather than commissions or fees,

'We know our operations better than a third party and we are willing to take time to understand the nuances on the operational side.'

Marcelo Neves,
Odebrecht Administradora
e Corretora De Seguros Ltda.

Mr. Neves said. Their earnings don't depend on bringing in new business, nor do they skew brokers' judgment when weighing risk retention versus risk transfer.

"The value we add to the group is in making sure we can identify the correct risks to transfer, and we are better positioned to identify (those than outside brokers) because we are within the company," Mr. Neves said.

"We know our operations better than a third party and we are willing to take time to understand the nuances on the operational side because our core mission is to transfer the correct risks; we are not looking at a bottom line approach," Mr. Neves said.

Systems not uncommon

Captive broker systems are not unusual worldwide, but it appears they are becoming less prevalent, said David Battman, director of strategy and international development in London for Gallagher

Global Risk, a unit of Arthur J. Gallagher & Co.

In Portugal, for instance, "there certainly have been a number of captive brokers...but less so than there used to be and I think that is pretty much the pattern" worldwide, Mr. Battman said.

Large conglomerates launched the captive broker system in Brazil about 30 years ago, said Antonio

INSURANCE AND BOND COVERAGE

At year-end 2006, Odebrecht Administradora e Corretora de Seguros obtained bonds totaling more \$2.15 billion and placed coverages for insured values exceeding \$18 billion for the following industries:

ENGINEERING & CONSTRUCTION:
Bonds and insurance **\$9.7 BILLION**

CHEMICAL & PETROCHEMICAL:
Bonds and insurance **\$10.7 BILLION**

Source: Annual report

Jorge Motta, chief executive officer for independent commercial broker LAZAM-MDS in São Paulo.

Insurance was so tightly regulated back then that every Brazilian insurer providing a quote had to offer the same price and terms, Mr. Motta said. So insurers differentiated themselves by continually raising the commission amount paid to brokers.

Commissions grew to exorbitant proportions, perhaps as much as 30% to 40%, Mr. Motta said. Large insurance buyers then formed captive brokers to capture the commissions.

But once insurance regulations relaxed to allow price competition, many of the buyers sold off their captive brokers, sources say. Some of those broker operations were acquired by the world's largest brokerages, which used them to launch their local operations.

Some other former captive brokers became independent brokerages and competitively place coverage for all accounts looking to purchase insurance, sources said. Many of them continue placing insurance for the companies that launched them.

LAZAM-MDS, for instance, still places coverage for a large pulp and paper conglomerate that initially created the broker during the mid-1970s, Mr. Motta said. Today about 3% of LAZAM-MDS' revenues currently come from that relationship.

Similarly, a Brazilian correspondent for Arthur J. Gallagher, Securitas Uniao Corretora de Seguros, earns a substantial portion of its revenue from the petrochemical conglomerate that launched it, Mr. Battman said.

In contrast, OCS' parent realized its core businesses—heavy construction and petrochemical production—are risk prone and require significant insurance purchasing and

risk management oversight, Mr. Neves said, so Odebrecht retained the captive brokerage that was closely aligned with its business needs.

Salvador, Brazil-based Odebrecht Group employs about 30,000 workers and its assets worldwide totaled nearly \$13 billion in 2006, when the company generated more than \$13 billion in gross revenues.

Its two largest units include Construtora Norberto Odebrecht S.A., an engineering and construction company that operates throughout Latin America, North America, Africa, Europe and the Middle East; and Braskem S.A., Latin America's largest petrochemical company providing products to more than 40 countries across Latin America, North America, Europe, Asia and Africa. It is traded on the New York stock exchange, Mr. Neves said.

The group also includes units that focus on sugar and ethanol production, power generation and management of public infrastructure projects.

OCS brokers place coverage with the world's major insurers, Mr. Neves said. Among other coverages, Odebrecht purchases property insurance for its petrochemical plants; surety protection for construction projects; all-risk engineering and construction insurance; marine policies for its equipment; and directors and officers liability for the publicly traded company.

OCS brokers also fill a risk management role and work closely with Odebrecht Group's safety engineers and construction managers to assure insurance and risk management best practices are transferred throughout the operating units, Mr. Neves said.

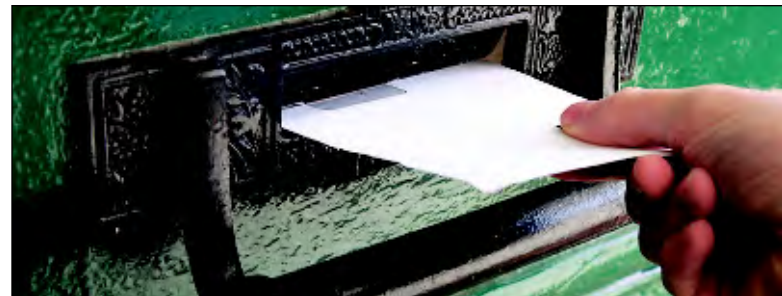
The brokers employ a risk matrix system to assess the risk of each operation, Mr. Neves said. They also rely on other tools such as annual risk engineering surveys to quantify exposures and help determine which risks should be transferred and which should be retained.

OCS brokers are licensed to purchase insurance products—the same as an independent broker—in many of the countries where Odebrecht Group operates, Mr. Neves said.

In countries where OCS brokers are not licensed, the company contracts with global brokers for insurance placement and risk management services, Mr. Neves added.

OCS offices include one in Miami, which handles risk management, insurance purchasing and the surety needs for its U.S. operations that is currently building new terminals for Miami International Airport, Mr. Neves said.

The OCS model could serve other Latin American companies that recognize the need to implement best practices for insurance purchasing and risk management, Mr. Neves said.



Insurers target potential clients by using direct mail campaigns.

Commercial insurers enter affinity market

Latin America's economic stability spurs business

By **ROBERTO CENICEROS**

Latin American commercial insurers and brokers are making a play for corporate customers' employees through "affinity" strategies.

Affinity business refers to personal lines coverage distributed mainly through two channels: Coverage is sold to individual employees through employers, sometimes as a supplement to group products; or coverage is sold through other inexpensive means, such as solicitations accompanying utility bills or credit card statements, to reach large groups of consumers.

In Brazil, for example, 70% of electric bills serve as a distribution channel for ACE Seguradora S.A. products, such as personal credit protection, accident coverage, automobile insurance and unemployment insurance, said Marcos Aurelio Couto, president and chief executive officer for the São Paulo, Brazil, unit of the ACE Ltd.

In November, ACE launched a group life insurance pilot program in Brazil and Mexico, which is aimed at employers, Mr. Couto said. ACE plans to expand the pilot program into other Latin American countries as well.

Purchasing power

Commercial brokers and insurers say personal lines and affinity strategies are one of the major drivers of insurance purchasing throughout Latin America. They are aggressively pursuing affinity business because the region's booming economic growth is creating millions of first-time insurance consumers, they said.

Countries such as Colombia and Brazil are benefiting from unprecedented foreign investment, said Thomaz C. Menezes, São Paulo-based regional leader for Latin America and the Caribbean for Marsh Inc.

Other Latin American countries are also experiencing stable economic growth and favorable exchange rates that have raised income levels. That, in turn, has provided more residents with the means to purchase insurance for new valuables worth protecting.

"In countries where the economy is stable, and there is a lower- to middle-class with increased purchasing power and a bigger conscience of 'I need to protect myself,' there is a huge opportunity for affinity on the consumer side of the insurance industry," Mr.

Menezes said.

Affinity business is one of Marsh's fastest growing areas and accounts for 22% of the broker's total revenue in Latin America, Mr. Menezes said. Marsh's Latin American affinity customer base has grown from fewer than 500,000 individuals to more than 5 million over the past five years.

The broker has about 600 people in Brazil to operate an affinity business "platform" that can help Marsh service customers in other countries, Mr. Menezes said. Additionally, Marsh recently launched a duplicate platform for a credit card

Affinity strategies are one of the major drivers of insurance purchasing throughout Latin America.

company client that will include a call center in Mexico.

"We are looking to do that in Colombia, and then we are going to look at other countries. But the key focus for us in the consumer affinity business is basically going to be Mexico, Colombia and Brazil and eventually Puerto Rico."

For São Paulo, Brazil-based commercial brokerage LAZAM-MDS, affinity business provides an opportunity to meet employer clients' total needs through two entry points, said Antonio Jorge Motta, CEO for the brokerage.

Affinity products, such as auto and homeowner insurance, are sold through a client's human resources department, along with life and health products for employees whose dependents are not covered under their employer group plans.

While LAZAM-MDS provides affinity products, it also places commercial property/casualty insurance for its clients, Mr. Motta said.

P/C insurers looked to affinity business to compete with banks, which dominate insurance sales in some Latin American countries, said Pedro Purm, São Paulo-based president of Zurich Brasil Seguros S.A., a unit of Zurich Financial Services Group.

Mr. Purm also said he expects to see more P/C insurers follow ACE's example and enter the life business, also as a means to compete with banks for insurance customers.

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Market Moves

UnitedHealthcare finalizes Fiserv health-related buy

BROOKFIELD, Wis.—UnitedHealth Group Inc.'s UnitedHealthcare has completed the acquisition of most of the health care-related business of Brookfield, Wis.-based Fiserv Inc., the companies said.

The \$775 million purchase, announced last year and completed earlier this month, includes Fiserv's third-party administrator for self-funded health plans as well as its specialty solutions and plan management outsourcing units. Minnetonka, Minn.-based UnitedHealthcare's purchase also includes prescription benefits administrator Innoviant Inc., prescription mail-

order service Innoviant Pharmacy and care management company Avidyn Health, the companies said in a statement.

How the purchased operations would be branded had not yet been decided, a UnitedHealth Group spokesman said.

When the deal was announced, Fiserv said it would keep its workers compensation services organization that includes WorkingRx and its CareGain Inc. technology business.

Australia's QBE to buy P/C insurer

SOUTHFIELD, Mich.—Property/casualty insurer North Pointe Holdings Corp. has agreed to be acquired by New York-based QBE Holdings Inc. for about \$146 million in cash, the companies said.

Southfield, Mich.-based North Pointe said its board approved the acquisition by the U.S. arm of QBE Insurance Group Ltd. of Sydney, Australia. North Pointe also said the deal was subject to regulatory

approval and expected to close during the first half of the year.

Frank O'Halloran, QBE Group's chief executive officer, said the purchase will "enable us to achieve further synergies with our existing business. Subject to unforeseen circumstances, we anticipate a combined operating ratio in the low 90s in 2009."

Beecher Carlson buys Southwest agency

PHOENIX—Beecher Carlson Holdings Inc. has expanded its presence in the Southwest with the purchase of Alliance Insurance Group.

The Atlanta-based brokerage did not disclose details of the acquisition of the Phoenix-based agency, which will retain its name and location, Beecher Carlson said in a statement.

Alliance Insurance Group President and Chief Operating Officer Frank Beranek will remain with the agency in those roles, while Chairman and co-founder Guy Labelle

will be a consultant until retirement at an unspecified date, a spokeswoman for Beecher Carlson said.

HRH expands Baltimore presence

BALTIMORE—Hilb Rogal & Hobbs Co. has completed the acquisition of Baltimore-based employee benefits brokerage and consulting firm Integrated Group Benefits, HRH said.

HRH, which did not disclose transaction details, said in a statement that IGB would merge into HRH's existing Baltimore office under the leadership of Steven Deal, vp and mid-Atlantic regional director.

Swiss Re merges former GE units

JEFFERSON CITY, Mo.—Swiss Reinsurance Co. has merged two insurance operations it gained as part of the 2006 acquisition of GE Insurance Solutions.

Employers Reinsurance Corp. has been merged into Westport Insurance Corp. U.S. and Canadian clients previously served by Employers Reinsurance now will be served by Jefferson City, Mo.-based Westport, Swiss Re said.

TO SUBMIT ITEMS

BI's new Market Moves column reports on activities by insurance industry companies and related entities. Personnel changes appear in Comings & Goings, while new product offerings appear in Products & Services. Please send Market Moves news to: Charmain Benton, *Business Insurance*, 360 N. Michigan Ave., Chicago, Ill. 60601-3806; cbenton@businessinsurance.com.

Items for the Products & Services and the Comings & Goings reports should be e-mailed to Joe Walker at jwalker@businessinsurance.com.

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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK
IN RE PETITION OF JOHN C. GIBBONS,
AS LIQUIDATOR OF NEW CAP
REINSURANCE CORPORATION LIMITED,
DEBTOR IN FOREIGN PROCEEDINGS
CASE NO. 99-B-42752 (SMB)

NOTICE IS HEREBY GIVEN THAT ON JANUARY 15, 2008, THE BANKRUPTCY COURT ENTERED AN ORDER (THE "ORDER") CONTINUING THE PRELIMINARY INJUNCTION ORDER PURSUANT TO 11 U.S.C. §304 ORIGINALLY ENTERED IN THIS CASE ON MAY 7, 1999. THE ORDER SHALL REMAIN IN EFFECT PENDING A HEARING SCHEDULED TO BE HELD ON JULY 15, 2008 AT 10:00 A.M. (THE "RETURN DATE") BEFORE THE HONORABLE STUART M. BERNSTEIN, UNITED STATES BANKRUPTCY JUDGE, IN THE UNITED STATES BANKRUPTCY COURT LOCATED AT ONE BOWLING GREEN, NEW YORK, NEW YORK. ALL PAPERS SUBMITTED FOR THE PURPOSE OF OPPOSING CONTINUATION OF THE ORDER AFTER THE RETURN DATE SHALL BE FILED WITH THE COURT, WITH A COPY TO THE CHAMBERS OF THE HONORABLE STUART M. BERNSTEIN AND SERVED ON COUNSEL FOR THE PETITIONER LISTED BELOW, SO AS TO BE RECEIVED AT LEAST FOURTEEN (14) DAYS PRIOR TO THE RETURN DATE. ANY PERSON WISHING TO OBTAIN A COPY OF THE ORDER SHOULD CONTACT COUNSEL TO THE PETITIONER.

CHADBOURNE & PARKE LLP
ATTORNEYS FOR THE PETITIONER
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LEGAL NOTICE

IN THE SUPREME COURT OF BERMUDA
CIVIL JURISDICTION
IN THE MATTER OF LASALLE RE LIMITED
AND IN THE MATTER OF
THE COMPANIES ACT 1981, SECTION 99
NOTICE OF COMPLETION OF
SCHEME OF ARRANGEMENT

Notice is hereby given that the Scheme of Arrangement between LaSalle Re Limited and its insurance creditors which became effective on 2 May 2007 (the "Scheme") has been completed in accordance with its terms as of 22 January 2008. All Scheme Liabilities have been finally determined and all Payable Scheme Claims have been paid in full in accordance with the terms of the Scheme and no further payments shall be made by the Company in respect of Scheme Claims.

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International NEWS

Quake models analyzed

Forecast tools aim to better predict occurrences

By **GLORIA GONZALEZ**

Experts are developing forecast models for earthquake risks in Asia, Europe and the United States that they hope will better predict the occurrence of quakes.

A model used by forecasters in Japan, for example, estimated that the greater Tokyo region has about



In 1994, a magnitude 6.7 earthquake occurred in Northridge, Calif.

a 30% chance of experiencing severe shaking in the next 30 years, said Shinji Toda, a scientist with the Active Fault Research Center of the National Institute of Advanced Industrial Science and Technology in Tsukuba, Japan.

The area has already experienced several earthquakes above 7.0 magnitude, including the 7.8 magnitude Kanto earthquake in 1923 that

devastated Tokyo and killed more than 100,000 people, he told attendees of Risk Management Solutions Inc.'s 2008 symposium on "Advances in Earthquake Forecasting" in New York last week.

When analyzing earthquake risk in Tokyo, the modelers ran different scenarios to determine the probabilities of a quake. One scenario modeled an earthquake with a magnitude equal to or greater than the 7.3 Ansei-Edo quake of 1855. The model determined that there was a 20% chance of a quake that size occurring within 50 kilometers of Tokyo in an average 30-year period and a greater than 35% chance of such a quake over the next 30 years. By contrast, the models determined that the probabilities of an earthquake equal to or greater than 7.9 magnitude—the size of the 1923 Taisho earthquake—occurring within 100 kilometers of Tokyo are 11% for the average 30-year period and 0.5% for the next 30 years.

Due to the high population—Tokyo is home to about 10% of the country's 127 million people—and economic concentration of Tokyo, an earthquake above 7.0 magnitude would be devastating, Mr. Toda said. "That's the problem," he said.

He cited a report by the Central Disaster Council of Japan that projected that a 7.3 magnitude earth-

See **QUAKE** next page

Berkshire buys stake in Swiss Re

Arrangement seen as a 'defensive move' for added financial flexibility

By **JUDY GREENWALD**
and **MICHAEL BRADFORD**

ZURICH, Switzerland—Berkshire Hathaway Inc.'s move last week to assume a 20% share of Swiss Reinsurance Co.'s property/casualty business under a proportional reinsurance contract and to take a 3% stake in the Swiss reinsurance giant makes sense for both companies, observers say.

The quota share reinsurance arrangement with Omaha, Neb.-based Berkshire Hathaway, which took effect Jan. 1, lets Swiss Re reduce the capital it holds for property/casualty business, the Swiss reinsurer said in a statement. Berkshire will assume a 20% share of all Swiss Re's property/casualty business for the next five years, the statement said. Swiss Re also intends to acquire up to 1.75 billion Swiss francs (\$1.6 billion) of its own shares over the next 24 months as it realizes capital relief from the quota share arrangement. The repurchase is in addition to the reinsurer's previously announced share buyback and Swiss Re now plans a total buyback, including shares already repurchased, of up to 7.75 billion Swiss francs (\$7.08 billion).

"This reinsurance arrangement is further evidence of our commitment to actively manage the (property/casualty) cycle in the best interest of our shareholders," said Swiss Re Chief Executive Officer Jacques Aigrain, in the statement. "The additional capital efficiency, as well as the downside protection, will permit Swiss Re to retain flexibility in a softening property and casualty market. The arrangement also underlines the strength of our underwriting capabilities. It will allow us to increase capacity rapidly

should pricing conditions improve. Furthermore, it will advance our efforts to manage earnings volatility—a key strategic objective," he added.

Berkshire Hathaway acquired the Swiss Re shares on the open market and is holding them through its Columbia Insurance Co. subsidiary.

Observers say the quota share deal benefits both Swiss Re and Berkshire.

"I see this as a defensive move" that was motivated by Swiss Re's desire for downside protection "and the added financial flexibility that the transaction affords them," said John L. Ward, chief executive officer of

Cincinnati-based Cincinnati Partners L.L.C., an advisory firm that specializes in the insurance industry. He noted that future write-downs are anticipated as a result of the reinsurer's subprime and bond investments.

In November, Swiss Re reported a 1.2 billion Swiss franc (\$1.07 billion) market-to-market loss, or 981 million Swiss francs (\$879.9 million) after tax, arising from its exposure to two related credit default swaps written by its Credit Solutions unit that provide protection for a client against a fall in the value of a portfolio of assets.

"On the positive side (Swiss Re



'The additional capital efficiency, as well as the downside protection, will permit Swiss Re to retain flexibility in a softening property and casualty market.'

Jacques Aigrain,
Swiss Reinsurance Co.

has) got some additional risk sharing on their balance sheet" with the deal and so is reducing its exposure, said Mark Rouck, senior director with Fitch Ratings Ltd. in Chicago. On the negative side, its share repurchase is "taking capital out of the organization."

Mark Lane, an analyst with William Blair & Co. in Chicago, said, however, from Swiss Re's perspective, using the capital to buy back stock seems to be part of "a broader effort to manage capital more aggressively."

He noted that "it is a little surprising that Berkshire Hathaway would make a commitment to the

P/C business at this cyclical point," with prices and returns likely to be under pressure for the next few years.

Bruce Ballentine, an analyst with Moody's Investors Service in New York, said, "for Berkshire, it's a large, commercially attractive transaction, and perhaps large enough that not a lot of other companies could offer such coverage."

Damien Magarelli, a director at New York-based Standard & Poor's Corp., said the quota share agreement obviously "gives Berkshire access to Swiss Re's market breadth

See **SWISS RE** page 19

French banking group insured against employee fraud

By **ADRIAN LADBURY**

PARIS—Société Générale S.A., France's second-largest publicly traded banking group, has insurance coverage that may respond to the €4.9 billion (\$7.08 billion) fraud that that was carried out by an employee.

Michel Yarhi, risk manager with Société Générale and immediate past president of the Assn. pour le Management des Risques et des Assurances de l'Entreprise, con-

firmed that the company does have insurance but declined to provide details on the coverage or where it was underwritten.

One London market source who is involved with the financial institutions insurance market said that it is likely that the bank would have no more than €200 million (\$288.8 million) in coverage for fraud, much of which would be placed in the French market. The source explained that the market for such risks is limited, with only about

€669 million (\$966.0 million) in coverage available worldwide.

Speaking at the 16th annual AMRAE conference in Deauville last week, Mr. Yarhi confirmed that the fraud coverage would be far from adequate to cover the almost €4.9 billion loss.

Last week, Société Générale announced that it had been hit by a fraud carried out by a single trader. The bank said that a trader, who was responsible for futures hedging on European equity market indices,

had taken "massive fraudulent directional positions" in 2007 and 2008 beyond his "limited authority."

Société Générale noted that the trader was assisted by an "in-depth knowledge" of the bank's control procedures that he gained when he formerly worked in its middle office. This enabled him to conceal his positions through a "scheme of elaborate fictitious transactions," said the bank.

The bank also announced fresh

write downs of €2.05 billion (\$2.96 billion) for the fourth quarter of last year for exposures related to the U.S. subprime crisis and that it would need to raise €5.5 billion (\$7.94 billion) in fresh capital as a result.

Mr. Yarhi said he believes that the €4.9 billion fraud loss could spur a new effort among risk managers in the sector to seek out a solution to their capacity shortages, possibly through some form of alternative risk transfer.

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Commentary

Legal stories that fell through the cracks

Comedian Lewis Black occasionally does a bit on the "The Daily Show with Jon Stewart" called "Back in Black." In the segment, he riffs on stories that might otherwise have slipped through the cracks, generally working up a bit of righteous ire along the way.

I am under no illusions that I am anywhere near as clever as Mr. Black. Nevertheless, a trio of stories, all involving the legal system, caught my attention in recent weeks. None of them led me to work the kind of anger Lewis Black experiences, but rather left me both amused and bemused.

All of the stories involve trademarks or copyrights, the legal system and—no doubt purely by coincidence—Minnesota in one way or another.

STORY NO. 1 involves a legal dispute between Fraser, Colo., and International Falls, Minn.

It seems both towns claim to own the trademark "Ice Box of the Nation." According to the Associated Press, they're suing each other over ownership of the slogan, which each claims to have used for at least half a century.

International Falls won an earlier round in this battle in 1986 by paying \$2,000 to its Colorado counterpart in exchange for Fraser dropping its claim to the name. But International Falls failed to renew its federal trademark, thus opening the door to further action by Fraser.

No doubt both are lovely places to live and raise a family. But the right to call oneself the "Ice Box of the Nation" doesn't strike me as something worth a protracted legal battle unless a town really wants to make itself attractive to frostbite fetishists.

STORY NO. 2 takes us to Duluth, Minn. It seems the federal government believes that a nearly \$222,000 damage award levied against a woman who illegally shared copyrighted music files on the Kazaa file-sharing system meets constitutional standards. Given that a Duluth court found that defendant Jammie Thomas had illegally shared 24 songs, that award boils down to better than \$9,000 per song.

I don't know exactly what Ms. Thomas downloaded. But as far as I am concerned, even a hitherto unknown Beatles album—no more of which could ever be recorded—wouldn't draw \$9,000 a song from even the most diehard fan. In fact, according to published reports, Ms. Thomas and her lawyer argued that downloading the 24 songs would have cost all of \$23.76 on iTunes. Like I said, I don't know what



MARK A. HOFMANN

Senior Editor Mark A. Hofmann can be reached at: mhofmann@businessinsurance.com

Ms. Thomas shared, but paying even that much for the work of Britney Spears or Clay Aiken strikes me personally as excessive.

STORY NO. 3 is something even the most ardent tort reformer couldn't make up. Once upon a time not that long ago—a year or so ago to be exact—there was an organization called the Assn. of

The mere spectacle of trial lawyers suing trial lawyers over the right to an acronym guarantees it will be one of the most amusing cases.

Trial Lawyers of America. The group decided to change its name to the American Assn. for Justice—or AAJ. This is not be confused with the American Justice Partnership—or AJP—which is a tort reform group.

It came to pass that a group of trial lawyers decided to form an organization called the American Trial Lawyers Assn., which goes by TheATLA. AAJ, formerly ATLA, was not amused and—guess what?—sued the TheATLA in a Minnesota court for trademark infringement.

And it gets better. According to the Washington Post, the American College of Trial Lawyers has also filed suit against TheATLA, claiming TheATLA's name is too close to its own.

At last check, the new ATLA was still calling itself TheATLA, and the old ATLA didn't respond to an e-mail requesting information on the suit's status. While it may not end up being the trial of the century in terms of legal precedent, the mere spectacle of trial lawyers suing trial lawyers over the right to an acronym almost guarantees it will be one of the most amusing.

Quake: Forecast models in the works

CONTINUED FROM PREVIOUS PAGE

quake in Tokyo Bay would cause an estimated \$1 trillion in losses, only 5% of which would be insured, he said.

Italy has also experienced earthquakes slightly above a magnitude 7.0, but even small to moderate earthquakes can cause serious damage due to the presence of many historical buildings, making the country highly vulnerable to earthquakes, said Warner Marzocchi, a geophysicist with the Institute of Geophysics and Volcanology in Rome, Italy. The Institute is testing

different forecasting models to better predict seismic activity, he said.

Additionally, earthquake forecasters are finalizing a report on California quake risk that found the South San Andreas fault to be "the most dangerous fault" in the state with a 59% probability of experiencing a 6.7 earthquake in a 30-year time period, said Tom Parsons, a geophysicist with the U.S. Geological Survey in Menlo Park, Calif. The second most dangerous faults in California are the San Jacinto fault and Hayward faults, which have a 31% probability of experiencing a 6.7 magnitude quake, he said. The

1994 Northridge earthquake that caused an estimated \$12.5 billion in insured losses was a 6.7 magnitude quake.

The California Earthquake Authority, a Sacramento, Calif.-based entity that offers residential earthquake insurance to California homeowners, is tasked to use the most informative science available to give the most accurate rates across the state, but faced challenges because of varying models, he said. Now the agency will have a uniform methodology and study to use in evaluating quake risk and setting rates, he said.

Stoneridge: Ruling raises disclosure issues

CONTINUED FROM PAGE 3

duty to say something" to warn investors, Mr. Washington said.

Mr. Washington said that scenario is not likely, but he noted there is limited, though tangential, case law on the issue. For example, one case establishes potential liability for a securities analyst that reports on a company that has issued misleading financial statements, if company officials and the analyst worked together closely on the analyst's report.

The issue of when and how business partners should try to avoid liability by disclosing a questionable transaction with another company when those partners have no duty to issue public statements will present difficult internal questions for third parties, said Steve Shappell, managing director of the legal and claims practice for Aon Financial Services Group in Denver.

A late disclosure or none at all could create "a real risk" of third-party liability, Mr. Shappell said.

But, he said, the risk of coming forward is that "if I'm a plaintiffs attorney, I'm framing my claim around that transaction," and the public statement puts the third party in the middle of the deal.

The language of the disclosure

would be important, but "you're probably getting into uncharted territory there," said Ms. Hart, the plaintiffs attorney.

Insurer attorney Richard J. Bortnick, a partner with Cozen O'Connor P.C. in Philadelphia, said he expects that third parties in most circumstances will not come forward, because they will conclude that another company's investors did not rely on their activities.

In addition, he said: "If those companies are viewed as a public policeman, they could lose credibility with business partners, which wouldn't want to do business with them."

Another option is self-reporting to the Securities and Exchange Commission, which can hold third parties accountable even when another company's investors cannot, legal experts suggested.

"It prevents the SEC from coming down and crushing you," said Mr. Shappell, adding that a simultaneous public disclosure also may be necessary.

Inviting an SEC probe with such a disclosure could hurt a company's share price in the short term, "but it's hard to imagine why it's not better in the long run," said policyholder attorney William G. Passannante, a partner with Anderson, Kill

& Olick P.C. in New York.

Other third parties—such as lawyers, accountants, joint venture partners and public relations firms—that speak on behalf of another company and may have more direct input in that company's financial statements may be legally obliged to disclose problems they detect, so their liability risk is greater, experts agreed.

Indeed, a court could invoke a legal doctrine—the rebuttable presumption of reliance—that allows it to presume investors relied on those third parties' actions unless the defendants can prove otherwise, Mr. Passannante said.

While Mr. Bortnick agreed that attorneys and accountants face a greater risk of third-party liability, he does not expect them to come forward or fire clients except "in the most egregious circumstances."

Otherwise, "who would want to be their clients?" he asked.

But insurer and defense attorney Dan A. Bailey said the notion of third parties stepping forward and somehow disclosing another company's wrongdoing transcends the *Stoneridge* decision. "You probably should do something about it with or without *Stoneridge*," said Mr. Bailey, a partner at Bailey Cavalieri L.L.C. of Columbus, Ohio.

Ruling won't have big impact on D&O market

The U.S. Supreme Court's ruling earlier this month on third-party liability in securities fraud litigation is somewhat of a relief to the directors and officers insurance market, market experts said.

Many Side C, or corporate entity, provisions in D&O policies do not cover securities claims from another company's investors, they say. And neither Side A nor Side B of a D&O policy would respond to those claims, because those provisions cover directors, who are not the target of third-party securities fraud lawsuits.

But the Side C components of some policies do cover that risk,

the experts say.

"D&O policies are all over the map on how they define securities coverage," noted Damian Brew, national claims advisory practice leader for the FINPRO unit of New York-based Marsh Inc.

Insurer executive Carl Pursiano said underwriters "have to be wary" of third-parties' participation in securities fraud.

But, "that's nothing new, per se," said Mr. Pursiano, a New York-based senior vp with Liberty International Underwriters, a unit of Liberty Mutual Group Inc. He noted that while the *Stoneridge* decision did not eliminate those insurance buyers'

potential liability, it also did not increase their potential liability.

The issue "has been on the back of our minds the last couple years," he said. But, he predicted that the ruling will not trigger additional lawsuits against third parties.

As a result, the Supreme Court's decision likely "won't change the underwriting practices" of insurers, he said.

In the errors and omissions market, underwriters largely exclude securities claims, Mr. Brew said. Investment banks can buy the coverage, but most do not because of its hefty price tag, he said.

—By Dave Lenckus

Limits: Buyers overall not increasing coverage

CONTINUED FROM PAGE 3

paste, and the ensuing product recalls is a good example, he noted.

"That, to me, brings to mind other areas of concern that maybe people hadn't thought of in the past as additional exposures," he said. And it's not just in China, it could be the case of supply chains anywhere around the world. It may not be a company's direct product, but if it becomes a component part of that company's product, it could be subject to liability suits, he said.

Marsh's report tracks various jury verdict awards and other loss trends, including product recall exposures.

Not surprisingly, companies that have experienced sizable casualty losses purchase more limits, the survey found.

The U.S. companies that experienced a \$5 million or greater loss within the past five years purchased liability coverage limits averaging

\$203 million in 2007 compared with the average \$58 million in limits purchased by companies that had not experienced such a loss.

Among other findings from the survey:

- Globally, the highest average limits in 2007 were purchased in the United Kingdom at \$93 million, followed by Denmark at \$73 million and the United States at \$66 million. Countries with the lowest average limits were Malaysia at \$1 million, Poland at \$2 million and Venezuela at \$3 million.

- The highest average prices per \$1 million of coverage were found in Korea at \$25,347, France at \$16,537 and Spain at \$14,409. Australia had the lowest prices, averaging \$1,426 per \$1 million of coverage, followed by New Zealand at \$1,709 and Venezuela at \$1,901.

Copies of the report, "Limits of Liability 2007," are available at no charge by calling Donna Mohan at 212-345-5343.

CDHP: Account-based plans aiding worker health

CONTINUED FROM PAGE 4

He added that such measurements were important because the primary reason most employers implement such plans is to change employees' attitudes and behaviors regarding their use of health care services.

For example, employers offering account-based health plans were more likely to report positive developments in health care utilization and health status than those offering traditional health plans.

Specifically, 72% of employers with account-based health plans said their plans were encouraging better use of health care, compared

with just 47% of employers offering traditional plans.

About the same percentage of employers offering account-based health plans, 71%, also said their plans supported their employees' good health, compared with 54% of employers offering traditional health plans. Moreover, 65% of employers said their account-based health plans were changing employee behaviors that have an impact on costs, compared with 45% of employers offering traditional plans.

To view the complete survey report, visit www.towersperrin.com/tp/getwebcachedoc?webc=HRS/USA/2008/200801/ABHP.pdf.

Swiss Re: Berkshire takes stake in global reinsurer

CONTINUED FROM PAGE 17

and scope, and more specifically their distribution and access to clients and accounts." He noted that the deal has not affected Berkshire's AAA rating.

Berkshire's investment in Swiss Re "has already paid off, because the announcement and the market reaction was very positive," creating "an immediate positive bounce that benefited all shareholders, but particularly Berkshire," Mr. Ward said.

"I would expect the stake to increase, but to always stay in a very small minority position, and I don't see this as an initial step towards a full acquisition," Mr. Ward said. "I see it as Berkshire Hathaway being opportunistic given the current market conditions and their mov-

ing quickly to take advantage of a very good value opportunity."

"Financial stocks have been beaten up, and while Swiss Re's not a household name, within the insurance industry, it is a premier name, so their investment is consistent with Berkshire's strategy overall," Mr. Lane said.

Steve McElhiney, president of reinsurance intermediary EWI Inc. in Dallas, said the deal is "a bit surprising, given Berkshire's involvement" with General Re Corp. and the fact that Swiss Re and Gen Re are competitors.

"I see it more as financial play for Berkshire as opposed to a real, strategic realignment.... We don't see any changes whatsoever...in how we interact with Swiss Re" as a result of this deal, he said.



John J. Hampton is the KPMG Professor of Business and Dean of the School of Professional and Continuing Studies and Graduate Business Programs at St. Peter's College in New Jersey. He specializes in business ethics, legal liability and enterprise risk management. He is a former executive director of RIMS. To read Mr. Hampton's columns and interviews, visit www.BusinessInsurance.com/ERM.

The author thanks John Farrell, National ERM Lead Partner at KPMG, for contributions to development of this article.

Emerging Risk STRATEGIES

Governance a start for ERM

By John J. Hampton

Governance is a good starting point for enterprise risk management. In this column on Emerging Risk Strategies, we'll explore the drivers of ERM and offer a good example of how an ERM approach could help Chrysler Corp.

Executives are increasingly talking about the need to improve risk management across the entire organization. They are responding to multiple drivers, including:

- **Regulatory requirements.** ERM has been discovered by regulators. The Securities and Exchange Commission requires public companies to file 10-K reports that discuss risk factors in plain English. Basel II requires banks to demonstrate adequate capital to handle the risks they accept. Securities exchanges have implemented tighter listing requirements with respect to risk reporting.

- **Funding requirements.** ERM affects the raising of debt and equity capital. The New York Stock Exchange requires listed companies' audit committees to discuss risk assessment and risk management. Rating agencies are introducing requirements for an ERM program before a company can achieve a favorable rating on debt issues.

- **Transparency and accountability.** ERM is becoming a component of improving management processes. The Sarbanes-Oxley Act requires the chief executive officer and chief financial officer of public companies to sign off on the adequacy of internal controls and reliability of financials. Failure to implement effective risk management processes can lead to criminal penalties.

- **Competitive pressures.** ERM is improving the risk profile of organizations as they operate in more complex and rapidly changing environments. The first company to identify risk trends and respond to them may be the most successful in a market.

- **Performance.** It is one thing to have a strategy; it is another to execute it in a risky world. ERM is a tool that increases the likelihood of a high level of performance.

Where to start?

ERM can begin anywhere, but three approaches seem to be emerging:

- **Governance.** The board, CEO and CFO are at risk, and they place the entity at risk when they fail to understand critical risks. They can start the ERM process.

- **Strategy.** C-level management believes it understands critical risks. How should the leadership assess them, identify options to deal with them, select a strategy and monitor its effectiveness?

- **Performance.** The organization needs processes to achieve profit and other goals, reduce cash flow volatility, control costs, comply with policies and otherwise improve the efficiency of operations. ERM can provide a framework to improve performance.

An organization can develop a successful ERM program from any of these points. In this article, let's deal with governance.

A director, CEO or other C-suite executive can raise the need for ERM. Board members

and senior executives are likely to display immediate skepticism: "We are doing just fine." "We have been in business a long time." "We know what we are doing." These are typical responses.

Fortunately, a simple test exists to see if ERM is needed. A consultant or facilitator simply has to ask, "What are your seven to 10 most critical risks?" In many boardrooms, the question has produced an uncomfortable silence followed by a vigorous and maybe even rancorous discussion. Then boards realize more needs to be done to understand risk across the enterprise.

The first obstacle confronting executive leadership is risk identification and developing agreement on critical risks. A specific example can illustrate the scope of the problem.

Chrysler's critical risks

In September 2007, five teams of MBA candidates at Saint Peter's College were assigned to identify five to 10 critical risks facing Chrysler Corp. They learned that Cerberus acquired Chrysler after Daimler-Chrysler could not turn it around. Cerberus brought in a controversial CEO—Robert Nardelli, formerly of General Electric Co.—who had attracted national attention for his management style when he was CEO of Home Depot. Several observations from their lists:

- **Leadership risk.** Teams identified Mr. Nardelli as a critical risk. Will his management style work better in the crisis environment of Chrysler as compared to Home Depot?

- **General vs. specific.** Should risks be broad or narrow? If we identify the wrong risk, the mitigation strategy will not matter. What can Chrysler do about housing and gas prices, reputation or competition if it faces pressing issues from production efficiency, legacy pension and benefit costs, or supply chain exposures?

- **Short vs. long-term.** Where do we start? We will not survive in the long term if we do not address deeply embedded risks. We will not survive short term if we run out of money.

One interesting issue is the absence of cultural risk on any of the five lists. It does not seem reasonable to limit the leadership exposure to the style and skills of the new CEO. Aside from governance risks and subsequent strategies that a CEO might develop to address them, will the culture allow the execution needed to turn around the ailing company?

In this context, ERM argues that the upside of risk is opportunity. Mr. Nardelli succeeded at GE and struggled at Home Depot. His appointment may be the perfect risk to be accepted by Cerberus. Only time will tell. Whatever happens, risk identification and consensus on critical risks should be a starting point for ERM at the level of governance. If Chrysler focuses on the right exposures, it increases the odds to develop the strategies and pursue the performance needed to achieve its goals.

Medicare: Drug subsidy challenging for employers

CONTINUED FROM PAGE 1

senior consultant at Towers Perrin in New York. "They didn't realize the amount of data they would have to collect and the time commitment.... As a result, employers have spent far too long with a lot of frustration to get payments that are less than they expected."

In some cases employers "overestimated how many they thought would be eligible or the claims that they would be able to capture," said Mr. McGill. Only claims for drugs on the Medicare formulary can be included in the analysis, he said.

"I was amazed at how many steps there were in the process," said Barb Zavodny, senior manager of corporate benefit strategy at McCormick & Co. Inc. in Sparks, Md., which applied for the RDS for prescription drug costs incurred by 800 retiree benefit plan members. "There are 12 steps in the reconciliation process, and each step has two or three steps. If you're doing it in-house, it almost takes a half of a person to do this."

Ray Brusca, vp-benefits at Black &

'I was amazed at how many steps there were in the (reconciliation) process.'

Barb Zavodny, McCormick & Co. Inc.

Decker Corp. in Towson, Md., said the company didn't receive its first RDS payment for 2006 until December 2007. Black & Decker expects to collect \$250,000 from CMS on behalf of the 700 retirees and spouses enrolled in its retiree health care benefit plan, he said.

"It's a new program. They obviously had a lot of bugs to work out," Mr. Brusca said. "But they just got around to issuing our first payment."

Part of the reason why RDS payments have been delayed or less than employers expected is that many employers have been unable to verify the eligibility of all of their retiree benefit plan members, a basic requirement for RDS payments.

In particular, many plan sponsors are missing the Social Security numbers of the spouses of former employees. And because of concerns about potential identity theft, many of these spouses have been hesitant to provide the information when asked by plan administrators.

"What delayed a lot of employers was getting their census squared away," said Derek Guyton, a principal and worldwide partner at Mercer L.L.C. in Chicago. "A lot of companies found their census data was inadequate. The big gap was information about the spouses."

In other cases, employers have to contact retirees that inadvertently enrolled in Medicare Part D plans to

confirm they intended to leave their former employer's prescription drug plan. If not, those retirees must contact CMS themselves so they can be added back to their former employer's rolls, said Kristi Davin, manager of employer Medicare products for CIGNA Healthcare in Nashville, Tenn.

Another reason for the RDS payment delays was that it took a while for the CMS computer system administering the application process to get up and running, according to Mr. Morfe.

"Early on, it was a little like moving into a house that wasn't quite done," he said. "CMS didn't get the application process installed until July 2006."

But even though CMS may have started late, it has caught up quickly, according to a spokesman for the government agency that administers RDS payments.

"As of December 2007, 97% of interim payment requests submitted by plan sponsors have been paid," the spokesman wrote in an e-mail. "The RDS system did experience a technical issue in the fall of 2007 that temporarily delayed the processing of reconciliation payment requests to a small number of plan sponsors. However, the issue was resolved and reconciliation payment processing recently resumed."

While many employers have applied for and received interim RDS payments, CMS said that so far only 6% of plan sponsors have submitted their final payment requests, a process called "reconciliation." Under RDS rules, employers only have 15 months after the close of their benefit plan year to "reconcile" all of their claims and the eligibility status of plan members. But CMS extended the deadline until March 31, 2008.

"If you don't file (a reconciliation), you have to give all the money back," said Pritpal Virdee, vp-Medicare at St. Louis-based prescription drug benefit manager Express Scripts. "And employers that were unable to prove the eligibility of certain retirees will have to return interim payments made on their behalf."

Unfortunately, "many employers have a fraction of retirees eligible for Medicare that they can't get approved (by CMS) and are running out of time," said Mr. Morfe. "It may be a small number, but it's big enough to matter."

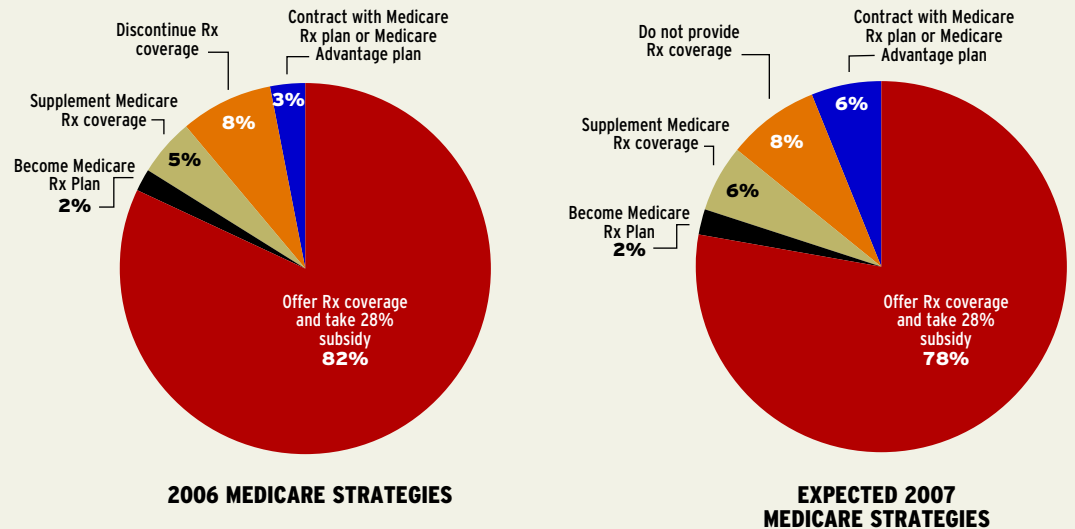
Rick Johnson, senior vp and public sector health practice leader in the Washington office for the Segal Co., said he expects some of his clients may never be able to verify the eligibility of certain plan members and will have to forgo any subsidy attributable to them for 2006.

"They very much bit off more than they could chew," he said. "But the question is, who else could have chewed it?"

Even though employers can delegate the eligibility confirmation task to a third party, such as an insurer or PBM, it is ultimately their responsibility to make sure it is done, Mr. Johnson noted.

MEDICARE PRESCRIPTION DRUG STRATEGIES

Employers' 2006 and expected 2007 Medicare drug benefit strategies for the largest age 65+ plan, based on responses from private-sector firms with 1,000 or more employees offering retiree health benefits.



Source: Kaiser/Hewitt 2006 Survey on Retiree Health Benefits

Cost, administrative burdens prompting employers to look beyond drug subsidy

By JOANNE WOJCIK

Many employers that initially took the Medicare Retiree Drug Subsidy are exploring other options, either to reduce their administrative workload or because it may be more financially advantageous.

Part of the reason employers chose RDS over other options was because the regulations governing prescription drug plans were not issued until after many of them had already finalized their 2006 plan years, according to Mike Morfe, a senior vp at Aon Consulting based in Somerset, N.J.

Moreover, "the insurance companies and pharmacy benefit managers weren't ready yet" to offer commercial prescription drug plan products, he added. "The marketplace is much more mature now."

In particular, employers whose caps on contributions to retiree health benefits cause them to fail the test that requires prescription drug benefits offered to Medicare-eligible retirees to be actuarially equivalent to Medicare Part D benefits to qualify for the RDS may consider contracting with a commercial PDP when they reach those caps, retiree benefit experts say.

"To get the RDS, the government looks at overall plan design like deductible, what is being charged to the retiree, etc. Does the employer contribute enough to take the subsidy? That's the thing that the caps affect. Many employers will reach the point where they no longer qualify for the subsidy," said Rick McGill, a principal responsible for retiree medical consulting services in the Atlanta office of Hewitt Associates Inc. "That point could be anywhere from a year or two to

five years from now."

In some cases, employers that have reached their caps have adopted dual strategies, according to Mr. McGill.

"They have groups for which they can get the subsidy for, and others for which they can't, so they're offering them a PDP," he said.

While they may no longer receive RDS payments directly, such employers can receive at least some indirect financial benefit through the government subsidy paid to PDPs, according to Derek Guyton, principal and worldwide partner in the Chicago office of Mercer L.L.C.

However, there is a downside. "The payments to PDPs may be comparable to RDS, but the RDS is tax-free, which can make it worth more" to a for-profit entity, such as a corporation, he said. "There is also a tax deduction for the benefit costs, and with the PDPs the tax deduction actually goes down because the premiums are lower."

Because public entities don't pay taxes and don't need such tax breaks, the PDP may be more attractive than the RDS because the capitated payments PDPs receive from the Centers for Medicare & Medicaid Services can be used to lower plan costs, thereby reducing the future retiree health care liabilities that public entities must report under the new Government Accounting Standards Board rules.

By contrast, public entities cannot apply RDS payments to their retiree health liabilities because these payments are considered "intergovernmental transfers," public entity retiree benefit experts say.

"With a PDP, the plans' premiums reflect the capitated pay-

ment received from CMS," said Rick Johnson, senior vp and public sector health practice leader for the Segal Co. based in Washington. "Then the actuary takes into account that the entity has an insured contract with a price lower than the projected claims costs. It's like they're transferring the risk."

Darrell Wells, director of risk management and benefits at the city of Odessa, Texas, switched the retiree benefits provided by the city's Family Health Benefits Pool to a PDP from RDS for 2007.

"The first year, we went the subsidy route. By the end of that year, I crunched the numbers and decided that the claims minus the subsidy was more than it would cost to pay the premium for a PDP," he said. "The GASB impact was also a consideration."

The transition worked. "After switching to a PDP strategy for 2007, total claims plus PDP premiums dropped below retiree contributions for the first time," Mr. Wells said.

However, he added, "claims for this small group are inherently unpredictable. Next year, the ratio may reverse."

While most of his public entity clients chose RDS for plan years 2006 through 2008, "they are asking about putting a PDP option in their next contract bid," said Mr. Johnson. He predicts that most public entities will eventually switch to a PDP for three primary reasons:

"They don't have to deal with all the reconciliation; they get the benefit of the reduced premiums regardless of what they're subsidizing; and they can administer it as a contract, which is what government people do best," Mr. Johnson concluded.

FMLA: Expansion may cause administration challenges for employers

CONTINUED FROM PAGE 1

Under the other expansion, employees who are the spouses, children, parents or next of kin of a servicemember could take up to 26 weeks of leave under the FMLA to care for the servicemember who incurred an injury during military service when that injury results in the servicemember being unable to perform his or her duties.

Business groups, while not objecting to the expansion, say the way legislators tacked the FMLA provisions onto the broader bill—no congressional hearings, for example, were held on the provisions—will complicate FMLA administration for employers.

For example, the legislation does not specifically say when the provisions will take effect. "This was done in a rushed way and it shows," said Marc Freedman, director of labor law policy at the U.S. Chamber of Commerce in Washington.

"Employers definitely need clarity on the effective date," said Lisa Horn, manager of health care for the Society for Human Resource Management in Alexandria, Va.

Ultimately, it would be up to the Labor Department to specify the effective dates of the provisions. Benefit experts, though, say they have heard informally from federal regulators that the 26-week provision will take effect when the legislation is signed into law, while the 12-week provision would not be effective until regulations are issued.

Other provisions also will need regulatory guidance from the Labor Department to help employers administer the expansion. For example, the legislation does not spell out the situations in which employees could take leave when a family member is called up or is on active duty.

"Are we talking about situations in which the wife needs leave to

CHANGES IN FMLA

How the Defense Department spending bill would expand the Family and Medical Leave Act:

- Extends FMLA to family members of employees called up for military service.
- Provides up to 26 weeks of leave to family members of military personnel who are injured during military service.

ISSUES TO BE RESOLVED:

- Effective date of the new FMLA provisions.
- Defining situations in which family members are eligible for leave under the FMLA after employees are called up for military duty.

take the kids to soccer practice because the husband has been called up?" asked the Chamber's

Mr. Freedman.

While the legislation says leave could be taken for a qualifying exigency, "exigency" is not defined, leaving it to the Labor Department to provide guidance, said Amy Kohn, a consultant with Hewitt Associates Inc. in Lincolnshire, Ill.

Once the legislation is signed into law, employers will have to revamp their FMLA policies and administration, as well as communicate the new FMLA eligibility rights to employees.

"You are going to have to incorporate this information in employee handbooks," said Neil Grossman, an attorney with Mercer L.L.C. in New York.

Experts say it is unlikely that many employers are even aware of the congressional action, given that the FMLA provisions are tucked away in a broader bill and that the provisions have received little publicity.

"This happened very quickly,"

said Ms. Kohn.

The impact of the FMLA provisions on employers will vary significantly, with the greatest impact on those employers, such as airlines and defense contractors, where large numbers of employees are called up for military service.

"The prevalence will be quite industry specific," said Tom Klett, a senior consultant in the Stamford, Conn., office of Watson Wyatt Worldwide.

While precise figures are not available, the Labor Department estimated in 2005 that between 8% and 17% of eligible employees took FMLA leave.

Even though relatively small numbers of employees will be affected by the FMLA expansion, the availability of the benefits will be "deeply important" for those individuals and their families, said Andy Anderson, of counsel with Morgan, Lewis & Bockius L.L.P. in Chicago.

Recession: Prolonged economic slump may tighten insurance market

CONTINUED FROM PAGE 3

generally speaking, marketwide."

"The primary impact is going to be within the investment portfolio," said Mr. Lane, noting that some insurers' portfolios are exposed to the mortgage-backed and asset-backed market.

In addition, he noted that the industry overall invests significantly in the municipal and corporate bond markets. "As the credit environment continues to deteriorate and credit losses go up, that's going to put pressure on their investment portfolio, but we don't view it as a major drag on capital adequacy."

Like Mr. Gallant, Richard Kerr, chief executive officer of Dallas-based electronic insurance exchange MarketScout, predicts that even if the current economic turmoil doesn't turn into a recession, D&O insurers, as well as some other professional liability underwriters, are likely to feel the pinch. "We do believe the professional liability market will be impacted by the trickle down of the subprime mortgage crisis," he said.

Previous recessions have tightened the market somewhat, said David Cummins, professor of risk

management, insurance and financial institutions at Temple University in Philadelphia. "Any investment downturn could tighten the market," he said.

"If there was a prolonged slump in the stock market or if bond defaults began to go up, this is going to tighten the market," he said. He added that insurers generally hold very high-quality bonds.

Some observers warn if current conditions deteriorate into a full-fledged recession, though, insurers

'We're in the midst of a soft market now, so they're challenged to find revenue growth as it is.'

Jim Auden, Fitch Ratings Ltd.

could be hit by a double whammy of price stagnation and spikes in some claims.

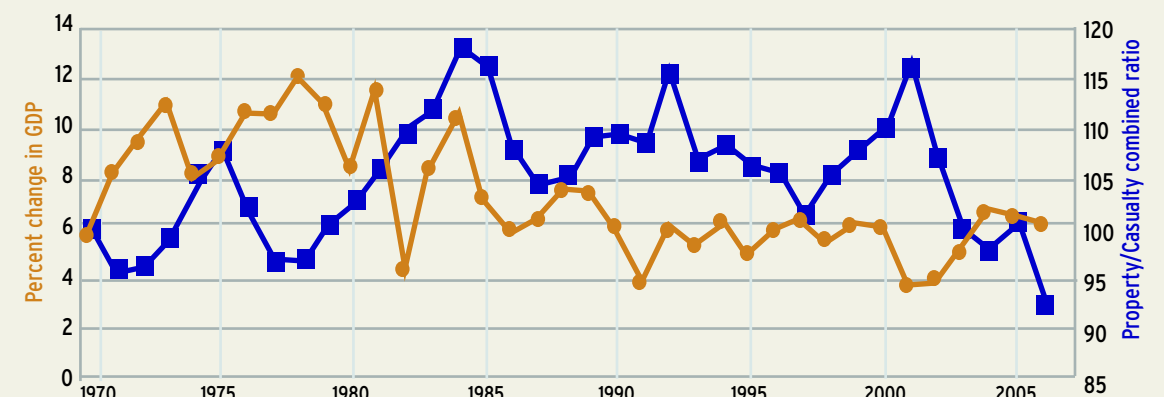
The hit on revenue would be obvious, said Jim Auden, managing director of Fitch Ratings Ltd. in Chicago. "Unemployment's up, so you're selling less workers compensation," he said. Revenue from commercial property insurance would also drop, because "there's less construction and values aren't going up."

And insurers would be hard-pressed to make up the difference, he said. "We're in the midst of a soft market now, so they're challenged to find revenue growth as it is." Recession "could trigger declines in investments, and it could also affect claims," said Temple's Mr. Cummins. "The research on the correlation between claims and economic conditions is not very clear."

"On the commercial side, you'd see some impacts because workers compensation premiums are linked to employment," said Sean

SNAPSHOT

Comparison of 30 years of percentage change in the gross domestic product to the combined ratio of the property/casualty industry



Source: Insurance Services Office, Bureau of Economic Analysis

Mooney, chief economist at Guy Carpenter & Co., the New York-based reinsurance brokerage unit of Marsh & McLennan Cos. Inc.

In addition, "you see a direct impact" on coverage related to sales and inventory because of decreased demand.

In addition, Mr. Auden and others say that the nature of any future

recession could have a considerable affect on what insurers experience. A downturn accompanied by inflation, termed "stagflation," could "work very adversely because of claim cost escalation and it gets harder to predict claim costs. You get a bump up in inflation; it's hard to keep up."

"Is this a recession where we have

stagflation?" asked Myron Picoult, an independent insurance consultant. "I don't think anybody's got the answer."

"Inflation has clearly crept up," he said, and "any pick up in inflationary pressures doesn't help the business, because it seems to bring into question in the adequacy of reserves."

Recession could spark more insurance fraud

If the subprime mortgage crisis triggers a recession, fraud could become a greater issue for property/casualty insurers of both the commercial and personal lines variety, say industry observers.

That could be particularly true in regard to homeowner arson, said Sean Mooney, chief economist of Guy Carpenter & Co. L.L.C. in New York. "When the value of your home drops below the value of your mortgage, there is an incentive" to turn to such an extreme response, he said.

That could be true for commer-

cial properties as well, said Myron Picoult, an independent insurance consultant.

"If you've got situations where people are facing foreclosure, have there been any unusual incidents of theft or fire?" asked Mr. Picoult. "Somebody says 'I can't pay the mortgage here, let 'em burn down,'" he said.

This could be a temptation for speculators who hoped to flip properties and find themselves with empty buildings instead, he said.

Workers compensation could also have its share of fraudulent

claims, observers say.

"Workers comp could see claim costs go up; people are getting laid off and right about that time, you get some injuries at work," said Jim Auden, managing director of Fitch Ratings Ltd. in Chicago.

"Sometimes, you'll see an employer in advance of a layoff see if they can put more people on permanent or temporary disability," said Mr. Mooney. "Sometimes, that's straight fraud or sometimes it's just bending the rules a little bit."

—By Mark A. Hofmann

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which is owned by Citigroup, has made an undisclosed, "significant" investment in Beecher Carlson to further accelerate growth, the broker said. The funding will be used to invest in specialized production and client service teams, technology and strategic acquisitions, Atlanta-based Beecher Carlson said.

Anderson Kill attorneys depart after merger fails

Policyholder law firm Anderson Kill & Olick P.C. has rejected a merger offer

from the much-larger Reed Smith L.L.P. law firm, but the firms are coordinating the movement of more than one-third of Anderson Kill's partners to Reed Smith. As a result, about two dozen of Anderson Kill's 69 partners will be moving to Reed Smith. Altogether, about 55 of Anderson Kill's 120 attorneys will be moving to Reed Smith. Reed Smith has 23 offices and more than 1,500 attorneys worldwide. Insurance recovery will remain a core practice for Anderson Kill, according to a statement by the New York-based firm.

Prescription for pot doesn't bar firing

An employee whose doctor recommended that he use marijuana cannot claim disability-based discrimination against an employer that fired him for testing positive for drug consumption, the California

Supreme Court ruled. The plaintiff in *Gary Ross vs. Ragingwire Telecommunications Inc.* claimed his former employer violated state anti-discrimination law when it fired him rather than make accommodations for a disability. At issue was whether California's Compassionate Use Act would override an employer's policy against drug use. The 1996 act provides a criminal defense in cases where a doctor recommends marijuana use. But nothing in the act suggests voters intended the act "to address the respective rights and duties of employers and employees," justices said in the 5-2 decision, upholding lower court rulings.

Noted

Swiss Reinsurance Co.'s capital markets unit has structured and placed \$85 million worth of securities covering windstorms in the

United States and earthquakes in California and Central America....Two of the candidates for the Republican presidential nomination have endorsed the creation of some form of **national insurance backstop** that would respond to natural disasters. Both former New York Mayor Rudolph Giuliani and former Massachusetts Gov. Mitt Romney expressed their support for the idea during last Thursday's GOP debate in Boca Raton, Fla....**Wausau Insurance** has appointed Susan Doyle as president and chief operating officer. Ms. Doyle, who replaces the retiring Mark Fiebrink, has served as executive vp for field operations since 2005....Leah Binder, vp of Franklin Community Health Network in Farmington, Maine, has been named chief executive officer of the Washington-based **Leapfrog Group**. She replaces Suzanne Delbanco, the organization's first CEO, who left in October.

Gen Re: Defense strategies at odds in finite trial

CONTINUED FROM PAGE 1

tinue throughout the trial," Frederick Hafetz, Mr. Milton's lawyer, told U.S. District Judge Christopher F. Droney last week. "I don't see how we can exist in the same courtroom."

Reid Weingarten, Ms. Monrad's lawyer, agreed: "It's become clearer and clearer that...there is open antagonism between our defenses," he said.

Judge Droney denied the joint motion to sever, as he has similar motions filed before the trial got underway, and testimony resumed for a third week.

Defense lawyers in multiple-defendant white collar fraud cases often bring motions to sever their clients, but those motions often are denied, said Philip Hilder, a former federal prosecutor now with Hilder & Associates in Houston.

Severance is often sought on grounds of mutually antagonistic defense strategies or because a defendant less involved in alleged wrongdoing is concerned about being found guilty by association with more culpable defendants, he said.

Courts, however, "don't like to carve up cases that will have to be tried numerous times," Mr. Hilder said. "There's a high burden defendants have to meet. Courts don't grant these motions lightly."

Charged with conspiracy and fraud along with Mr. Milton and Ms. Monrad are Ronald E. Ferguson, Gen Re's former CEO; Christopher P. Garand, former senior vp in charge of U.S. finite underwriting for Gen Re; and Robert Graham, former senior vp and legal counsel for the reinsurer.

Prosecutors charge that the defendants engineered a sham loss portfolio deal that allowed AIG to inflate its loss reserves by \$500 million in the last quarter of 2000 and the first quarter of 2001 to allay stock analysts' concerns about AIG's reserve levels.

While the deal appeared to transfer \$600 million of potential

losses to AIG for a \$500 million premium, the defendants agreed that no real risk would be transferred and that AIG would secretly refund a \$10 million initial premium payment from Cologne Re Dublin and pay Gen Re a \$5 million fee for entering the deal, prosecutors allege.

Mr. Houldsworth took the stand last week following testimony from Richard Napier, a former Gen Re senior vp. Both have pleaded guilty to conspiracy in the case and are cooperating with the government.

Mr. Houldsworth, a former accountant with Deloitte & Touche and KPMG in Bermuda, said he first learned of the proposed loss portfolio deal when he returned a call from Ms. Monrad while at dinner in London on Nov. 13, 2000.

Two weeks before, on Oct. 31, the deal had been launched by a phone call from AIG CEO Maurice R. Greenberg to Mr. Ferguson, according to earlier testimony.

Mr. Greenberg, identified as an unindicted co-conspirator, has not been charged in the case.

Ms. Monrad said that AIG wanted up to \$500 million in loss reserves and that Gen Re did not want to do the deal in the United States because it did not want to report the transaction in a U.S. subsidiary's financial statements, Mr. Houldsworth told jurors.

Mr. Houldsworth said he understood from this conversation that the deal was to be designed so that Cologne Re Dublin would not have to transfer cash to AIG, that there would be no tax consequences for the Dublin unit and that "we would not be charging them any losses, if we had any."

Within a couple of days, Mr. Houldsworth had drafted a reinsur-

ance slip for the deal and forwarded it to Ms. Monrad and others at Gen Re. The slip called for AIG to assume \$600 million in liabilities for a \$500 million premium, \$490 million of which would be withheld by Cologne Re Dublin.

The \$600 million liability limit was only intended to give the deal the appearance of risk transfer, Mr. Houldsworth said. Asked by Assistant U.S. Attorney Eric Glover how he came up with the figure, Mr. Houldsworth replied, "I just pulled it out of the air. It had to be more than \$500 million, and \$600 million was the next round number."

Attached to the slip was a schedule of six underlying reinsurance contracts to be included in the portfolio transfer. The nature of the contracts ensured that AIG faced virtually no risk of loss, Mr. Houldsworth testified: Two of the six, comprising \$315 million of the \$500 million of the transferred reserves, had already been retro-

ceded to other reinsurers by the Cologne Re Dublin, and it was "impossible that (losses on) the remaining contracts could ever add up to \$500 million, let alone \$600 million," he testified.

Much of Mr. Houldsworth's testimony related to a series of phone conversations with the defendants and others at Gen Re that were recorded by a Cologne Re Dublin taping system.

In one Nov. 15, 2000, call, for example, Ms. Monrad is heard to say that AIG "might have a tough time getting the accounting treatment they want out of the deal they want to do."

Asked by Mr. Glover what he believed she meant, Mr. Houldsworth said, "My understanding was that AIG wanted to account

for this as a risk deal and wanted the \$500 million of reserves."

Jurors heard excerpts of several other of Mr. Houldsworth's phone conversations, including:

- A Nov. 16, 2000, conversation with Milan Vukelic, former head of Cologne Re's Alternative Solutions unit in London. After Mr. Houldsworth describes the proposed AIG transaction, Mr. Vukelic observes in the recording that the deal will have no effect on AIG's profit and loss statement, but will "artificially bump up their reserves."

Mr. Vukelic has not been charged in the case.

- A Dec. 11, 2000, conversation with Franklin Montross IV, Gen Re's current president and chief underwriting officer, in which Mr. Houldsworth cites the "reputational risk" of the AIG deal to Gen Re and seeks Mr. Montross' OK to go ahead. In the recording, Mr. Montross notes that "Ron signed off on this," referring to Mr. Ferguson.

Mr. Houldsworth told jurors that since Mr. Montross was aware of the transaction and did not object, Mr. Houldsworth believed he had approved it.

Mr. Montross has not been charged in the case.

- A Dec. 11, 2000, conversation with Mr. Garand in which the two allegedly discussed how to transfer Cologne Re Dublin's part of the \$5 million fee for the AIG deal from Gen Re to Dublin without linking it to the loss portfolio deal. Mr. Garand suggests in the recording that "we could write you a losing transaction."

Mr. Houldsworth testified that Gen Re ultimately executed a reinsurance deal with its Dublin unit that was guaranteed to lose Gen Re \$12.6 million.

The only purpose of that transaction, Mr. Houldsworth said, was to repay Cologne Re Dublin the \$10 million premium it had advanced to AIG plus its \$2.6 million part of the fee.

Mr. Houldsworth's testimony continues this week.



Mr. Houldsworth.

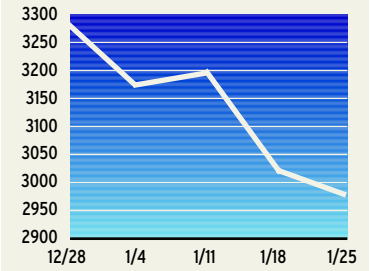
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Stock Index

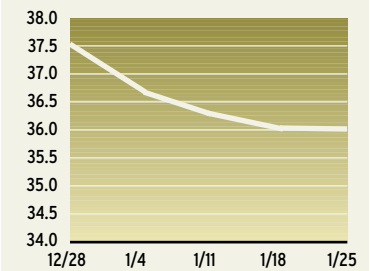
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Up-to-the-minute data for all 82 companies that comprise the BI Stock Index can be found at www.IndustryFocus.com.

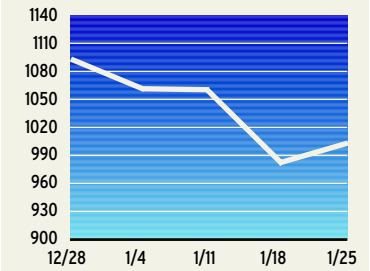
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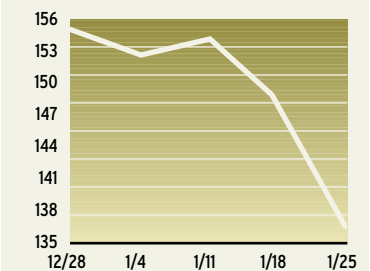
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BI INSURER/REINSURERS INDEX



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Percentage change of BI Stock Index vs. key indicators

BI STOCK INDEX	2971.72	↓ -1.22%
DOW JONES	12207.17	↑ 0.89%
S&P 500	1330.61	↑ 0.41%

LARGEST GAINS

Ambac Financial Group	83.06%
MBIA Inc.	66.08%
XL Capital Ltd.	13.08%
Citigroup Inc.	8.96%
SCOR S.A.	7.69%

LARGEST LOSSES

WellPoint Health Networks	-9.88%
Health Net Inc.	-8.98%
ING Groep N.V.	-8.18%
UnitedHealth Group	-8.09%
Humana Inc.	-7.58%

Source: Financial Content Inc. <http://fjfinancialcontent.com>

Business Insurance

END PAGE

Contributing: Jeff Casale,
Judy Greenwald,
Mark A. Hofmann, David Lenckus

CIA agent spied a good deal on coverage

Even some spies left out in the cold may not be totally on their own. A growing number have cover provided through a professional liability insurance policy that in some cases is government-subsidized.

Among the federal employees eligible for the coverage who has purchased it is a former Central Intelligence Agency supervisor facing an investigation over the destruction of interrogation videotapes, confirmed a spokesman for Wright & Co., which administers the program. Arlington, Va.-based Wright is a subsidiary of the Special Agents Mutual Benefit Assn.

The professional liability insurance policy is available to any full-time federal employee, defined as working at least 17.5 hours per week. For managers and supervisors in law enforcement agencies, the government covers half of the annual \$292 premium, according to the spokesman.

The insurance, which has been available about 15 years, currently covers about 30,000 federal employees, more than double the number of policyholders in 2000, he said.

The policy provides \$1 million of coverage for damages, plus \$200,000 of defense costs related to administrative actions and \$100,000 of criminal defense and investigation coverage.

Additional coverage that must be especially attractive to spies provides \$10,000 of accidental death and disability limits and \$10,000 of identity theft protection.

Under its "discovery period" feature, the policy continues to cover federal employees for 36 months after they leave government employment.

New York-based Hudson Insurance Group, a division of Stamford, Conn.-based Odyssey Re Holdings Corp., underwrites the policy.

Earvin 'Magic' Johnson is partnering with Aetna to help promote urban health care quality.

'Magic' tapped to help Aetna

A little "Magic" could go a long way for Aetna Inc. in its attempt to inform businesses and individuals in urban areas about the need for quality health care.

The Hartford, Conn.-based health insurer announced last week that it was teaming up with Magic Johnson Enterprises to help engage people and businesses in diverse communities to help them make informed decisions about health care, improve health care literacy and show them the benefits of wellness through exercise and healthy eating habits.

"Both Aetna and MJE are committed to improving community vitality by helping reduce the number of uninsured, particularly among entrepreneurial, urban business owners, and we want to improve racial and ethnic equality in health care," said Ronald A. Williams, Aetna chairman and chief executive officer in a statement.

Former Los Angeles Lakers guard and NBA legend Earvin "Magic" Johnson is chairman and CEO of the Beverly Hills, Calif.-based MJE. MJE, which formed in 1987, is built on partnerships with communities and businesses in ethnically diverse urban areas, providing them with entertainment, fitness centers and restaurants.

"If we can improve health care education, show people the benefits of wellness, exercise and healthy eating, and empower the community with knowledge to make informed choices about their health care options, we will have achieved significant results," Mr. Johnson said in a statement.

LANDOV

Reports of regulator's demise exaggerated

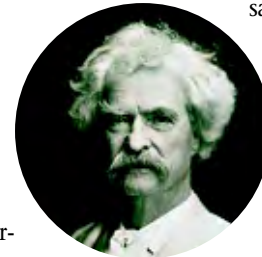
At first glance, Jim Poolman might not seem to have much in common with Mark Twain.

Mr. Poolman is a very much alive former insurance commissioner of North Dakota. Mark Twain is a legendary American author, who is no longer living.

But Mr. Poolman, who resigned from his post last year, noticed that a recent issue of a magazine called "Campaigns and Elections" referred to him as being no longer among the living. But instead of dying, Mr. Poolman had simply decided to step down early to establish his own insurance consulting firm.



AP



The living Mr. Poolman (top) and the late Mr. Twain

In an interview with a Bismarck, N.D., television station, an obviously amused Mr. Poolman said that he found the error "very funny" and wrote it off as "obviously an honest mistake" for which some poor magazine intern might have gotten a chewing out.

But Mr. Poolman must now have a bit better feeling for Mr. Twain's reaction upon learning that his obituary had been published prematurely. Like Mr. Twain, Mr. Poolman can now honestly protest that the report of his death was greatly exaggerated.

Wait till they get the legal bills...

A federal district court has waddled into a dispute between two "duck" tours. Boston Duck Tours and Super Duck Tours both operated Boston-area tours in amphibious landing vehicles.

Last July, the federal district court in Worcester, Mass., issued a preliminary injunction against Super Duck from using the phrase "duck tours" as a trademark. Super Duck Tours changed its name to Super Duck Excursions. But Boston Duck said its competitor's purchase of a sponsored link attached to the phrase "Boston Duck Tours" on Google's Web site violated that injunction.

The court disagreed. The advertisement, "which is fair, albeit aggressive competition," does not violate federal trademark law and is permitted under the injunction, said the opinion.



REUTERS

Two competing "duck" tour operators in Boston have squabbled in court over trademark infringement. A court ruled that the purchase of a sponsored link to the phrase "Boston Duck Tours" on Google.com didn't violate an injunction.



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