AIG won't face indictment, Spitzer suggests / 3

Wal-Mart investing in nation's first state-of-the-art hospital / 3

April 11, 2005
$5

www.businessinsurance.com

Business Insurance®

COMPENSATION CRISIS

WILLIS PAYS $51M TO END PROBES

By SALLY ROBERTS

NEW YORK—Joining its two larger competitors, Willis Group Holdings Ltd. last week reached settlements with state officials to end probes into the brokerage's compensation practices.

London-based Willis will pay $50 million in restitution to policyholders and adopt a new business model to resolve concerns about fraud and anti-competitive practices raised by New York Attorney General Eliot Spitzer and Acting New York State Insurance Superintendent Howard Mills. Simultaneously, Willis agreed to pay $1 million to settle investigations by Minnesota officials.

Specifically, the New York officials said Willis unlawfully deceived its clients by steering their business to insurers paying the highest contingent commissions; by unnecessarily running business through its own wholesale brokerage operation to derive additional commissions, and by leveraging its retail business to obtain reinsurance brokerage businesses.

Willis' settlement is modeled on earlier agreements reached with Marsh & McLennan Cos. Inc. and Aon Corp., the New York officials said.

MMC agreed in January to pay $850 million and reform its business model to settle fraud and bid-rigging charges, and Aon last month agreed to pay $190 million and change its practices to settle charges of fraud and anti-competitive practices. Unlike MMC and Aon, however, Willis did not face a civil suit from Mr. Spitzer and did not issue a formal apology as part of its settlement.

"We welcome the attorney general's conclusion that it was not appropriate to file a complaint against our company based on the findings of his investigation," Joe Plumeri, Willis' chairman and chief executive officer, said in a company statement.

"Willis moved quickly to remedy its problems," Mr. Spitzer said in a statement. "Its actions will help bring about greater transparency

See WILLIS / page 18

Wachovia purchase of Palmer & Cay boosts bank's bid to grow nationally

By SALLY ROBERTS

CHARLOTTE, N.C.—Banking giant Wachovia Corp. is making it known that it wants to be a major force in the insurance brokerage industry as well.

The Charlotte, N.C.-based bank announced last week that it has agreed to acquire Savannah, Ga.-based insurance broker Palmer & Cay Inc., in a deal that will enhance Wachovia Insurance Services Inc.'s property/casualty and employee benefits capabilities and also expand its footprint east of the Rocky Mountains.

For Palmer & Cay, the deal caps a 137-year history as an independent privately held firm but gives it the needed capital to achieve its ultimate vision of being a national brokerage.

After the deal, Wachovia Insurance will have more than $400 million in annual revenues, 40 offices and nearly 2,000 employees, according to the firms.

In 2004, Wachovia Insurance ranked as the

See WACHOVIA / page 17

Aon picks outsider as Ryan successor

By SALLY ROBERTS

CHICAGO—Aon Corp. is banking on a young, relatively unknown insurance consultant to lead the Chicago-based brokerage giant during one of the most tumultuous times in the industry's history.

Gregory C. Case, a 42-year-old McKinsey & Co. consultant, became president and chief executive officer of Aon last Monday, succeeding Patrick G. Ryan, who announced last fall his intentions to step down as CEO after nearly 40 years at the helm (*BI*, Oct. 4, 2004).

Mr. Ryan, a high-profile figure within the insurance industry, will remain executive chairman of Aon, which he built into the world's second-largest insurance brokerage through a series of major acquisitions over the past 35 years.

Mr. Case

While observers say the appointment of Mr. Case removes any uncertainty about the brokerage's leadership going forward, they are concerned about his youth and inexperience.

Unlike his predecessor, who spent his entire career running insurance companies or brokerages, Mr. Case has little operational experience in the industry. He has spent most of his career—the past 17 years—with McKinsey, where he most recently served as head of the management consulting firm's financial services practice. Prior to that, he was responsible for McKinsey's global insurance practice, of which Aon had been a client.

Marsh & McLennan Cos. Inc. also has been a client of McKinsey. The consulting firm in the late 1990s helped Marsh develop its Global Broking unit, which was at the heart of bid-rigging allegations in a suit filed by New York Attorney General Eliot Spitzer last October (*BI*, Nov. 1, 2004). Mr. Case said he has no knowledge of

See AON / page 18

Late News

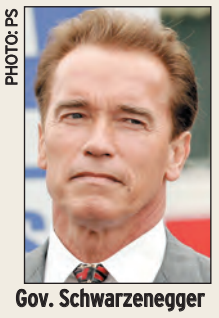
Reinsurers queried about Bermuda company

PartnerRe Ltd. and RenaissanceRe Holdings Ltd. Friday announced that they had received subpoenas from New York Attorney General Eliot Spitzer and the Securities and Exchange Commission seeking information relating to Bermuda-based Channel Reinsurance Ltd., in which both PartnerRe and RenaissanceRe are investors. The investigators recently requested information from another Channel Re investor, bond insurer MBIA Inc., which earlier was subpoenaed over certain financial reinsurance arrangements.

Schwarzenegger delays pension overhaul bid

California Gov. Arnold Schwarzenegger said he will postpone a ballot initiative aimed at cutting state spending by replacing the defined benefit pension plans covering public employees with defined contribution plans. California now is contributing about $2.6 billion a year to its pension program, up from $160 million in 2000, and the costs are out of control, the governor said. Gov. Schwarzenegger said firefighters and law enforcement officials pressed him to reconsider because the initiative, according to a state analysis, would erode their death and disability benefits. He said that he will delay the effort to meet with legislators in hopes of crafting compromise legislation.

PHOTO: PS



Gov. Schwarzenegger

See LATE NEWS/page 19

International

2004 natural disasters lower Lloyd's profits

Finite risk reinsurer Inter-Ocean to run off

Page 13

Aon Focus
www.aon.com/focus

Across the United States, the frequency of claims has more than doubled and severity has tripled in the long-term care industry since 1996.

APRIL 11, 2005

Long-term care continues to experience the worst liability cost increases in health care

Theresa W. Bourdon is managing director and actuary for Aon Risk Consultants. She is co-author of the Long Term Care 2005 General Liability and Professional Liability Benchmark Analysis. Theresa can be reached at theresa_bourdon@aon.com.

The long-term care industry is in a state of crisis across the nation. Following trends initially observed in Florida and Texas, an alarming number of states are experiencing dramatic increases for general liability and professional liability (GL/PL) coverage. A recent study, commissioned by the American Health Care Association, found that 14 of the 16 states analyzed experienced double-digit annual increases in their GL/PL costs over the past decade, with a majority of them experiencing loss cost trends in excess of 25 percent.

The study, which represented 23 percent of the beds in the United States, also found the following:

- Numerous states across the country are still experiencing increasing trends in the average annual loss cost per bed - most notable are Arkansas, Mississippi, California, Georgia, Alabama, Arizona and Tennessee.
- Increases in frequency remain problematic in the majority of states, with 12 of the 16 states analyzed experiencing annual frequency rate increases at or above 10 percent.
- The number of claims per year that long-term care operators incur has more than doubled, from 6.2 per 1,000 occupied skilled nursing care beds in 1996 to 13.1 in 2004, and the average cost per claim has increased to close to $180,000.
- Annual commercial insurance premium levels increased for the fourth straight year.
- Attorneys' fees are making up almost half of the total amount of claim costs paid for GL/PL claims in the long- term care industry.
- In Texas, tort reform that passed in 2003, and was strengthened by a constitutional amendment, appears to be having the greatest impact of any reforms among the states reviewed in the study on reducing GL/PL claim costs.

Unfortunately, as a result of the current crisis, the future of the long-term care industry is uncertain. It is expected that rising costs will continue to eat away at the government dollars set aside to fund long-term care, thus decreasing the amount available for patients. In addition, as operating long-term care facilities becomes less and less financially viable, the number of beds available will fail to keep up with increasing baby boomer demand.

It seems that tort reform, if well written and containing provisions that truly reduce claim frequency and severity, may have an impact on curbing the cost increases in long-term care; however, this is not a silver bullet, because litigation is not the sole contributor to the problem. A complete solution will come only when the insurance industry, consumers, the government and the long-term care industry all work together for a fair and effective resolution. This includes establishing realistic expectations for elder care; supporting public policies that encourage less government reliance, such as tax benefits for long-term care insurance; creating fair and reasonable patient care dispute resolution, including setting reasonable limits on damages and supporting the use of arbitration; and focusing on increasing the quality of health care.

Businesses facing pension plan crises create solutions through modeling and other strategies

Three years of declining interest rates and equity values have placed significant stress on U.S. pension plan sponsors, who have seen hundreds of billions of dollars in surplus assets deteriorate. Companies today face many challenges to their pension plans, including continuing declining interest rates, funding shortfalls, pension regulation and legislation, and a quickly aging workforce. Beleaguered companies are implementing strategies to mitigate the cost and volatility of their pension plans. Some potential solutions for businesses to explore include asset liability modeling and immunization strategies. To read more about pension plan solutions, visit **www.aon.com/focus**.

Global benefits management helps multinationals control costs, implement strategy

Driven by a number of factors, including Sarbanes-Oxley regulations, organizations conducting business globally are taking more interest in the details of worldwide employee benefits. These firms are striving for benefits that are appropriate, properly funded and compliant with legal requirements. An effective global benefits management program blends overall business strategy with local implementation. Several key factors contribute to the success of these programs, such as an appointed global account manager and a structured, customized, repeatable process. To read the complete article on the strategies behind global benefits management, visit **www.aon.com/focus**.

Inside

Online poll - [4/4 - 4/8]

Will you review your age anti-discrimination policy because of the Supreme Court decision allowing age discrimination suits to proceed even if the plaintiffs haven't been victims of deliberate bias?

Yes 43.3%

No 40.0%

Not sure 16.7%

Departments

REPORTING ON CORPORATE RISK AND EMPLOYEE BENEFIT MANAGEMENT NEWS

Business Insurance (ISSN 0007-6864) Vol. 39, No. 15, is published weekly by Crain Communications Inc., 360 N. Michigan Ave., Chicago, Ill. 60601-3806. Periodicals postage is paid at Chicago and at additional mailing offices. POSTMASTER: Send address changes to Business Insurance Circulation Department, 1155 Gratiot Ave. Detroit, Mich. 48207-2912. $5 a copy and $97 a year in the U.S. $130 in Canada and Mexico (includes GST). All other countries, $230 a year (includes expedited air delivery). Canadian Post International Publications Mail Product (Canadian Distribution) Sales Agreement No. 40012850, GST No. 136760444, Canadian return address: 4960-2 Walker Road, Windsor, ON N9A6J3. Printed in U.S.A.

Spitzer signals AIG won't face indictment

Investigators preparing to question Greenberg and Buffett

By DOUGLAS McLEOD

NEW YORK—New York Attorney General Eliot Spitzer last week indicated that he will not pursue criminal charges against American International Group Inc. as probes of the insurance industry expanded and investigators prepared to question former AIG Chairman Maurice R. Greenberg and Berkshire Hathaway Inc. Chairman Warren Buffett.

Mr. Buffett is scheduled to be interviewed today by investigators for Mr. Spitzer, Securities and Exchange Commission investigators and federal prosecutors about transactions between Berkshire's General Reinsurance Corp. and various insurers, including AIG, Berkshire reported last week.

"General Re and Berkshire have been responding to requests from all of the governmental authorities involved in these investigations for information relating to certain transactions that may have been accounted for incorrectly by counterparties of General Reinsurance…including in at least one case with" AIG, Berkshire reported. Regulators have already interviewed a number of current and former General Re officers and employees, the company added in an SEC filing.

Mr. Greenberg, who resigned as AIG's chairman and chief executive officer last month, is to be questioned under oath Tuesday.

One focus of the interviews is expected to be a 2000 transaction in which a General Re unit retroceded $500 million in premiums in a loss portfolio deal with an AIG unit.

AIG has admitted improperly accounting for the transaction as insurance, and questions about the deal apparently contributed the AIG board's decision to oust Mr. Greenberg.

Mr. Berkshire earlier this year disclosed the

See AIG / page 14

In the hot seat

PHOTO: AFP

Maurice R. Greenberg, left, and Warren Buffett were slated to face questions this week.

Wal-Mart to help fund hospital upgrade

Technology initiative to mirror giant retailer's inventory tracking system

By JOANNE WOJCIK

BENTONVILLE, Ark.—By 2007, the rural community of Bentonville, Ark., may be home to the nation's first state-of-the-art digital hospital, largely as a result of the philanthropy of the town's largest employer: Wal-Mart Stores Inc.

Wal-Mart's donation—$5 million distributed over three years—may also represent the first employer pay-for-performance initiative involving an upfront technology investment. It is part of the retailer's efforts to help address the nation's health care crisis, according to Susan Chambers, executive vp of risk management, benefits and administration.

"We're starting small—right in our hometown—where we've built a very strong and satisfying partnership with Mercy Health System of Northwest Arkansas," Ms. Chambers said in a speech responding to criticism of Wal-Mart's employee benefit practices (see story, page 4).

Wal-Mart is the biggest employer in Bentonville, its corporate headquarters. It employs 12,000 people at its home office campus, technology and distribution center and at local stores.

"In all too many hospitals, there is still a paper chart hanging off patients' beds. And many doctors don't have anything more sophisticated than a beeper," Ms. Chambers remarked at the National Business Group on Health's 2005 Business Health Agenda last month in Washington.

By contrast, she noted, Wal-Mart associates use hand-held computers to track inventory and stores have touch-screen credit card readers to conduct real-time transactions.

"The health care industry uses new medical technology relentlessly to develop new treatments and cure disease. Private industry uses new technology relentlessly to add value and to reduce cost," she said.

Specifically, Wal-Mart is helping to finance new technology, implement new operational

See WAL-MART / page 16

PHOTO: GETTY

Wal-Mart hopes the hospital project will benefit its workers in Bentonville, Ark.

Sale of ACE units a bad deal for policyholders, insurers say

By MICHAEL BRADFORD

HARRISBURG, Pa.—Insurers petitioning regulators to block the sale of three ACE Ltd. subsidiaries to a London investment firm have outlined new concerns about potential harm to policyholders from the deal.

Attorneys for Allstate Insurance Co., American International Group Inc. and Chubb Corp. last week filed new objections to the sale with the Pennsylvania Department of Insurance. In that deal, Bermuda-based ACE is seeking to sell ACE American Reinsurance Co., Brandywine Reinsurance Co. S.A.-N.V. and Brandywine Reinsurance Co. (UK) Ltd.—units that are running off asbestos and environmental claims—to Randall & Quilter Investment Holdings Ltd.

The April 5 letter revises complaints the lawyers lodged with insurance regulators in two other letters to the Insurance Department. In a Feb. 18 missive, the insurers noted that they would be adversely affected by the sale because they have ceded millions of dollars of reinsurance to the ACE subsidiaries (*BI*, Feb. 21).

In addition, Boston-based Liberty Mutual Group Inc. said last week that it wrote to the Insurance Department expressing concerns that the proposed transaction will have a "significantly unfair and unreasonable effect upon policyholders and reinsurance cedents, including Liberty Mutual." If approved, the acquisition "would establish an unfortunate precedent under which a financially strong company could walk away from potentially underfunded liabilities," the insurer said.

Pennsylvania regulators say they have the authority to approve the ownership changes because ACE's U.S. operations are domiciled in the state.

Mark A. Aronchick, an attorney with Hangley, Aronchick, Segal & Pudlin in Philadelphia, wrote in the April 5 letter to regulators that documents that were not available at the time his firm first filed objections gave rise to insurers' additional concerns.

Among the concerns outlined in Mr. Aronchick's letter is that policyholders will be harmed by Randall & Quilter's "aggressive claims management." The attorney refers to a document that he says indicates Randall & Quilter intends to take claims management responsibility away from National Indemnity Co., which now provides that service.

The document shows that Randall & Quilter intends to become "more aggressive in compelling commutations and settlements, and thereby force policyholders to settle for less coverage than they are entitled to under their policies," Mr. Aronchick charges in his letter.

The letter also charges that ACE is seeking to limit its liability, while "keeping a substantial potential upside." Mr. Aronchick said the purchase and sale agreement between ACE and Randall & Quilter shows that the insurer is attempting to dump the liabilities but is entitled to a 50% interest in future capital distributions from ACE Re and Brandywine UK.

The agreement also gives ACE the right to 50% of any "future release of reserves in the event that U.S. tort laws are reformed and the reserves of ACE Re and Brandywine subsidiaries are reduced as a result," Mr. Aronchick notes in the letter.

A spokesman for ACE declined to comment on the concerns outlined in Mr. Aronchick's letter.

Airline can't tap property policy for Sept. 11 losses: Court

Denial of business interruption coverage upheld

By RUPAL PAREKH

NEW YORK—United Airlines Inc. cannot recoup earnings lost in relation to the Sept. 11, 2001, terrorist attacks under the business interruption portion of a property insurance policy, a federal judge has ruled.

The airline in July 2003 filed a lawsuit against the Insurance Co. of the State of Pennsylvania, a Philadelphia-based unit of American International Group Inc., charging that it wrongly denied liability under a "property, terrorism and sabotage" insurance policy carrying limits of up to $25 million (*BI*, July 21, 2003).

Chicago-based United in its complaint contended that a business interruption provision of the policy was triggered due to a Federal Aviation Administration mandate that shut down airports nationwide, and a system-wide loss of revenue as a result of the attacks on the World Trade Center and the Pentagon.

Two of the four passenger planes hijacked on Sept. 11 by terrorists were United flights.

United—whose owner, UAL Corp., filed for Chapter 11 bankruptcy protection in December 2002—said it took a charge of nearly $1.2 billion related to losses from the terrorist attacks, and sought damages for no less than $25 million from its insurer.

The airline claimed it was physically impacted, at its World Trade Center ticket counter, which was destroyed in the attacks, as well as its gate property at Washington's Reagan National Airport, which it said was affected by debris from the attack on the Pentagon.

Under the policy, ISOP stated it would provide coverage for "property damage, loss of gross earnings, and extra expense" resulting from damage caused by acts of civil authority or terrorism at insured locations, among other things.

The policy also insured against business interruption losses caused by terrorism-related damage or destruction at insured locations.

"As far as civil authority coverage is concerned, it was our view that

See UNITED AIRLINES/page 19

PHOTO: GETTY

United Airlines claimed its gate property at Reagan National Airport was affected by debris from the Sept. 11, 2001, attack on the Pentagon.

States consider ways to make employers pay uninsured health costs

By JOANNE WOJCIK

As states consider ways to recover their costs of caring for the uninsured, employers in some are facing proposals to make them foot part of the bill.

Legislation proposed last week in Massachusetts would charge employers that do not provide health benefits for the state's costs of providing care to such companies' employees.

Meanwhile, a measure requiring large employers to spend at least 8% of their payroll on providing health insurance benefits passed the Maryland Senate on Tuesday.

PHOTO: REUTERS

Massachusetts has named McDonald's Corp. as one of four companies that create health care cost burdens on the state.

In Massachusetts, Senate President Robert Travaglini, D-First Suffolk and Middlesex, introduced a bill that would impose a "free-rider surcharge" on employers of between 50% and 100% of the cost of free care provided to uninsured employees or their dependents.

For people who work for more than one employer, none of which provides health benefits, the surcharge would be divided among those employers using a formula established under the legislation.

Uncompensated care provided to employed individuals and their dependents cost the state more than $52 million between 2002 and 2004, according to a report released in February by the state Executive Office of Health and Human Services. The report cited four companies—Dunkin' Donuts Inc., Stop & Shop Cos., Wal-Mart Stores Inc. and McDonald's Corp.—as creating the greatest burden on the state, with more than 1,000 employees from each receiving public health benefits.

In Maryland, senators passed S.B. 790, which would force employers with at least 10,000 employees to spend at least 8% of their payroll on providing health insurance benefits. Those that fail to do so would have to contribute to a state fund that provides health care coverage to low-income residents.

The bill, which passed the House last month, is expected to become law because it has the support of enough lawmakers to override Gov. Robert L. Ehrlick Jr.'s likely veto, sources say.

The legislation also would require nonprofit employers with 10,000 or more employees to spend at least 6% of their payroll on health benefits.

Though the measure applies to all employers with more than 10,000 employees in Maryland, it became apparent during Senate debate last week that the bill would have the largest impact on Bentonville, Ark.-based Wal-Mart, which employs 15,000 workers in Maryland.

Lawmakers said the company told them a year ago that it spent about 5% of its payroll on health benefits.

A spokesman for Wal-Mart could not be reached.

Employers turning to networks to help curb rising comp costs

By ROBERTO CENICEROS

Employers in California and Texas are banking on doctor networks to curb the overutilization of medical treatments in their workers compensation systems, with additional efforts expected to follow in other states.

California employers and insurers in January began directing employees to provider networks, as a result of workers comp reforms adopted last year. Current legislation in Texas allowing employers and insurers to direct injured workers into provider networks is likely to be enacted this year, said John Marlow, assistant vp state affairs in Austin, Texas, for the American Insurance Assn.

Other states could follow with similar legislation next year, observers say.

Studies by the Cambridge, Mass.-based Workers Compensation Research Institute show that doctor networks tend to use fewer medical services and lower medical costs. They manage to do so without increasing disability duration or income benefit costs, and they are particularly successful where networks have the greatest penetration.

But experience in states that already allow employers and insurers to provide treatment by doctors contracted into networks also reveals that certain network business models actually promote utilization, observers say. Employers, therefore, need to scrutinize how networks are formed and managed once they are in place.

Companies that form networks can fuel utilization by contracting to pay doctors discounted rates for each treatment while promising to direct patient volume to them, said Debra Borger-Cerrato, chief executive officer for Professional Reviews Inc., a physician peer review company based in Atlanta.

If doctors grow disenchanted with such compensation arrangements, they might spend less time with patients yet increase their revenues by performing additional services for each injured worker under their care.

"Utilization has been the reason networks were formed and the reason that networks failed," Ms. Borger-Cerrato said. Additionally, she noted, the better doctors in a given geographic area may already attract

See WORKERS COMP/page 16

Catastrophe losses weigh down P/C reinsurers' performance

By JUDY GREENWALD

U.S. reinsurers, coming off a catastrophe-heavy year in 2004, face the prospect of softening rates and continued uncertainty over adverse loss development.

But, barring more major catastrophes, the reinsurers should report strong results this year, despite those factors, say observers.

"The business is still going to be attractive," said Mark P. Lescault, head of the divisional underwriting office at Swiss Re America Corp. in Armonk, N.Y. January renewals indicated relative stability, he said.

"Certainly, we saw some moderate rate softening, but things stayed at attractive levels without question—still well above the soft market-type of pricing," he said.

The 26 reinsurers that reported their year-end results to the Washington-based Reinsurance Assn. of America posted a 106.2% combined ratio vs. 101.2% ratio reported by a comparable group for 2003. The top 20 reinsurers, based on net premiums written, also posted a 106.2% combined ratio vs. a 100.2% combined ratio for the comparable period a year ago.

Reinsurers' 2004 results

Net premiums written for the RAA reinsurers totaled $28.76 billion, a 6.1% decline from the $30.63 billion reported by a comparable group in 2003. The 20 largest reinsurers reported $28.44 billion in net premiums written, which was almost flat compared with a year ago.

It was a "pretty strong year" for reinsurers, said Mark Rouck, senior director at Fitch Ratings in Chicago. "There was some adverse effect from the hurricanes, and to a lesser extent the tsunami and Japanese typhoon losses, but generally the results were pretty strong."

Mr. Lescault said, "Overall, underwriting-year results were good in the sense that the quality of the basic business continues to be good,

See RESULTS/page 15

We want you to know

Aetna Pharmacy

Now you can clearly see how your plan benefits your business.

Aetna introduces a more open approach to Pharmacy benefits management. Understanding the costs and overall value of your prescription drug plan, and selecting the right company to manage it, can be difficult and confusing. But it doesn't have to be. Aetna shares individual price elements as well as other relevant cost and revenue information, so you can be confident that what your company is getting is worth what you're paying. It's another way Aetna is providing better information to improve the quality of our benefits and services. To find out more about what makes Aetna the clear choice in Pharmacy management, call your broker, Aetna representative, or visit us today at aetna.com.

We want you to know℠

Aetna®

Health
Dental
Pharmacy
Disability
Long-Term Care
Life

New York, New Jersey in talks on for-profit health plan conversions

By GLORIA GONZALEZ

Despite aggressive regulatory oversight that halted several recent attempts by nonprofit health insurers to convert into for-profit companies, news has emerged of possible plan conversions in New York and New Jersey.

Although only informal discussions have taken place at this point, Horizon Blue Cross & Blue Shield of New Jersey and HIP Health Plan of New York have been identified as candidates for conversion by state officials.

The trend of nonprofit health plans converting into for-profit companies has slowed in the past two years, with five Blue Cross & Blue Shield plans either abandoning conversion attempts or having their conversion applications denied by state regulators.

Currently, the only nonprofit Blues plan seeking to convert is Mountlake Terrace, Wash.-based Premera Blue Cross. Insurance regulators in Washington state and Alaska rejected its conversion applications last year, decisions that are being appealed in state courts.

In the case of Horizon and HIP, though, state officials have initiated the latest conversion talks, which observers believe increases the likelihood of the companies converting to for-profit status.

Reasons to convert

- New York Gov. George Pataki's 2005/06 budget proposal includes $400 million in revenues from health insurance plan conversions.
- Changing to for-profit status would allow access to capital to compete with other for-profit companies.

New York state Gov. George Pataki's 2005/06 budget proposal includes $400 million in revenues from insurance company conversions. While Gov. Pataki did not name any companies, a HIP spokesman said there have been "fact finding" meetings with the governor and legislative officials.

Similarly, New Jersey officials have held informal discussions with representatives of Newark, N.J.-based Horizon regarding a possible conversion.

Horizon had explored the possibility of converting a few years ago, but abandoned its efforts before even filing an application with regulators due to the difficult regulatory environments its counterparts in other states were encountering (*BI*, Sept. 1, 2003). "We have not put it back on the table," a Horizon spokesman said. "We have not filed any applications with the state."

The fact, though, that state officials are now advocating a conversion of the company makes it more likely that the conversion will actually happen this time, analysts say.

"The state really wants them to go public because of the money they stand to gain if the company goes public, so it's a bit unique in that situation," said Isabelle Roman-Barrio, senior financial analyst at A.M. Best in Oldwick, N.J.

The rationale for conversions—namely, access to capital that would enable the nonprofit companies to effectively compete with larger, for-profit companies—still exists, analysts say. In fact, the HIP

See CONVERSIONS / page 19

PAUL WINSTON

Editorial Director

Readers take sides on industry's silence

A few weeks ago, I wondered why the industry was mute in response to the regulatory offensive against individuals, companies and practices in the insurance and brokerage industries. Where, I asked, were the voices of leaders who would stand up for the industry against the allegations of rampant corruption, unethical practices and lax oversight?

While the industry still lacks a clear champion, several readers wrote to share their views of the situation, which I think are worth sharing.

Don McNay, president of McNay Settlement Group in Richmond, Ky., and a self-described "business columnist with a rock and roll attitude," suggested that the problem behind the insurance industry's public response is that it lacks a clear and recognizable spokesman.

"Everyone recognizes the AFLAC duck, but I don't know anyone, including myself, who could identify the president of AFLAC," he wrote in his most recent column, which can be read at *www.donmcnay.com*.

"Spitzer, like Teddy Roosevelt, a New Yorker of an earlier generation, understands there is a road to the White House by taking on big business," Mr. McNay wrote. "Like Roosevelt, Spitzer comes from wealth and relishes a good fight. The bullying tactics that always worked for Greenberg backfired when he came up against Spitzer."

"I won't be surprised to see state attorneys general and members of Congress adopt the mantra of insurance reform as they seek higher offices. It is a no-lose political issue as long as 'Hank' is the public face of the industry," commented Mr. McNay.

The CEO of a risk management consulting firm suggested the insurance industry's actions mean it won't win much sympathy from consumers. "Let us not forget the ill will the insurance industry causes with their perpetual swings from soft market to hard market and then back again....How many businesses, especially small businesses, have been damaged due to these maniacal market swings?" the consultant questioned.

The president of an actuarial consulting firm said of industry executives, "of course they're silent," for fear of becoming targets.

"Even if they've done nothing wrong and their companies are squeaky clean (and many of Spitzer's targets have done nothing illegal, immoral, or unethical), they will be distracted from running their businesses and will spend many millions of dollars defending against frivolous charges (and there is no sanction for an out-of-control prosecutor). In the process they may be ruined, personally and professionally, because they are presumed guilty until proven innocent, and even if proven innocent, the damage may be permanent.

"The end result of all of this is that a few bad apples will be punished, a lot of good apples will be ruined, and we all will end up paying more for insurance coverage," he wrote.

Several readers, however, suggested that where's there's smoke, there's fire, and that Mr. Spitzer's investigations are needed to uncover real and pervasive wrongdoing in the industry.

"Our leaders in industry had an opportunity to change their business practices after watching Enron, WorldCom, Tyco and some of the other companies who had chosen to defraud both individuals and businesses. Our leaders chose not to make changes and this had led to our current situation," a claims executive wrote. "I can only hope that we learn from this and go forward from here to set the business standard once again. Until we are willing to take a hard look at ourselves, I doubt that we will break free from times such as these," a claims executive wrote.

And, as Felix Kloman, editor of "Risk Management Reports," wrote in an April 4 letter in *BI*: "Perhaps the lack of insurance industry response is because too many of its practitioners, even the large majority who are free of direct corruption, acknowledge what Eliot Spitzer and the SEC have found: a system riddled with blatant conflicts of interest. True...only a few...have broken the law, but the entire industry, including the buyers, have willingly subscribed to a system that is basically unethical, one that has misaligned interests for more than 40 years. Perhaps it's the silence of embarrassment that you hear," he wrote.

Editorial Director Paul Winston's commentary appears fortnightly. He can be reached at pwinston@businessinsurance.com.

American Re Direct Treaty

American Re Direct Facultative

Munich-American RiskPartners

American Re Broker Market

American Re HealthCare

Strength.

American Re. It's just plain good for your business.
If you want protection you can count on in uncertain times, you want a reinsurance company that's got real power. You want American Re.

For over 86 years, we've been a source of strength and stability to our clients in good times and bad. And as part of the Munich Re Group, we're more committed than ever to continuing this proud legacy of service.

No matter what your needs are, American Re stands ready to serve up a strong solution.

AMERICAN RE
A Member of the Munich Re Group

555 College Road East, Princeton, NJ 08543
www.amre.com

Products and services provided by American Re-Insurance Company.

Editorial

Positives for Aon's new CEO

Aon Corp.'s new chief executive has little experience running an insurance brokerage. Is that a good thing? We think so.

Gregory C. Case, as we report on page 1, comes to Aon from McKinsey & Co., where he led the consulting firm's insurance and financial services practices. While Mr. Case is only 42 years old and hasn't run an insurance organization before, he clearly understands how insurance businesses operate.

Critics who view Mr. Case's inexperience in the brokerage field as a negative should recall that the CEOs of Aon's principal competitors, Marsh Inc. and Willis Group Holdings Ltd., also were outsiders when they joined those companies. Acumen in business, we think, is a more important quality than experience running an insurance brokerage.

While Mr. Case may lack experience running a big publicly held company, as a leader at one of the nation's premier management consulting firms, he certainly brings with him ample experience in analyzing what makes organizations successful.

And being an outsider will be positive if Mr. Case brings a fresh perspective and new ideas, rather than feeling bound to preserve traditions. After the bloodletting brought on by the allegations of steering and other improprieties, the insurance industry definitely needs new blood.

It goes without saying that Mr. Case has his work cut out for him. Aon has struggled to achieve the stated goals of its acquisition spree in the 1990s—for example, better results for clients and shareholders. The business that Patrick G. Ryan built into the world's second-largest retail broker, despite numerous restructurings, is lagging behind its peers.

And, like other brokers, Aon faces many challenges. It has to find new revenue sources after giving up contingent compensation.

Aon still has to restore the trust and confidence of its customers. Indeed, its reputation took a deservedly big hit when three state attorneys general outlined a litany of sins in civil suits against Aon. Its $190 million settlement is only one, albeit vital, step toward restoring the trust of clients and investors.

Can Mr. Case make the potentially painful changes needed to reverse Aon's fortunes? With Mr. Ryan still on board as executive chairman, that remains to be seen. Mr. Case says his priorities are growth, value for clients and operating discipline. Under Mr. Ryan, Aon had tremendous growth through acquisitions. The new CEO's success will be judged on whether he can achieve those other goals.

Letters

Society holds CPCUs to high standard

To the editor: In his March 28 *Business Insurance* column, "Industry's silent defense offensive," Paul Winston claims that New York Attorney General Eliot Spitzer has depicted the insurance industry as "rife with corruption" and wonders why more industry representatives haven't come to its defense publicly. One reason many of us in the industry have not is that we don't have all the facts yet.

CPCU Society President Don Hurzeler said in a recent interview, "I've heard a few defenses come out. Somebody isn't thinking. Why would you even start to defend until all the facts are out on the table?" And he's right. So I won't make defenses, either.

Instead, I'd like to share some thoughts with you about the CPCU Society's long-term commitment to adhere to the highest ethical standards. The nearly 28,000 members of the CPCU Society are bound by an enforceable code of ethics, overseen by its longstanding Ethics Committee. The Society established March as Ethics Awareness Month years ago, and the vast majority of its 153 chapters participate by focusing and learning what it means to, as every CPCU pledges, "place the interests of customers above my own."

I know the Society, along with other industry groups, quickly released statements last fall that expressed zero tolerance for illegal or other practices or policies that undermine an open and fair marketplace or jeopardize the interests of the insurance buyer. This has prompted the Society to form a special task force to understand and catalog any "corrupt" practices for member educational purposes.

Members and leaders of the CPCU Society are proud to be defined as professionals in the property casualty insurance industry. That doesn't mean the Society defends all industry practices and all industry developments. It does mean that it holds its own members to a higher standard.

James R. Marks
Executive Vp
CPCU Society
Malvern, Pa.

See LETTERS/page 15

Schillerstrom

Editorial

A good but flawed beginning

Should Congress pass the Bush administration pension funding reform package?

The short answer is yes—but not in its entirety.

There is much that we like in the measure, whose passage is needed to shield the Pension Benefit Guaranty Corp. from future massive losses and avoid either a huge increase in premiums employers pay the PBGC or a taxpayer-funded bailout of the agency.

The package includes such commonsense provisions as barring financially distressed employers with underfunded plans from boosting benefits. Obviously—and we don't know why Congress hasn't acted before on this—companies in ill health have no business increasing benefits. And it isn't fair to ask other employers, through their PBGC premiums, to help honor the commitments of other companies that, because of their weak condition, never should have made such promises in the first place.

We also like the simplification of funding rules. In brief, liabilities would have to be funded over seven years, an easy-to-understand schedule and one that would replace the various schedules set under current law.

While benefit lobbying groups are beefing about the proposed hike in the base premium employers would pay the PBGC, we think an increase from $19 to $30 per plan participant is modest, especially since Congress last raised premiums 14 years ago.

We can't, though, endorse the sweeping change proposed on how employers would measure their plan liabilities. Under the method now allowed, which we think is a good one, liabilities are valued with an interest rate equal to the four-year weighted average yield of long-term corporate bonds.

That simple and fair approach would be replaced with a complex one in which rates would be tied to plan demographics. Contrary to what the administration says, we think the benefit of a somewhat more accurate measurement of plan liabilities would be outweighed by increased complexity, which we think would drive away even more employers from the defined benefit plan system.

In all, though, the administration package is a good one from which to start discussions. We hope Congress starts those discussions soon and produces a legislative package that can restore the PBGC's financial position to good health, while encouraging employers to retain their pension programs.

Business Insurance

Vice President/Publisher: Martin J. Ross III (New York)
Editorial Director: Paul D. Winston (*Chicago*)
Editor: Regis J. Coccia (*Chicago*)
Editor-at-Large: Jerry Geisel (*Washington*)
Managing Editor: Gavin Souter (*Chicago*)
Assistant Managing Editor - Graphics: Kathy L. Barnes (*Chicago*)
News Editor: Matt Scroggins (*Chicago*)
Senior Editors: Michael Bradford (*New Orleans*); Roberto Ceniceros (*Los Angeles*); Meg Fletcher, A.R.M. (*Chicago*); Judy Greenwald (*San Jose*); Mark A. Hofmann (*Washington*); Dave Lenckus (*Tucson*); Douglas McLeod (*New York*); Sally Roberts (*Denver*); Joanne Wojcik (*Denver*); Rodd Zolkos—*Industry Focus* (*Chicago*)
Bureau Chiefs: Sarah Veysey (*London*)
Associate Editors: Gloria Gonzalez (*New York*)
Staff Reporter: Rupal Parekh (*New York*)
Correspondents: Carolyn Aldred (England); Elizabeth Fry (Australia)
Copy Editor/Graphics: William Murphy (*Chicago*)
Copy Editors: Mary B. Nick (*Chicago*); Joe Walker (*Chicago*)

Directory Editor: Kevin P. Edison (*Chicago*)
Assistant Directory Editor: Carrie A. Peinado (*Chicago*)
Online Editor: Kathy Downing (*Chicago*)
Online Producer: Amy R. Kepka (*Overland Park*)
Executive Assistant/Reprint Manager: Karen Brown Tucker (*Chicago*)
Editorial Cartoonist: Roger Schillerstrom (*Chicago*)
Advertising Director: Kenneth F. Luker Jr. (*New York*)
Director - Business Development : Robert L. Niesse (*Chicago*)
Interactive Sales Manager: Chris Crain (*New York*)
District Managers: Laura Booth (*Irvine*); Ron Kolgraf (*Boston*); William J. McGuire (Chicago); Robert B. Murray (*New York*); John L. Phillips (*Chicago*)
Classified Advertising Manager: Tina Vasilakis (*Chicago*)
Assistant to the Publisher: Pat Ghazvini (*New York*)
Advertising Traffic: Monique Murray (*New York*)
Production Manager: J. Thomas Janka (*Chicago*)
Circulation Manager: Kevin Scott (*New York*)
Circulation Coordinator: Craig Bowman (*Detroit*)
Director of Communications: Ronnie I. Drachman (*New York*)
Promotion Manager: Michael Ambrosio (*New York*)
Promotion Coordinator: Barbara O'Brien (*New York*)

EDITORIAL: Chicago: 312-649-5200; Denver: 303-282-4260; London: 44-207-457-1400; Los Angeles: 323-370-2455; New Orleans: 985-871-1090; New York: 212-210-0100; San Jose: 408-774-1500; Tucson: 520-579-1937; Washington: 202-662-7200
ADVERTISING: Boston: 617-292-4856; Chicago: 312-649-5276; Irvine CA: 949-255-5355; New York: 212-210-0133
SUBSCRIPTIONS: Detroit: 888-446-1422

Business Insurance is published by Crain Communications Inc.

Chairman: Keith E. Crain
President: Rance Crain
Secretary: Merrilee Crain
Treasurer: Mary Kay Crain
Executive Vice President/Operations: William A. Morrow
Senior Vice President/Group Publisher: Gloria Scoby
Group Vice President/Technology, Circulation, Manufacturing: Robert C. Adams
Corporate Director/Production & Manufacturing: Dave Kamis

G.D. Crain Jr. Founder (1885-1973)
Mrs. G.D. Crain Jr. Chairman (1911-1996)
S.R. Bernstein Chairman-executive committee (1907-1993)

Published weekly at 360 N. Michigan Ave., Chicago, Ill. 60601-3806, Fax: 312-280-3174, *biweb@crain.com*. Offices: 711 Third Ave., New York, N.Y. 10017-5806, Fax: 212-210-0704; 71121 Minkler St., Abita Springs, La. 70420; Fax: 985-871-4006; Suite 814, National Press Building, Washington, D.C. 20045-1801, Fax: 202-638-3155; 6500 Wilshire Blvd., Suite 2300, Los Angeles, Calif. 90048- 4947, Fax: 323-655-8157; 967 Bermuda Court, Sunnyvale, Calif. 94086-6750, Fax: 408-774-1155; 34 Southwark Bridge Road, London SE1 9EU, Fax: +44-(0)20-7457-1440; 8157 N. Torrey Place, Tucson, Ariz. 85743, Fax: 520-579-3476; 1746 Cole Blvd., Suite 150, Golden, Colo. 80401, Fax: 303-733-9941; 12524 Acuff Ct., Olathe, KS 66062, Fax: 312 280-3174. 77 Franklin St., Suite 809, Boston, Mass. 02110-1510; Fax: 212-210-0704. 4 Executive Circle, Suite 185, Irvine, CA 92614-6791. $5 a copy and $97 a year in the U.S., $130 in Canada and Mexico (includes GST). All other countries, $230 a year (includes expedited air delivery). Rudolf Von Bartesch, circulation manager. Four weeks' notice required for change of address. Send subscription correspondence to Circulation Department, *Business Insurance*, 711 Third Avenue, New York, N.Y. 10017-5806. Microfilm copies available: University Microfilms, 300 Zeeb Road, Ann Arbor, Mich. 48013. Microfiche copies: Bell & Howell, Micro Photo Division, Old Mansfield Road, Wooster, Ohio 44691. Portions of the editorial content of this issue are available for reprint or reproduction in other media. For reprints or reprint permission: Karen Brown Tucker, *Business Insurance*, 360 N. Michigan Ave., Chicago, Ill. 60601-3806, 312-649-5319, Fax: 312-280-3174.

BPA INTERNATIONAL
To subscribe, call 888-446-1422, or 313-446-0450 outside the United States.
www.businessinsurance.com
ABM

Certain plan designs threaten tax status of HRAs

Plan may become taxable if funds used for anything other than medical expenses

By JERRY GEISEL

WASHINGTON—Health reimbursement arrangements will lose their tax-favored status if employers allow employees or their dependents to take unused HRA balances in cash, the Internal Revenue Service says.

In Revenue Ruling 2005-24, the IRS outlines three theoretical HRA designs, each of which would permit the cash-out of unused balances. In all three situations, the IRS rejects the designs as violating both the Tax Code and earlier rules that make clear that HRA account balances, to remain tax-favored, must be limited to the reimbursement of medical care expenses.

Employer contributions to HRAs would be taxable to employees "if any person has the right to receive cash or any other taxable or nontaxable benefit under the arrangement other than the reimbursement of medical care expenses," the IRS said.

> What the IRS is saying is that the accounts, without exception, have to be used for reimbursement of medical costs.
>
> **Joe Martingale**
> **Watson Wyatt Worldwide**

In the same ruling, though, the IRS says, in situations when employees retire, their employers can make tax-free contributions to HRAs equal to the value of all or a portion of the retiree's accumulated unused vacation and sick leave. But even in that situation, the amount credited to the HRA must be used for medical-related expenses.

"You get a little extra flexibility," said Joseph Walshe, a principal in Washington in the human resources unit of PricewaterhouseCoopers L.L.P., referring to the HRA and vacation/sick-leave issue.

Still, benefit experts say, the IRS ruling affirms what had been commonly accepted understanding of the prohibition on cashing out HRA balances.

"It is completely unsurprising," said Mark Wincek, a senior partner with the law firm of Kilpatrick & Stockton L.L.P. in Washington.

Experts speculate that while the answers the IRS has provided may be obvious to many, the IRS, through the new guidance, may have wanted to make its positions even more clear, particularly to less-informed smaller employers and their advisers, benefit experts say.

"The IRS may have gotten a lot of questions on what you can and cannot do," Mr. Walshe said.

The new revenue ruling comes nearly three years after the first HRA guidance, in which the IRS gave a green light to the arrangements, as long as certain procedures are followed.

Under that guidance, the IRS said HRAs—typically linked to high-deductible health insurance plans—must be funded by employers and that account balances must be used to pay for uncovered health care expenses. Unused balances can be rolled over to pay for succeeding years' health care expenses. The plans, like health savings accounts, are rapidly supplementing or replacing more traditional and expensive plan designs in which employees have much less direct exposure to medical costs.

Rejected designs

The first HRA design rejected by the IRS in its latest guidance was one in which employees receive a cash payment equal to all or a portion of HRA account balance at the end of the year or upon termination of employment.

In the second design, unused account balances—upon the death of an employee—would be paid in cash to a beneficiary designated by the employee, or if no beneficiary were designated, to the employee's estate.

In the last situation, also rejected by the IRS, an employer offers an "option plan," which the employees can elect to enroll in prior to the start of the plan year.

Under this arrangement, unused HRA balances would be forfeited at the end of the plan year. However, the option plan provides that the employee may elect to transfer the account balance to a retirement plan or to receive the amount in cash.

None of these arrangements passes muster because in all the situations, the plans "pay amounts irrespective of whether medical expenses have been incurred," the IRS said.

What the IRS is saying is that the accounts, without exception, have to be used for reimbursement of medical costs, said Joe Martingale, national strategy health care leader for Watson Wyatt Worldwide in New York.

Most workplace violence avoidable

By Paul Viollis

As a result of the 5,500 incidents of workplace violence that occur every day, at least three people are murdered. On average, 17 workers are killed each week and 13,000 women are assaulted, stalked or murdered at work by a significant other each year. Recently, the U.S. Department of Labor reported that 2003 saw the first spike in workplace violence in three years. But even though these statistics underscore the threat posed to all U.S. companies from workplace violence, most employers are failing to mitigate the increased risk of such incidents.

While layoffs, which are the No. 1 reason for workplace violence to erupt, have reached a historical high, only 1% of the respondents to a 2004 survey by the American Society of Safety Engineers said they have written policies on workplace violence. Only 50% of the companies said they have procedures in place that employees can follow to discreetly report the red flags that signal impending violence. Further hampering the potential for preventing violence is the fact that most workers have not been trained to recognize these overt warning signs.

The vast majority of incidents of workplace violence are completely preventable if employees know what to look for and how to report it. While younger individuals and females have increasingly emerged as workplace violence offenders in the past several years—possibly a spillover from school violence—the demographic and behavioral characteristics of the individuals who typically perpetrate acts of violence have, for the most part, remained the same. Such individuals are predominately male, between 25 and 40 years of age, do not handle stress well and are chronic complainers, manipulative and socially withdrawn, among other characteristics.

The most significant difference employers should be aware of between these individuals and others is the manner in which they resolve conflict. The following are examples of recent trends in workplace violence:

> The warning signs exhibited by the typical workplace violence offender are both extremely reliable and overtly obvious to the educated eye.

- Downloading a virus into the employer's data center, disabling its operations and, ultimately, its production, causing business interruption costs that could add up to the millions of dollars.
- Tampering with an employer's product development cycle, causing a costly recall, adverse media, business interruption and a decline in stock value.
- Directing electronic or handwritten death threats at senior management and their families, prompting exorbitant security and business interruption costs.

Doing almost as much damage to the workplace is domestic violence. While domestic violence was often regarded in the past as a personal problem to be handled outside of work, it is now clear that employers must be committed to fighting it. The strongest defense in combating domestic violence in the workplace is treating it as seriously as sexual harassment. American employers have worked earnestly over the past 10 years to craft policies and train employees on the various aspects of sexual harassment while clearly defining unacceptable behavior and the ramifications for nonadherence.

The U.S. Occupation Safety and Health Administration mandates that employers foster a work environment free from potential hazard. If incidents occur and employees are hurt or killed, they or their families can sue for civil damages that can be uncapped and result in millions of dollars in damages. For example, in 2003, six workers were slain at Lockheed Martin Corp.'s plant in Meridian, Miss. Recently, a federal judge ruled that Lockheed cannot hide behind workers compensation law to deflect millions of dollars in potential damages. The trial has been set for October, and the jury will be instructed to determine if Lockheed was aware of the potential for violence to erupt but failed to take the necessary precautions to protect its employees.

For an employer to pass the test of reasonableness in providing a safe work environment, the following steps must be taken:

- Craft a comprehensive policy clearly defining and addressing the various manifestations of workplace violence, including domestic violence, while outlining unacceptable behavior and the ramifications for noncompliance. Topics such as access control, visitor escort procedures, domestic violence protocols, Americans with Disabilities Act compliance and threat mitigation procedures should be addressed in this document.
- Train all employees to recognize and report the early warning signs of workplace violence, so that the employer's security department can act before an incident occurs that is financially and emotionally costly.
- Conduct a holistic vulnerability assessment to determine the likelihood of violence to erupt.
- Ensure that security standards for the employer's premises meet best practices.

Additionally, it is imperative that risk managers hold subject-specific meetings with their insurance brokers to ensure that their organizations are effectively protected from the financial devastation that typically accompanies incidents of workplace violence. Invariably, during a post-incident briefing, the bad news is delivered to the risk manager that the costs associated with the incident are not covered, leaving an enormous unbudgeted expense. Some examples of such costs are business interruption, consultant fees for added security crisis communications, critical-incident stress management, executive protection, prelitigation support interviews and organizational rehabilitation. Conducting thorough due diligence on the front end is extremely cost beneficial.

Apart from the lone gunman seeking immediate gratification, workplace violence is completely avoidable and is never spontaneous. The warning signs exhibited by the typical offender are both extremely reliable and overtly obvious to the educated eye. Similarly, the victim of domestic violence also displays systematic behavioral indicators to those around her or him.

Is your organization prepared to recognize these signs and respond with preventive action, or will it take the loss of life to re-engineer your corporate culture to avoid workplace violence? That's your call.

Paul Viollis is president of Risk Control Strategies, a threat management and risk assessment firm in New York.

BI's coverage of Risk Management

TO MINIMIZE RISK, EVERY OFFICE NEEDS ONE.

Risk management is all about putting out fires – before they even flare up. One safe way to avoid taking chances with your own business development and client retention is by advertising in *Business Insurance's* issues devoted to RIMS 2005. Before, during and after the conference, our readers – your clients and prospects – will depend on *BI's* coverage of the hot issues, trends and developments in the risk management arena.

Don't get burned. **Please contact Ken Luker at 212-210-0133 or e-mail kluker@BusinessInsurance.com** to find out how advertising in *Business Insurance* can fireproof your marketing efforts.

April 4	**RIMS Conference & Philadelphia Tourism Preview**	Ad Close: March 23
April 18	**Risk Manager of the Year**	Ad Close: April 6
April 25	**RIMS Conference Report**	Ad Close: April 13
May 2	**RIMS Conference Review**	Ad Close: April 20

New York: 212-210-0133 | **Chicago:** 312-649-5275 | **Boston:** 617-292-4856 | **Irvine:** 949-255-5355

Business Insurance www.businessinsurance.com

Commentary

Senior Editor Mark A. Hofmann

Action is needed on TRIA solution

Congress has already begun considering whether the Terrorism Risk Insurance Act, currently slated to sunset on Dec. 31, should be extended for an additional two years.

While many knowledgeable people I've spoken with expect lawmakers to extend TRIA, no one expects them to do so quickly. In fact, House leaders appear likely to keep the extension on ice until the Treasury Department issues its long-awaited report on the terrorism insurance marketplace. That report, required by law, does not have to be issued until June 30.

Even with the delay and even with the likely fallout from continuing investigations into industry misconduct, the extension still looks probable. But merely giving TRIA an additional two years is far from enough to address the underlying issue of terrorism coverage.

Face it: in all probability, the most lawmakers will do is grant a one-shot, two-year extension. House Financial Services Committee leaders said as much last fall, when that panel unanimously approved a two-year extension that ultimately went nowhere.

That's understandable. TRIA was designed to accomplish two goals—make coverage available and allow the emergence of a private terrorism insurance market. Everyone agrees that TRIA has achieved the first goal. The second goal, though, has been elusive.

And it's likely to remain so for the foreseeable future. Unlike natural disasters, manmade disasters are extremely difficult, if not impossible, to underwrite. Throw in such variables as biological and nuclear attacks, and any pretense to terrorism being an insurable risk goes out the window.

A truly devastating nuclear attack in, say, New York's financial district, could end up causing more damage than the property/casualty industry has surplus and capital to cover, particularly when factors such as workers compensation payments are considered.

That leaves lawmakers with some pretty stark options.

One, do nothing and hope new commercial activity doesn't cease in certain parts of certain cities. This is called wishful thinking.

Two, do nothing with the implicit understanding that the federal government would pick up the bulk of the cost of reconstruction. This option should be less attractive than the current TRIA arrangement, under which individual insurers accept quite a bit of risk and promise to pay back the government's contributions over time.

Three, devise some sort of long-term public-private partnership that recognizes the unique nature of the terrorism risk.

Of the three options, only the third merits serious consideration. It pains me to say that, because I'm generally skeptical of government intrusion into economic matters. Ideally, the private sector could cover the exposure all by itself.

But in an ideal world, there wouldn't be any terrorists, either.

Given our imperfect world, a long-term plan is needed as soon as possible—preferably before the end of this year. Anyone who followed the year-long campaign to enact TRIA knows that Congress acts neither quickly or smoothly on issues with which it has little experience, and property/casualty insurance is one of those issues.

It's not that insurance industry figures aren't aware of the urgency of the task. Just last week, American Insurance Assn. President Bob Vagley called for a long-term approach in a Perspective piece published in *Business Insurance* (*BI*, April 4). And only a few weeks before that, Ron Robinson, a Los Angeles lawyer who chairs the Defense Research Institute's TRIA subcommittee, outlined a possible approach in another Perspective piece (*BI*, Jan. 17).

What's needed is a consensus plan, and I don't pretend to be enough of an expert on the finer points of catastrophe underwriting to spell out which risks should be dealt with by the private sector and which should be backed by the public sector. But I do know that for a consensus plan to work, there's going to have to be a good deal of policyholder input.

Coming up with a politically viable solution isn't going to be easy, but it is doable, particularly in light of how quickly the insurance industry rallied in October 2001 behind a single terrorism insurance proposal that drew from the individual approaches of many groups. To use a phrase popularized by the late futurist Herman Kahn, it involves, in part, an exercise in "thinking about the unthinkable." But insurers, reinsurers and, above all, policyholders have to think about it, and soon. Dec. 31, 2007, is going to be here a lot faster than many would like to think.

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

PRODUCTS & SERVICES

Travis Software offers online COBRA product

HOUSTON—Travis Software Corp., a benefit information systems provider, has introduced an Internet-based system for the administration of Consolidated Omnibus Budget Reconciliation Act programs patterned after its server-based TravisCobra system.

WebCOBRA.com allows employers and administrators to perform COBRA administration online, rather than on a server-based system. Houston-based Travis' new online program provides users with ease of use and portability. It includes all of the functions of TravisCobra but, because it is Internet-based, allows for more capabilities, such as performing COBRA administration from any Internet-accessible personal computer.

Some of the features include the ability to automatically generate COBRA notification letters and enrollment forms for each covered qualified beneficiary; the customization of all letters and forms using built-in word processing software; the calculation of a 2% administrative fee; the coordination of state-mandated continuation with federal COBRA continuation; and the generation of late-payment notices.

For more information, contact Garth Williams, vp-marketing, at 866-802-2312 or visit the Houston-based company's Web sites, at *www.webcobra.com* or *www.travisoft.com*.

GE Insurance targets bed and breakfasts

KANSAS CITY, Mo.—GE Insurance Solutions has partnered with NAIS Inc., a Mount Airy, Md.-based multiline insurance agency, to offer a coverage program for bed and breakfast establishments.

The NAIS Innkeepers Program provides building, contents, business income, mechanical breakdown, crime and general liability coverages. It is available to bed and breakfasts, country inns and guesthouses, among others. Kansas City, Mo.-based GE Insurance Solutions has an exclusive arrangement with NAIS for this program.

The available limits for general liability are $1 million per occurrence and $2 million aggregate.

For more information, visit GE Insurance Solutions' Web site, at *www.geinsurancesolutions.com.*

Company issues global insurance market report

DUBLIN, Ireland—Research & Markets, a provider of international market research and data, is offering "The Global Insurance Handbook 2005."

The publication focuses on legislation and insurance law and provides analysis and advice on trends, industry standards and the importance of good risk management. The handbook also includes market reviews on the insurance developments in locations such as Brazil, Japan, Spain, Sweden and the United States.

More information can be obtained by visiting the Web site of Dublin, Ireland-based Research & Markets, at *www.researchandmarkets.com/reports/c13729*.

ACE USA adds new accident product

PHILADELPHIA—ACE USA has expanded its occupational accident product by offering employer liability coverage for Texas private employers that opt out of the Texas Workers' Compensation program.

Private employers in Texas have the option of not participating in the state's workers compensation system. Philadelphia-based ACE USA is now offering the Primary Employer Indemnity product for the Texas nonsubscriber market. The PEI product provides occupational accident and employer liability coverages. Optional benefits include owned aircraft coverage, pilot and crewmember coverage and the waiver of subrogation.

Limits up to $10 million per occurrence, as well as combined single limits up to $1 million per covered person, are available. Policy aggregates are available up to $25 million.

For information, visit *www.aceaccidentandhealth.com.*

Best updates online risk management offering

OLDWICK, N.J.—A.M. Best Co. Inc. has updated its online risk management resource, "Best's Underwriting & Loss Control Center," with new and revised articles.

The online tool provides detailed articles and on-site inspection checklists for commercial and industrial classifications for risk managers, loss control consultants and insurance underwriters to assess risk and loss exposure. The latest update includes revised articles on aerial application contractors, fruit juice manufacturers, hog confinement centers, horse breeding farms and nail salons. New articles on swim clubs and swimming pools have also been added.

For more information, contact the Oldwick, N.J.-based company's customer service department at 908-439-2200, ext. 5742. More information can also be found at *www.ambest.com/sales/buglosscenter*.

We'd like to report on new risk management and employee benefit products and services offered by your company. Send information about your new offerings to: Carrie A. Peinado, Business Insurance, 360 N. Michigan Ave., Chicago, Ill. 60601-3806; telephone: 312-649-5313; fax: 312-649-7801; e-mail: cpeinado@businessinsurance.com.

Lloyd's profits down but market stable

By SARAH VEYSEY

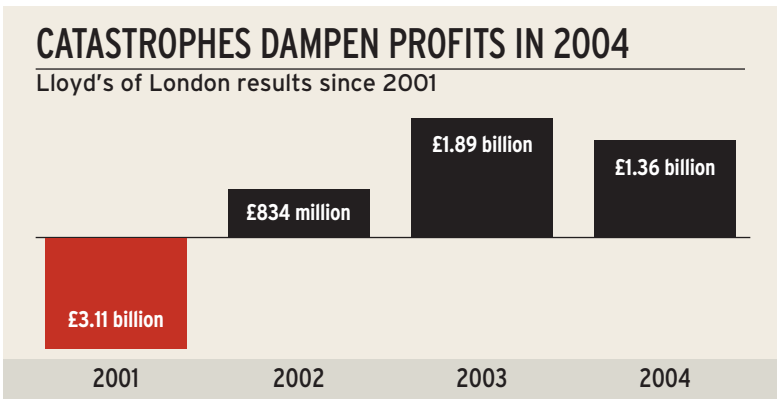
LONDON—Lloyd's of London reported lower profits and premiums for 2004 as losses from the hurricanes that hit the United States last year, a settlement over a disputed reinsurance contract for the market and lower premium rates all took their toll.

But despite the 28% drop in profits, compared with 2003, to £1.36 billion ($2.58 billion) the market remains stable.

Nick Prettejohn, chief executive at Lloyd's, said it was too early to predict what would happen to rates during 2005.

But Miles Trotter, an analyst at A.M. Best in London, said that rates were expected to soften during 2005. Nevertheless, he noted, Best believes Lloyd's can achieve a combined ratio of below 95% for 2005.

Mr. Prettejohn said that underwriting conditions were strong in 2004, but results were dampened by the storm losses, which included £1.33 billion ($2.54 billion) in claims from the U.S. hurricanes. He noted that, by comparison, 2003 was a fairly benign year in terms of large losses.



Lloyd's combined ratio for 2004 was 96.9%, up from 90.7% in 2003.

Luke Savage, director of finance and risk management at Lloyd's, said that 2004 was the second costliest year for catastrophes in the market since 1994. The costliest catastrophe year was 2001 when Lloyd's was hit by £2.66 billion ($3.86 billion) in catastrophe claims, largely from the Sept. 11, 2001 terrorist attacks in the United States.

For 2004, Lloyd's reported gross written premiums of £14.71 billion ($28.10 billion), down 10.4% compared with 2003.

"We see (this reduction) as a good thing, a positive sign, an indication that the market is underwriting for profit," not volume, Mr. Savage said.

In addition to catastrophe losses, Lloyd's 2004 results also were affected by the March 2005 settlement of a long-running dispute with the reinsurers of its Central Fund for £152 million (*BI*, March 21).

The policy, purchased in 1999, was intended to meet unrecovered losses to the Lloyd's Central Fund when those losses exceeded £100 million ($192.6 million) in any one year, subject to a £350 million ($674.1 million) limit. The aggregate maximum payout over the policy period was £500 million ($963 million).

However, the reinsurers, led by SR Business International Co. Ltd., a unit of Swiss Reinsurance Co., refused to pay some claims related to Lloyd's U.S. trust funds, saying that the policy was not intended to cover those payments, sources say.

Lloyd's said that the impact of the settlement on the Central Fund was about £226 million ($431.6 million), and that this contributed 2.7% to the market's combined ratio for 2004.

Mr. Prettejohn declined to comment on whether Lloyd's was considering legal action against the brokers of that policy, Aon Ltd. and

See LLOYD'S / page 14

Finite reinsurer Inter-Ocean shuts doors, enters runoff

By DOUGLAS McLEOD

HAMILTON, Bermuda—Finite risk reinsurer Inter-Ocean Holdings Ltd. has ceased underwriting and will run off the business of reinsurance units in Bermuda and Ireland.

"After much consideration, the board of directors of Inter-Ocean has decided to put the company into voluntary runoff," an Inter-Ocean spokeswoman said. "Current management will be retained in order to direct the company's runoff operations."

The spokeswoman declined to comment further on the decision, though analysts have cited the mounting regulatory scrutiny of finite reinsurance as a potential roadblock to Inter-Ocean's future business prospects.

In recent months, the Securities and Exchange Commission and New York Attorney General Eliot Spitzer have subpoenaed several insurers and reinsurers for information regarding finite transactions. A.M. Best Co. downgraded Inter-Ocean's financial strength rating in February to A- from A, citing the impact of the regulatory pressure on Inter-Ocean's ability to "generate deal flow," among other concerns.

Best downgraded the reinsurer again to B++ and withdrew the rating yesterday at Inter-Ocean's request following the company's decision to enter runoff.

Inter-Ocean is owned by 11 insurance and reinsurance companies (see box) that have helped produce much of its business and that act as 100% retrocessionaires of its two units, Inter-Ocean Reinsurance Co. Ltd. of Bermuda and Inter-Ocean Reinsurance (Ireland) Ltd. The two units thus retain no net underwriting risk and have collected only fees and, in some cases, profit commissions on the business they assume, analysts say.

Inter-Ocean deals have already caused trouble for one of these shareholders: RenaissanceRe Holdings Ltd. is restating its earnings for 2001 through 2003 after concluding that it accounted improperly for transactions with the reinsurer, according to RenaissanceRe's 2004 10-K report filed last week with the Securities and Exchange Commission.

The problems stemmed from a 2001 aggregate excess of loss reinsurance agreement under which RenaissanceRe ceded business to Inter-Ocean, along with a second deal under which it agreed to sell reinsurance recoverables to Inter-Ocean. While RenaissanceRe treated the excess of loss contract as traditional reinsurance, the two deals should have been considered together; in combination, they "lacked the necessary risk transfer" to be considered reinsurance, RenaissanceRe concluded after an internal review.

The effect of the restatement is to increase RenaissanceRe's 2003 net income by $1.3 million, reduce its 2002 net income by $21.9 million and increase its 2001 net income by $20.6 million, the company reported.

RenaissanceRe's outside directors also concluded that several senior executives, including Chief Executive Officer James Stanard, "made mistakes and in some instances lacked due care" in accounting for the Inter-Ocean deals, according to the 10-K.

A RenaissanceRe spokeswoman declined to comment.

Inter-Ocean's 11

The 11 Inter-Ocean shareholders are:

- Associated Electric & Gas Insurance Services Ltd.
- American Re-Insurance Co.
- Converium Holding Ltd.
- Federal Insurance Co., a unit of Chubb Corp.
- GMAC Insurance Holdings Inc.
- Hannover Ruckversicherung A.G.
- Platinum Underwriters Holdings Ltd.
- RenaissanceRe Holdings Ltd.
- Swiss Reinsurance Co.
- Westfield Insurance Co.
- XL Capital Ltd.

Canadian CFOs see pension deficit crisis continuing: survey

By GLORIA GONZALEZ

The number of Canadian chief financial officers who believe the country's pension deficit crisis will persist has more than doubled since last year, according to a study.

The percentage of Canadian CFOs who said problems in the pension system are widespread and will continue beyond the next few years rose to 43%, compared with 20% in 2004, according to preliminary results from a survey jointly conducted by Watson Wyatt Worldwide and the Conference Board of Canada.

The number of CFOs who said the problems are widespread, but largely cyclical and unlikely to become permanent, decreased from 39% in 2004 to 23% this year.

Several past studies have indicated that the majority of defined benefit pension plans in Canada are underfunded, forcing plan sponsors to make sizeable pension contributions.

Currently, 57% of the CFOs said their companies are making the required minimum contributions to their pension plans, compared with 32% that are contributing more than the minimum, according to the study.

The CFOs said the top threats to defined benefit pensions are the volatility of future contribution levels (67%) and the imbalance between pension funding and benefits (57%).

The CFOs consider most threats to the sustainability of defined contribution plans to be minor, except for a lack of investment knowledge among members—cited as a major threat by 47% of respondents.

More than 64% of CFOs said the adoption of a single pension regulator would strengthen the pension system. In addition, about 60% supported raising the "excess surplus" threshold—currently at 10%—which would allow plan sponsors to save excess surplus funds for times when their pension plans are in a more precarious funding position.

The survey collected responses from 77 chief financial officers.

The survey is available at *www.conferenceboard.ca/press/2005/Pensions.asp*.

Updates

India removes tariffs from hull business

Insurers writing marine hull business in India have gained some rating freedom. The Insurance Regulatory and Development Authority removed the line of business from its list of tariffed coverages on April 1. Insurers now are allowed to write the coverage on a file-and-use basis. Regulators will require insurers to indicate a minimum net premium rate for marine hull insurance and underwriters will not be allowed to write the business below that level.

European insurers show profit in 2004

Most European insurers recorded profit growth of more than 15% for 2004 because of improved underwriting results, among other factors, according to Standard & Poor's Ratings Services in London. Although rates began to soften for most lines of insurance in 2004, underwriting results likely won't be materially affected until 2007, the rating agency notes. S&P said it expects growth in written premiums to slow, or even fall, in 2005, reflecting insurers' efforts to manage the underwriting cycle.

Japan quake third most expensive: GIA

Insured damages from the earthquake that struck Japan's Fukuoka Prefecture last month will reach at least $146.2 million. The General Insurance Assn. of Japan in Tokyo ranked the magnitude 7.0 quake on March 20 as the third most expensive since it has kept records on insured damages caused by earthquakes. The costliest earthquake ranked by the GIA was the Great Hansin-Awaji quake in 1995, which cost insurers around $720 million. The Fukuoka quake has so far produced 16,893 claims from 18 insurers, according to the GIA.

U.K. pension regulator begins operations

The U.K.'s Pension Protection Fund and the new Pensions Regulator began operations last week. The Pension Protection Fund, loosely modeled on the U.S. Pension Benefit Guaranty Corp., has been set up to safeguard the pensions of defined benefit plan members whose sponsoring employers go bankrupt and leave their pension plans underfunded. The London-based Occupational Pensions Regulatory Authority was replaced by a new Pensions Regulator. One of the objectives of the Pensions Regulator is to prevent situations that cause claims for compensation from the Pension Protection Fund from arising, it said in a statement.

AIG: Spitzer says insurer cooperating, civil resolution possible

Continued from page 3

transaction to investigators—along with details of several other General Re deals unrelated to AIG—in response to an SEC request for information, according to a person familiar with the inquiry.

Midlevel General Re executives, meanwhile, altered documents related to the AIG loss portfolio deal about two months after it was completed, changing details of a fee, initially set at $5 million, that AIG was to pay General Re for the business, the New York Times reported, citing information from executives with direct knowledge of the transaction.

Following Mr. Greenberg's departure, AIG last week admitted to a number of accounting errors, among them its treatment of the General Re loss portfolio deal. AIG also said it may have improperly treated Barbados-based reinsurer Union Excess Reinsurance Co. as an unaffiliated entity, even though a significant part of its shareholders' interests were protected by Starr International Co. Inc., a company controlled by AIG executives. AIG further conceded that it should have treated two other offshore reinsurers—Richmond Insurance Co. Ltd. of Bermuda and Capco Reinsurance Co. Ltd. of Barbados—as affiliates.

The maximum potential impact of known errors and accounting changes would be a reduction of 2%—or $1.66 billion—in AIG's unaudited shareholders equity of $82.87 billion as of year-end 2004, the company reported. AIG has delayed its 2004 10-K filing while it reviews the accounting questions.

Within days of AIG's announcement, Mr. Spitzer seemed to put to rest fears that he might seek criminal charges against AIG itself.

"The board and current management of the company are now cooperating with this investigation," Mr. Spitzer said in a statement last Monday. "Based upon these efforts, and based upon our knowledge to date, we believe that a civil resolution with the corporation will ultimately be achievable."

Worries about an indictment of the company had been raised last month by the reported removal of documents from AIG offices in Bermuda and the destruction of certain computer records.

Last Thursday, the SEC obtained a protective order in U.S. District Court in New York requiring Mr. Greenberg, AIG and affiliate C.V. Starr & Co. Inc. to safeguard documents relevant to the SEC's investigation. In cases where there is a disagreement among Mr. Greenberg and the companies over ownership of the documents, the order prohibits documents from being removed from AIG offices.

The SEC subpoenaed Mr. Greenberg, the two companies and Starr International between March 25 and April 1, the agency reported.

In other moves related to the insurance inquiry:

- Mr. Spitzer's investigators last week interviewed executives of Munich Re about deals involving Richmond, in which Munich Re is a shareholder.
- Mr. Greenberg resigned as director and nonexecutive chairman of reinsurance holding company Transatlantic Holdings Inc., in which AIG holds a 60% stake. Also resigning as directors were Howard I. Smith, former AIG chief financial officer, who was fired last month for failing to cooperate with investigators; and Edward E. Matthews, chairman of AIG Financial Products Corp.

AIG Vice Chairman Thomas R. Tizzio remains a Transatlantic director.

Carolyn Aldred contributed to this report.

Lloyd's: Profits dip in 2004, market profitable

Continued from page 13

Benfield Group Ltd., both of London.

"It is far too soon for us to comment any further on the implications of the settlement," he said.

Observers said that despite the fall in profits in 2004, the market's profitability was still strong.

"The profit falls at the upper end of the range anticipated by A.M. Best, taking into account net catastrophe losses of approximately £1.20 billion ($2.29 billion) largely incurred in the second half of 2004, and the impact of the recent settlement with Central Fund insurers, which reduced the profit by £323 million ($616.9 million) before tax," the ratings agency said in a statement.

Marcus Rivaldi, credit analyst at Standard & Poor's Corp. in London, said that while the market is softening in some lines, that softening is fragmented, so Lloyd's can hope to make another good underwriting profit for 2005.

During 2004, Lloyd's reduced its reliance on reinsurance, according to Mr. Savage. In 2004, the market spent £2.91 billion ($5.56 billion) on reinsurance, compared with £4.17 billion ($7.96 billion) in 2003, he said.

This reduction in reinsurance spending "does lend some credence to the claims that underwriting discipline has been maintained" within the market, said Andrew Hubbard, a partner at accounting firm Mazars in London.

Letters to the Editor

Continued from page 8

Insurer execs are not above the Spitzer fray

To the editor: Thanks to Paul Winston for his good March 14 article, "Industry Proves That It's Not Above the Fray." It's been most surprising to me that, except for finite risk and earnings smoothing, insurance carriers have appeared to be above the Spitzer fray. The intermediaries have clearly been the focus and specifically at the management level. More troubling is that the accountability for carrier actions has stayed principally at the underwriter level.

For example, New York Attorney General Eliot Spitzer's complaint against Aon Corp., which *Business Insurance* covered in the same issue as Mr. Winston's column, says Aon told Zurich North America it could inflate a quote for Fieldstone Investment Corp. to make up for costs related to another account. This clearly was a business decision between specifically named senior Aon and ZNA management. But only the underwriter on the Fieldstone account was terminated.

If justice and/or improved accountability were the issues, one would presume that the focus of any investigation and proceedings about customer trust would be the decision-makers. It seems to me that by stopping with a few underwriters, the perception is that the carriers had a few bad apples.

The issue of trust is not only between customers and carriers but also between underwriters and managers. The actions of senior management at the brokers and carriers prove that they aren't above the fray, either.

Rick Grossman
Aurora, Ill.

Results: Reinsurers post solid results despite catastrophes; 2005 outlook good

Continued from page 4

terms and conditions continue to be strong, pricing levels remain attractive."

While there has been some moderate softening of rates, "basically, all the gains of the past few years are holding," said Mr. Lescault. "I think 2004 itself produced good results, realizing the fact that there were four hurricanes." He noted, however, that there were four separate retentions involved, which was less costly for reinsurers than one combined event would have been.

However, reinsurers "did not do as well last year as the year before, primarily because of the cat losses they suffered this year, as well as (asbestos and environmental) and prior-year development," said Yvonne Bernard, managing senior financial analyst at Oldwick, N.J.-based A.M. Best Co.

Results reflect "a lot of continued adverse development" in liability lines from the soft market years of 1997 to 2001, said James Eck, assistant vp and analyst with Moody's Investors Service in New York. They "continue to really negatively impact the reinsurers, and as insurers continue to take charges in those lines, the repercussions are still that it flows through to the reinsurers," said Mr. Eck.

Outlook positive

The outlook for the reinsurance industry this year is positive, say most observers.

"I think that there's plenty of profitability built into the rates," said James Inglis, managing director at Stamford, Conn.-based Philo Smith & Co., an investment banking firm. "I think they're still going to show good results."

"We've got a stable outlook on the sector right now," said Fitch's Mr. Rouck. There is more downward pressure on rates than a year ago, "but we think they're still adequate to generate underwriting profit and get a reasonable return, so we don't see that changing dramatically over the next 12 to 18 months," Mr. Rouck said.

Cliff Gallant, an analyst with Keefe, Bruyette & Woods in New York, said: "I think 2005 looks like another year of strong profitability, barring a major catastrophe."

Mr. Gallant added one other trend that could develop this year is more mergers, "particularly down in Bermuda among some of the smaller, newer companies, and more capital management actions" such as stock buy-backs and higher dividends.

William O'Donnell, president of GE Insurance Solutions' Americas direct treaty reinsurance unit in Philadelphia, said although there are "certainly changes taking place" in the market, "from our perspective, we see the environment we're operating in as being pretty stable." He pointed to the increases in primary pricing and firming of terms and conditions over the past three years.

However, Cincinnati-based independent insurance analyst John L. Ward said, "The outlook, I think, is neutral to slightly negative" over the next 12 to 18 months because of softening rates.

"Officially for this sector, we have a negative outlook," said Best's Ms. Bernard. "The market is weakening, for one," she said. "The prior year development continued to emerge at significant levels," she said.

Furthermore, "You have regulatory issues," said Ms. Bernard. "We don't know where the Spitzer investigation is going. Then the investment environment continues to be weak, and asbestos seems to be emerging again," while environmental issues "which we haven't heard a lot about is also on the horizon," she said.

Watching rates

Meanwhile, observers are continuing to keep an eye on rates. Mr. Rouck said rates on U.S. risks with Florida property exposures are up 10% to 20%, those with no Florida exposures are flat to down 10%, and casualty rates are down 5% to 15%.

"It really depends on the class of business you're writing, and where the exposures are, and what the recent loss history has been like. It has a huge effect on the pricing," he said.

Observers said they are concerned in particular about directors and officers liability.

"We've seen some significant price weakening here which we do not believe is warranted by the types of losses that are working their way through the system," Mr. Lescault said.

"The reinsurance market is becoming more competitive all the time," said Mr. Inglis. "Where there's an opportunity, companies are trying to expand market share." While competition is not "willy-nilly," he said, reinsurers "are taking opportunities to grow where they can."

However, Mr. Ward said uncertainties in the market, including those surrounding the finite risk reinsurance market, reserves and the possibility of extending the Terrorism Risk Insurance Act, are "scaring companies into stronger underwriting discipline."

Largest U.S. reinsurers' 2004 results

Ranked by net reinsurance premiums written. All amounts in thousands of dollars.

Reinsurer	Net reinsurance premiums written 2004	Net reinsurance premiums written 2003	Policyholder surplus (reinsurers only)	Net income (loss) 2004	Loss & loss-adjustment expenses	Loss ratio	Underwriting expenses	Expense ratio	Combined ratio 2004	Combined ratio 2003
GE Insurance Solutions [1]	$3,585,684	$3,490,841	$6,202,238	$(220,070)	$3,941,257	107.6	$940,141	26.2	133.8	110.3
Transatlantic Re/Putnam Re	3,393,309	3,100,365	1,944,450	137,809	2,478,708	75.0	904,421	26.7	101.7	96.3
National Indemnity Co.	2,808,601	2,740,860	27,224,759	2,185,999	1,347,644	49.9	405,151	14.4	64.3	52.9
Everest Reinsurance Co.	2,800,503	2,964,501	2,093,152	175,821	2,096,762	77.4	643,876	23.0	100.4	97.2
General Re Group [2]	2,746,950	3,440,123	7,176,417	610,435	2,103,808	69.9	896,897	32.7	102.6	99.1
Swiss Reinsurance America Corp.[3]	2,139,071	1,988,501	2,647,733	(100,251)	1,899,103	94.8	460,256	21.5	116.3	138.5
Odyssey American Re/Odyssey Reinsurance [4]	2,131,351	1,911,168	1,675,858	114,173	1,517,349	72.9	591,870	27.8	100.7	96.9
American Re-Insurance Corp. [5]	1,849,985	1,583,531	3,386,035	267,945	1,713,395	95.0	526,709	28.5	123.5	103.7
Berkley Insurance Co.	1,599,717	1,396,715	1,511,628	154,797	1,123,217	71.5	406,283	25.4	96.9	92.4
Folksamerica Reinsurance Co.	993,083	889,177	917,404	(959)	712,940	76.3	272,372	27.4	103.7	95.5
Partner Re U.S. [6]	875,947	1,040,578	586,543	13,976	692,001	79.1	265,311	30.3	109.4	107.2
Platinum Underwriting Reinsurance Inc.	715,432	667,516	403,121	20,574	299,243	45.4	369,019	51.6	97.0	97.9
XL Reinsurance America [7]	546,020	427,045	1,775,407	134,968	365,942	71.8	94,892	17.4	89.2	151.3
American Agricultural Insurance Co.	484,560	492,791	331,898	11,499	356,373	77.0	115,333	23.8	100.8	97.3
QBE Reinsurance Corp.	449,410	389,652	435,588	28,564	260,501	60.1	150,631	33.5	93.6	100.0
Converium Reinsurance (North America) Inc.	348,311	763,897	349,255	(355,698)	818,000	143.6	108,128	31.0	174.6	102.4
Endurance Reinsurance Corp. of America	339,102	423,688	504,465	(41,069)	239,565	76.8	135,563	40.0	116.8	107.1
The Toa Reinsurance Co. of America	282,964	278,673	330,037	3,316	251,324	90.3	70,144	24.8	115.1	106.3
Axis Reinsurance Co. [8]	218,600	113,077	517,040	(13,957)	120,376	79.4	54,388	24.9	104.3	99.3
SCOR U.S. Group/SCOR Reinsurance Co.	136,235	347,854	505,761	(35,741)	205,672	121.6	64,261	47.2	168.8	176.3
Totals for Top 20	$28,444,835	$28,450,553	$60,518,789	$3,092,131	$22,543,180	79.9	$7,475,646	26.3	106.2	100.2
Totals for all companies	$28,759,085	$30,630,787 [9]	$61,206,795	$3,141,501	$22,781,261	79.8	$3,832,168	26.4	106.2	101.2

1) Includes the combined results of Employers Reinsurance Corp. and GE Reinsurance Corp. 2) All data presented for the North American property/casualty segment of the General Re Group. Includes certain intercompany and other adjustments. Excludes other affiliates of the Berkshire Hathaway Group.
3) Represents only part of Swiss Re Group's business and includes a number of impacts including cessions to the parent. 4) Includes combined results of Odyssey America Reinsurance Corp., Clearwater Insurance Co., Hudson Insurance Co. and Clearwater Select Insurance Co. (formerly Overseas Partners US Reinsurance Co.).
5) Includes the combined results of American Re-Insurance Co., American Alternative Insurance Corp., and The Princeton Excess & Surplus Lines Insurance Co. 6) Includes the combined results of Partner Reinsurance Co. of the US and its subsidiary PartnerRe Insurance Co. of New York. 7) XL Reinsurance America's net underwriting results consist of the net pooled share of the combined underwriting results of the XL America Group Pool. All pool members are wholly owned subsidiaries of XL Reinsurance America. 8) Excludes reinsurance business of Axis Capital Holdings Ltd. written in Bermuda. 9) Total premiums written shown for December 2003 are those reported in the December 2003 Reinsurance Underwriting Report.
Source: Reinsurance Assn. of America

Wal-Mart: Company invests in state-of-the-art digital hospital in Arkansas

Continued from page 3

systems, construct learning labs and establish a technology information center that will bring "world-class health care to the region," Ms. Chambers said.

"You'll note that we're not inventing new vaccines or finding the cure for cancer. That's not our job. But we are helping at least one health care institution transform the way it functions by using information technology to improve patient safety and applying lessons we've learned to help the hospital with fundamental processes such as medication and supply chain management," according to Ms. Chamber's written speech, which provided more detail than she gave in her spoken remarks at the NBGH meeting.

"Our goal is to create scalable systems of supply chain management for the health care industry" that are, essentially, the health care equivalent to Wal-Mart's "Retail Link," a Web-based system available to all companies that serve Wal-Mart and Sam's Club in order to facilitate communication among suppliers, distribution centers and stores.

"We're trying to find out what the health care equivalent of Retail Link would look like," Ms. Chambers said at the NBGH meeting.

"Why are we investing in health care technology with Mercy? Because we believe health care providers can benefit from tools and systems developed for private industry," Ms. Chambers' written speech explained.

She also pointed out both in her speech and her live presentation that many of Mercy's customers are Wal-Mart employees.

Mercy Health System is a nonprofit community hospital serving the 300,000 people who live throughout the four-county area that comprises northwestern Arkansas. It is operated by the Sisters of Mercy of St. Louis, according to Clark Ellison, executive director of development at St. Mary's Hospital Foundation in Rogers, Ark., the hospital's primary fundraiser.

Wal-Mart's $5 million pledge, made in April 2004, brings the hospital more than halfway to its goal of raising $40 million to build the new hospital, which is scheduled to be completed by the end of 2007, Mr. Ellison said.

Mercy's 21st-century medical campus will be anchored by a 380,000-square-foot medical center with 200 beds and emergency services. The campus will provide care in cardiology, orthopedics, neurology and outpatient services. A medical office building to accommodate 90 physicians will complete the campus.

If the project meets its projected completion deadline, it will be the nation's first state-of-the-art digital hospital meeting all of the criteria outlined by President George Bush in his vision for the future of health care. This includes electronic medical records, computerized prescription order entry and digital diagnostic imaging equipment that can transmit images over the Internet.

Wal-Mart is investing $5 million in a hospital in Arkansas that will make extensive use of technology.

"There are hospitals with bits and pieces but do not have it all together," Mr. Ellison said.

It also may be the first major hospital technology initiative funded mostly as a result of the philanthropy of a single employer, as opposed to a hospital system's own resources, institutional grants and/or insurers.

"This is a new twist on an old story, in a way. Corporations and individuals all have donated money to hospitals with a very specific purpose enumerated for the spending of the money," said Rick Wade, senior vp of strategic communications at the American Hospital Assn. in Washington.

For example, in Annapolis, Md., television game show host Pat Sajak gave "a chunk of money" to a local medical center to develop a breast health center for women, according to Mr. Wade.

There also have been instances in which businesses in a community have collectively donated funds to a hospital to develop a particular service that the hospital didn't have because they knew the community needed that service, he noted.

"But this is the first one that I recall exactly like this in the technology area," Mr. Wade said.

It also answers many health care providers' pleas that they need money up front to invest in systems that improve the quality of health care before they can meet the objectives of many pay-for-performance initiatives.

"You've got a third of the hospitals in this country operating in the red, and you've got another third getting by and another third doing OK, but every one of them has a common goal around wanting to invest in new technology. And the money for a lot of hospitals is pretty scarce," observed Mr. Wade.

"One of the things you always hear the business community complain about is the rising cost of health care. But very seldom do they step up and say, 'Wait a minute; health care is like everything else. You get quality if you invest in it,'" he said.

"Handled properly, it could be a role model," Mr. Wade added. "It's a creative way to use philanthropy to address several of the business's goals. If the business wants to be seen as a good citizen in the community, check that off the list. If they want some tangible return for their investment, if they invest in technology that improves the quality and safety and lowers the cost of care, check that off the list. And if they're beginning to do some things that are beneficial to that organization in other ways, that's good, too. For the hospital, that means they've got somebody in the community willing to step forward and say, 'We're with you.'"

Helen Darling, president of the NBGH, said she is impressed that Wal-Mart is taking the initiative in developing technology that should lead to better-quality, lower-cost health care.

"We will all learn a lot from the application of fast-moving, efficient technical assistance on systems and business processes to hospitals from businesses as successful as Wal-Mart," Ms. Darling said.

Francois de Brantes, program leader for corporate health initiatives at General Electric Corp. and president of Bridges to Excellence, an employer-led pay-for-performance program, is equally supportive.

"If Wal-Mart can find a way to improve logistics and inventory management in hospitals, I'm sure that would result in significant efficiency gains," Mr. de Brantes said.

Workers comp: Doctor networks expected to curb costs

Continued from page 4

sufficient patient volume, making it hard for networks to recruit them with discounted payments.

Physician discounts arranged by workers comp preferred provider networks can exacerbate medical expense problems when their focus is only on discounting fees, agreed Joseph Paduda, principal at Health Strategy Associates, a managed care and workers comp company in Madison, Conn. One problem is that preferred provider organizations have commonly ignored promises to direct more patients to the providers they contract with, Mr. Paduda explained.

But other observers point out that organizations that create networks, along with insurers and self-insured employers that contract for network services, are increasingly re-evaluating discounted fee strategies. Employers, though, should make sure that the networks they contract with consider utilization and not just fee discounts.

The fee amounts paid to medical providers do influence utilization, agreed Dr. Richard Victor, executive director of the WCRI. But more network companies are shifting from attempting to lower costs through discounted doctor reimbursement contracts to focusing on reducing utilization. They are doing so, where state laws allow, by limiting their networks to include only those doctors they have identified as producing good outcomes, Dr. Victor said.

Workers compensation observers generally consider good outcomes to include efficient treatment utilization, quicker recoveries and positive return-to-work results.

> "We take discounts where we can get them. If we can't get the discount, but it's a provider we really want in because of utilization, we will put them in the network."
>
> **Mark Sidney**
> **Liberty Mutual National Market**

Particularly during the past year or two, larger insurers have been redirecting their networks away from the deep-discount model, said Jean Feldman, senior vp of care management operations for Choice Medical Management Services L.L.C., a Tampa, Fla.–based workers comp care management company that provides doctor networks.

Insurers have learned that the discounted provider fee strategy will not necessarily affect medical and indemnity costs. But getting the "right physicians"–those with the most experience in treating specific workers comp injuries–will.

"Then you will have less utilization, because they know what they are doing, they will pay attention to that injured employee," Ms. Feldman said. Doctors specializing in workers comp are also savvy about cooperating with case managers and adjusters on issues such as returning workers to modified duty.

But network contract language can influence their cooperation, Ms. Feldman said. Contracts should specify certain practices, such as a time frame within which doctors must see injured patients or return case managers' calls, Ms. Feldman added.

California's size, along with the interest of its employers and insurers in reducing unnecessary utilization, will make the state a "big engine" and an innovator in the drive for networks that reduce unnecessary medical treatment, the WCRI's Dr. Victor said.

That is already happening. Liberty Mutual, for example, has transformed an existing older network of California doctors, said Mark Sidney, senior vp and general claims manager in Boston for Liberty Mutual National Market. Liberty Mutual culled hundreds of providers from the existing network. It is also recruiting new ones after profiling their practices to determine their experience in treating specific occupational injuries, their treatment utilization records and their ability to work with employers for return-to-work results.

"We take discounts where we can get them," Mr. Sidney said. "If we can't get the discount, but it's a provider we really want in because of utilization, we will put them in the network."

Liberty Mutual now has 27,000 providers under contract in California and is also implementing new measurements to internally gauge its performance under several aspects of California's reforms, including efficiencies that might stem from its provider network.

It is self-evident that managed care practices, such as the use of provider networks, have resulted in cost savings, better treatment and better outcomes in the group health arena, said Tim East, former chairman of the Sacramento-based employer group the California Coalition on Workers' Compensation.

But Mr. East agreed that some networks may be formed mostly with an eye to cutting costs rather than to improving worker recovery. That is shortsighted and could result in poorer outcomes and higher costs over the long term, said Mr. East, who is also a risk manager for the Walt Disney Co. in Burbank, Calif.

Wachovia: Bank to expand brokerage operations with Palmer & Cay purchase

Continued from page 1

11th-largest broker of U.S. business, based on $188.7 million in 2003 brokerage revenues, according to *Business Insurance's* annual rankings. Palmer & Cay ranked at No. 15, with $143.8 million in broker-

"Wachovia is committed to the business, and Wachovia has the capital to play in the arena."

Stewart McDowell
Wachovia Insurance Services Inc.

age revenues (*BI*, July 19, 2004).

The deal, whose terms were not disclosed, also should benefit insurance buyers, executives from the two firms say.

"We think it's a terrific win for the buyers," said John E. Cay III, chairman and chief executive officer of Palmer & Cay, who will become chairman of Wachovia Insurance when the deal is completed.

"We think we can accomplish more on behalf of the client together than either one of us can separately," he said.

At the same time, the combined firm will offer clients an alternative to the megabroker model, said Stewart McDowell, president and CEO of Wachovia Insurance, who will continue in his current role.

Some major brokers have sought to grow in part through the addition of nonretail operations, such as wholesale and reinsurance brokerage.

But in recent months, amid investigations into conflicts of interest in the insurance industry, some have moved to divest some of those operations, Mr. McDowell said.

"We are not encumbered with those challenges right now," he said.

"We have essentially purely a retail distribution platform; we don't have those other organizations to deal with. We take the customer straight to the market or to the intermediary that best serves the customer, not our own in-house organization," he said.

Toward this end and prior to the signing of the definitive agreement, Palmer & Cay sold its property facultative reinsurance underwriting manager, Savannah Reinsurance Underwriting Management L.L.C., to Glencoe U.S. Holdings Inc., a U.S. subsidiary of Bermuda's RenaissanceRe Holdings Ltd. And it currently is "evaluating" the future of its reinsurance brokerage unit, Palmer & Cay Reinsurance Brokerage, Mr. Cay said.

Palmer & Cay also last month sold its benefits outsourcing group, Grand Rapids, Mich.-based Outsourcing Solutions Group, to HR XCEL L.L.C. of Charlotte N.C.

Like most of its larger competitors, Wachovia Insurance and Palmer & Cay ceased collecting contingent commissions at the end of 2004, following New York Attorney General Eliot Spitzer's fraud and bid rigging suit against Marsh & McLennan Cos. Inc.

Combined reach

When its deal to buy Palmer & Cay Inc. is completed, Wachovia Insurance Services Inc. will have:

- More than $400 million in annual revenues
- Approximately 1,800 employees
- A total of 46* offices

* *BI* estimate
Source: Wachovia

Going national

With the addition of Palmer & Cay, Wachovia Insurance moves one step closer to its goal of being a national firm.

"Wachovia is firmly committed to becoming a major force in the insurance brokerage arena," Stanhope Kelly, senior executive vp of Wachovia Corp., said in a statement. "The addition of Palmer & Cay will significantly enhance Wachovia's property and casualty, and employee benefits capabilities while significantly enhancing our market coverage on the East Coast, Midwest and Southwest," he said.

"Our dream is to become the Wachovia of the insurance brokerage business…(to) achieve that size and scale within the (brokerage) industry and have that reputation for quality and integrity," Mr. McDowell said, referring to the bank.

"It's a significant combination obviously, but I think strategically, it's a very significant move for Wachovia Insurance," said Jim Campbell, a principal and head of the bank consulting practice with Reagan Consulting Inc. in Atlanta. The deal "positions them as more than just a regional player. If they want to position themselves as more of a national broker, this is a significant move in that direction," he said.

"Palmer & Cay is an industry leader with a long tradition," said Timothy J. Cunningham, a principal with OPTIS Partners L.L.C. in Chicago. The deal "bolsters Wachovia's position as a middle market, upper middle market broker. And the fact that Palmer & Cay has a fairly broad geographic footprint…enhances Wachovia's goal to be a national player," he said.

"We're a work in progress. We have a lot ahead of us to achieve that vision, but we're committed to it and Wachovia is committed to the business, and Wachovia has the capital to play in the arena," Mr. McDowell said.

Access to that capital may have ultimately enticed Mr. Cay to sell Palmer & Cay, which had been embarking on an ambitious geographic expansion plan of its own over the past several years. That plan, the goal of which was to ensure that the brokerage remains competitive, financially stable and independent, included hiring hundreds of producers from its competitors, opening offices around the country and increasing its specialization capabilities.

In 2003 alone, Palmer & Cay recruited more than 150 industry executives and consultants and established 14 new offices in key markets throughout the country.

Some observers say that the costs associated with the ambitious expansion plan ultimately became too much for Palmer & Cay and may have motivated the sale.

"The massive geographic expansion did not deliver the intended results because of the significant capital needed to bring these producers on and to open new offices as well as to defend" litigation stemming from its recruiting, said one industry observer who asked not to be identified.

Indeed, while the staff additions did allow Palmer & Cay to expand, they resulted in numerous lawsuits around the country over various producer nonsolicitation agreements. Palmer & Cay was in legal battles specifically with Marsh or Aon Corp. in Georgia, Michigan, Wisconsin, Florida and the District of Columbia.

"We can accomplish more on behalf of the client together than either one of us can separately."

John Cay III
Palmer & Cay Inc.

"I'm pleased…to report that those issues have all but gone away," Mr. Cay said. "They've virtually all settled at this point. We have a few minor things left, but it did not play into our decision" to join Wachovia, Mr. Cay said.

"We had ambitious plans for growing our company, and we grew from being a regional firm to a firm of national prominence," Mr. Cay said. "We felt when we were approached by Wachovia that it was a very good strategic fit, that it was a great cultural fit and it allowed us access to capital to build out the West Coast, which we intended to do. So we are very optimistic about what we can accomplish for our clients going forward," he said.

Management changes

Part of the management team of Wachovia Insurance is still to be determined, executives say.

This includes what role if any James B. Meathe, who Palmer & Cay recruited in early 2003 from Marsh to become its president and chief operating officer, will take. In November, he became vice chairman of development at Palmer & Cay, replacing F. Michael Crowley, who left the brokerage to become an executive vp with Hilb, Rogal & Hobbs Co. John E. "Jack" Cay IV, who was head of Palmer & Cay's New York office, replaced Mr. Meathe as president and COO.

Mr. Meathe was the subject of a noncompete lawsuit that Palmer & Cay initiated in federal court in Savannah, Ga., in 2003 against Marsh (*BI*, June 2, 2003). That suit "is coming to an end," according to Mr. Cay.

Karen J. Lehman, Wachovia Insurance's chief financial officer, has been named CFO of the combined firm. Ms. Lehman left Palmer & Cay as its CFO in 2003 to join Wachovia.

Pension correction rule expands

By JERRY GEISEL

WASHINGTON–The Labor Department is expanding a three-year-old program that waives financial penalties on employers who find, report and correct mistakes they made in administering their retirement plans before federal regulators audit and catch the errors.

Launched in 2002, the Voluntary Fiduciary Correction Program is intended to give employers a financial incentive—an exemption from fines—to comb through their plans and report and correct mistakes.

Given the complexity of federal pension rules, the potential for making mistakes is high, benefit consultants say.

"It is hard not to make a mistake. Upon review, we nearly always find mistakes that need to be addressed, many of them minor, and all of them honest, inadvertent mistakes," said Mike Boro, a principal in the human resources unit of PricewaterhouseCoopers L.L.P. in New York.

"It is amazing" how many people do not know about certain rules, concurred Kyle Brown, an attorney with Watson Wyatt Worldwide in Washington.

In its expansion, the Labor Department has made mistakes related to the administration of savings plan participant loan programs eligible for the relief provided by the correction program. Additionally, the department has proposed how employers can, without penalty, dispose of "illiquid assets" such as a property held by a pension plan for which the employer is the only buyer. Normally, such sales with a party-in-interest would be considered prohibited transactions.

Under the expansion, such mistakes as providing plan loans to participants that are greater than those allowed under the Employee Retirement Income Security Act and allowing participants to repay loans over a longer period of time than is allowed under law will be eligible for protection from penalties if found and corrected. Outstanding loans generally cannot exceed $50,000, and the maximum length of a plan loan—except for a loan used to help purchase a primary residence—generally cannot exceed five years.

For example, take a situation in which a plan administrator inadvertently allowed a participant to repay a plan loan over 10 years rather than the legal maximum of five years. To correct the problem, the monthly loan repayment schedule would have to be recalculated to enable the loan to be paid off in five years. If more than five years had passed from the time the loan was originated, though, penalty relief would not be available, and the employer and the Labor Department would have to work out a settlement.

In the case of the sale of illiquid assets—such as an office building that a defined benefit plan holds and the employer then seeks to purchase from the plan—such a transaction would be allowed, provided the plan "is no worse than if the acquisition had never taken place," the Labor Department said.

To ensure that, the plan must receive either the higher of the fair market value of the illiquid asset, as determined by an independent appraiser, or the price the plan originally paid for the asset plus incidental costs.

Aon: Insurance consultant takes over as 'boss'

Continued from page 1

that relationship.

Mr. Case's appointment caps a five-month search, during which time the brokerage settled fraud and anti-competitive practice charges in suits filed by Mr. Spitzer and the attorneys general of Connecticut and Illinois (BI, March 7). Aon agreed to pay $190 million as restitution to policyholders and to revamp its business practices to settle the suits, which charged that the brokerage steered clients to the insurers and reinsurers paying the highest contingent commissions and linked insurance placements with reinsurance brokerage business.

Aon then reached a $38 million settlement to resolve a class action lawsuit in Chicago alleging the brokerage breached its fiduciary duty by collecting contingent commissions from insurers without disclosing them to clients.

With those issues behind it, on April 4, Aon announced Mr. Case's appointment.

"Our board was determined to conduct a thorough search, and we could not be more pleased with the result," said Andrew J. McKenna, Aon's lead director and chairman of the board's search committee, in a statement. "Greg's management experience in professional services, his firsthand knowledge of the insurance industry, and his keen understanding of the complexity of global organizations make him an ideal candidate to succeed Pat Ryan, who has built Aon into the tremendous franchise it is today."

As executive chairman, Mr. Ryan said in a conference call to analysts that he will focus his efforts working with existing client relationships and developing new client opportunities, a side of the business he said he "loves" and is "excited" to spend more time on.

"Let me make this clear," Mr. Ryan said. "Greg Case is now the boss of Aon, and my role is to support and assist him in any way I can."

During an interview with *Business Insurance*, Mr. Case said he too is "excited" about his new role.

"In essence, when I thought about the parallels and the alignment between McKinsey and Aon, that is what got me incredibly excited about this opportunity," Mr. Case said. "I never intended to leave the firm. I love the firm. It's a phenomenal place. I had a very, very unique role there, and I was privileged to have had it. But the alignment between McKinsey and Aon was unbelievably compelling to me."

Mr. Case noted, for example, that both firms are advice-based and talent-driven businesses.

Parallels to business

Although he has never run an insurance brokerage, Mr. Case said he did serve on McKinsey's shareholder's operating committee, which is the group of 25 individuals that runs the 11,000-person firm. He also headed up the global insurance and financial service practices, which he likened to individual businesses.

"Over the last 12 years, I have had direct hands-on operating experience guiding the firm overall and running these two practices," he said. And while McKinsey never talks about itself, "I will tell you that, of the 17 practices at McKinsey, the practices I was fortunate to be part of were quite successful."

Mr. Case also is intimately familiar with Aon.

"I've known Pat Ryan for two or three years from a business standpoint, not socially," Mr. Case said.

"I know Aon much, much better than most will ever know Aon," he said. "That has contributed to my excitement, having been able to see the skills, the leadership and the global reach first-hand."

Future path for Aon

Mr. Case also said that he relishes the opportunity to lead Aon, given the current state of the insurance brokerage industry.

"When you think about the industry and you think about McKinsey, McKinsey doesn't play unless there is turmoil and ambiguity," Mr. Case said. "We are never engaged with clients without turmoil. That's been my life for 17 years."

"To me, I look at the turmoil and I look at the change the insurance industry is going through, and I am very respectful of the challenges here, and I approach them with a lot of humility. But I have to tell you, I see huge opportunity for Aon, and I'm incredibly excited about it."

For Aon clients who may feel as though their trust with the brokerage has been broken due to the steering allegations, Mr. Case has a simple message: "We are absolutely about client value added. We're absolutely about values and trust, and we're absolutely about creating a world class of products and services that help them create value and run their businesses. I can't speak to the past, but that is my commitment."

Though Mr. Case said it is too soon for him to outline his specific goals and priorities for the company, he said that whatever decisions he makes will emphasize growth, creating value for clients and operating discipline.

"Those three ideas…will be the three lenses that I look at as I spend time with my colleagues around Aon," he said.

Observers upbeat

Industry observers are cautiously optimistic about Aon's new leadership.

"I think Fitch, in general, views the appointment as a positive, simply because it eliminates another thing on their list of things to do and they can get on to focusing more on their business model," said Gretchen Roetzer, a credit analyst with Fitch Ratings in Chicago.

Mr. Case's status as an outsider to the industry is a positive from Fitch's perspective, Ms. Roetzer added. "Aon is clearly sending a message that they want a fresh start, a fresh view, no conflicts—very much a post-Spitzer world operation," she said. "But at the same time, he's 42 years old and he has no corporate management experience and limited insurance experience."

"I think it's good that (Mr. Case) was at the management consulting firm," said Greg Simcik, an equity analyst with Standard & Poor's equity group in New York. "He's probably got some good relationships with at least the insurance companies, and that's important. He may need a little help with the client side, which is particularly important, given all the turmoil in the industry over the last six months or so. But Pat Ryan is going to be there to help out with that," he said.

Mr. Simcik said, though, that he does have some concern about Mr. Case being a novice CEO.

"He hasn't really run a company per se, but, then again, with Pat Ryan still being on the board and being involved in at least the day-to-day business, I'm sure he's going to have someone to rely upon," he said.

"Could they have gotten a higher-profile person? It is possible that if they'd done that, it would have been received better in the marketplace," Mr. Simcik said. "But it's sort of a wait-and-see thing."

The McKinsey connection

Like Aon Corp.'s newly appointed president and chief executive officer, Gregory Case, the current and former senior executives of several other major companies first rose within the ranks as consultants at McKinsey & Co.

Over the past several years, the international management consulting firm has served as a veritable breeding ground for top executives at a wide array of companies.

Other McKinsey alumni include:

- **Gary T. DiCamillo**, former chairman and CEO, Polaroid Corp.
- **Uwe Doerken**, executive chairman, DHL U.S.A.
- **Louis V. Gerstner**, former chairman and CEO, IBM Corp.
- **Harvey Golub**, former chairman and CEO, American Express Co.
- **Ted W. Hall**, former chairman, Robert Mondavi Corp.
- **Lukas Muehlemann**, former chairman and CEO, Credit Suisse Group
- **Leo. F. Mullin**, former chairman and CEO, Delta Air Lines
- **Dr. Helmut Panke**, chairman, BMW A.G.
- **Sharon Patrick**, former president and CEO, Martha Stewart Living Omnimedia
- **Philip J. Purcell**, chairman and CEO, Morgan Stanley
- **Jeffrey K. Skilling**, former CEO, Enron Corp.
- **Anton Von Rossum**, former CEO, Fortis
- **Robert Worcester**, chairman, MORI

Willis: Probes settled

Continued from page 1

and accountability in the insurance industry. Willis Chairman Joseph Plumeri has demonstrated admirable leadership in spearheading Willis' response to the issues raised in our investigation and in implementing reforms at the company."

Client deception

The New York investigation, which began last spring as part of a broad probe of compensation practices, revealed internal communications about efforts to maximize Willis' and insurers' revenues without regard to clients' interest, the officials said in a joint statement.

Specifically, New York officials, in a 24-page "assurance of discontinuance" document issued Friday by Mr. Spitzer's office and posted at his Web site, set forth the attorney general's findings.

The document cites a 2003 initiative at Willis North America to generate $2.5 million in additional income in November and December of 2003. One of the key objectives of that drive was to maximize premium volume flow to insurers with the most attractive contingent commissions, the document states.

"I need you to drive this initiative—I want to see you directing the flow of business to these companies," James Drinkwater, managing director of Willis Global Markets in North America, said in a 2003 e-mail to Willis' regional marketing officers, according to the attorney general's findings. The document refers to Crum & Forster Corp., Chubb Corp., St. Paul Cos. Inc and Hartford Financial Services Group Inc. as insurers with which Willis had contingent revenue agreements.

Moreover, according to the assurance of discontinuance document, Willis made clear to insurers that signing contingent fee agreements would mean that Willis would steer business their way.

Also part of Willis' revenue drive was a directive to place as much business as possible through Willis' wholesale unit, Stewart Smith Group, the document states. By doing so, Willis gained a second commission when it could have directly placed the business for a single fee, the document states. Willis has since agreed to sell Stewart Smith to American Wholesale Insurance Group Inc. (*BI*, Feb. 21)

According to the attorney general's document, Willis' Florida office received $156,000 in additional income in 2003 from a fee-based account after needlessly running the business through Stewart Smith.

Willis also sought to get its Willis Re unit involved in any possible retail account and used its leverage with insurers, the document states.

The attorney general's findings in the assurance of discontinuance cited one instance where, after learning that an ACE Ltd. unit placed a reinsurance contract on a Willis retail-placed account with Guy Carpenter, MMC's reinsurance brokerage, Mr. Drinkwater called Susan Rivera, then president of ACE INA Holdings Inc., and insisted the reinsurance be placed through Willis Re. Afterward, she ordered ACE to move the business to Willis Re. Ms. Rivera, however, was not a party to the assurance of discontinuance between Willis and New York officials and as of Friday had not had an opportunity to respond to the allegations in the document. At press time, she could not be reached.

Minnesota's investigation

Simultaneous to its New York settlement, Willis agreed to settle a probe of its compensation practices by Minnesota Attorney General Mike Hatch. Last month, he hinted Willis may have violated the state's consumer protection laws in court documents seeking to compel Willis to provide information relating to his investigation (*BI*, March 14).

Specifically, Mr. Hatch said Willis may have steered clients to the insurers paying it the most contingent commissions and that it may have engaged in fraud by using Stewart Smith to "churn" additional commissions. None of these commissions appears to have been disclosed to clients, Mr. Hatch said.

Under the agreement, Willis, which admitted no wrongdoing or liability, will pay $1 million in restitution to its Minnesota clients.

A new model

As part of its settlements, Willis agreed to reform its business practices, including no longer accepting contingent commissions, which it ceased doing in October. Willis received $71 million in contingent commissions in 2004.

Willis now will accept only a specific fee paid by the client, a specific percentage commission on premium to be paid by the insurer set at the time of purchase, renewal, placement or servicing of the insurance policy; or a combination of both, according the New York settlement. Among other reforms, Willis agreed to disclose to clients all quotes and indications sought as well as received by the brokerage in connection with the coverage of the client's risk and all terms.

"We believe that the regulatory investigations have been a catalyst for positive change in the industry," Mr. Plumeri said in the statement. "We strongly support the reforms that the attorney general has advocated and we previously had voluntarily implemented many as part of our Client Bill of Rights," he said.

ADVERTISER INDEX

Issue of April 11

United Airlines: Sept. 11 losses not covered

Continued from page 4

United Airlines was trying to inappropriately expand the breadth of coverage based on the well-known facts at hand," said Jeffrey S. Weinstein, a lawyer for ISOP and partner with Mound, Cotton, Wollan & Greengrass in New York.

United and its lawyers, meanwhile, argued that policy language such as "damage" and "adjacent" was ambiguous and reasonably susceptible to varying interpretation of the coverage terms.

In his decision, New York District Court Judge Richard M. Berman focused on three main issues:

- Whether "physical damage" is a prerequisite for business interruption coverage under the policy.
- Whether destruction of United's ticket counter at the World Trade Center and damage to its ticket counter in Reagan Airport triggered systemwide business interruption coverage under the policy.
- Whether the Pentagon should be considered an "adjacent premises" to Reagan Airport under the policy's civil authority terms.

Finding the policy language to be lucid and the amount of recovery sought to be inconsistent with the actual damage suffered, the judge late last month upheld the insurer's refusal to indemnify the airline.

Lawyers familiar with the lawsuit said that the policy at the center of the case was noteworthy compared to the first-party property policies involved in other decisions related to the attacks because it specifically covered terrorism.

"United strongly disagrees with the decision and expects to be vindicated on appeal," said United attorney Peter M. Gillon, of Greenberg, Traurig L.L.P, in Washington.

Conversions: New York, New Jersey in talks

Continued from page 6

spokesman cited this factor when asked if the company would be interested in a conversion.

But in Horizon's case, there is less urgency to convert than in previous years, because the company is profitable, said Joseph Marinucci, credit analyst with New York-based Standard & Poor's Corp. In its 2003 annual report, Horizon reported a net income increase of 50% over the previous year.

"Horizon is making good money," Mr. Marinucci said. "The conversion thing doesn't carry as much weight."

Of the two companies, a HIP conversion is more likely to occur, because New York is looking to get out of a budget crisis and "converting a nonprofit is one way to do it," he said.

The state, though, would first need to pass legislation authorizing a conversion, the HIP spokesman said.

In addition, Mr. Marinucci noted that negotiations regarding the use of the assets attained from a conversion would be detailed and extensive, because New York state officials would want to ensure there would not be a repeat of the Empire Blue Cross & Blue Shield situation. New York-based Empire, a unit of WellChoice Inc., converted in 2002, with the majority of its stock designated to The New York Public Asset Fund. A lawsuit filed by the Washington-based Consumers Union, though, challenged the conversion process, and the proceeds from the stock offering—valued at about $800 million—are being held in escrow while the dispute is in litigation.

A HIP conversion "looks like it may get done," Mr. Marinucci said. "It all depends on the wrangling."

Whether the potential conversions in New York and New Jersey indicate the trend is regaining momentum remains to be seen, observers say.

"It might break up the logjam over conversions, but there are a lot of ifs there," said Joy Grossman, senior health researcher for the Washington-based Center for Studying Health System Change.

BI Stock Index [4/4 - 4/8]

Up-to-the-minute data for all 87 companies that comprise the *BI* Stock Index can be found at *www.businessinsurance.com*.

Percentage change of *BI* Stock Index vs. key indicators

***BI* Stock Index**	2387.58	▲ 1.61
Dow Jones	10461.34	▲ 0.55
S&P 500	1181.20	▲ 0.71

Largest gains

WellChoice Inc.	6.99%
Clark Inc.	6.64%
HealthNet Inc.	6.21%
Zenith National Insurance	5.39%
MBIA Insurance Group	5.21%

Largest losses

PMA Capital Corp.	-5.21%
XL Capital Ltd.	-4.24%
Tower Group Inc.	-3.64%
American Safety Insurance	-3.17%
Cincinnati Financial Corp.	-2.82%

Weekly change by market segment

Brokers	0.80%
Insurers/Reinsurers	0.52%
Managed care organizations	2.65%

Source: FinancialContent Inc. *(http://financialcontent.com)*

Late News

Continued from page 1

FASB to revisit risk transfer rules

The Financial Accounting Standards Board, which determines generally accepted accounting principles, voted last week to re-examine its criteria for risk transfer in finite insurance and reinsurance contracts. The issue has gained recent attention in connection with the investigations of insurers' accounting. FASB's FAS 113 allows a U.S. company to account for a contract as reinsurance only if it transfers significant underwriting risk; however, observers have noted there is a gray area in terms of determining when adequate risk transfer has occurred.

North Dakota rejects discriminatory RRG bill

North Dakota legislators gave final approval to legislation requiring auto dealers and distributors selling vehicle service contracts to purchase reimbursement policies from insurance companies that meet certain financial standards. The action came after a House-Senate conference committee rejected a Senate-passed measure that the risk retention group industry vigorously opposed, arguing that it would effectively exclude RRGs from the reimbursement policy market by mandating the purchase of coverage from insurers in the state guaranty association. RRGs cannot be members of those associations.

APIW honors RAA's Cohen

Marsha Cohen has been named the 2005 Insurance Woman of the Year by the Assn. of Professional Insurance Women. Ms. Cohen is the senior vp-state relations and director of education for the Washington-based Reinsurance Assn. of America. Ms. Cohen, who joined RAA in 1992, is a former APIW president and was named one the 100 Leading Women in Insurance by *Business Insurance* in 2002. Ms. Cohen will be honored by the APIW at a ceremony on June 8 in New York.

Bias case brings $29 million award

Swiss bank UBS AG must pay a former employee $29.2 million in damages for sex discrimination and illegal retaliation, a federal jury in New York ordered last week. UBS denies the claims and said it plans to appeal the decision, which awarded the plaintiff $9.1 million in compensatory damages and $20.1 million in punitive damages. The sum is believed to be the largest-ever jury award in the United States to an individual plaintiff in a bias case.

Bias suit against Willis gets class action status

A gender bias lawsuit against broker Willis Group Holdings Ltd. and several of its subsidiaries has been granted class action status. Filed in a New York district court in July 2001, the suit represents a class of 200 women who allege that London-based Willis systematically discriminated against them with respect to promotions and compensation.

Health plan alliance targets Mich. employers

CIGNA HealthCare and Detroit-based Health Alliance Plan have formed a marketing affiliation to offer national, open-access products to midsize and large employers with sites in Michigan and other states. Employers that purchase the affiliation offerings will have access to HAP's network of physicians and hospitals in southeast Michigan as well as CIGNA's extensive national network. In December 2004, CIGNA HealthCare announced a similar strategic alliance with New England-based Tufts Health Plan.

Obesity costly to employers: Study

Obesity and inactivity cost California $21.7 billion annually, with employers bearing about three-quarters of cost burden, according to a state Department of Health Services study released last week. The costs include $10.2 billion in direct and indirect medical expenses, workers compensation expenses totaling $338 million, and $11.2 billion in lost productivity, according to the report, "The Economic Costs of Physical Inactivity, Obesity and Overweight in California Adults."

Briefly noted

W. Dave Brining, one of the founders of Max Re Capital Ltd., has retired to pursue personal interests. He will continue to be involved with the Bermuda-based company, providing occasional consulting services....Tropical Storm Risk, a London-based consortium of insurance industry experts and academics, said there is an 80% chance of an **above-average 2005 Atlantic hurricane season**.

At businessinsurance.com

- New **Opinion Poll:** Will finite-risk products continue to be sold in the future?
- Items in the Late News column originally appeared in *BI*'s Daily News feature on *www.businessinsurance.com.* Visit the *BI* Web site to sign up to receive *BI*'s Daily News by e-mail. Information on online stuff

AIG®

IN CLAIMS MANAGEMENT, SIZE AND EXPERIENCE MATTER.

Over the last ten years, corporations have experienced an alarming increase in the severity and number of claims brought against them. If your company is insured by a carrier with weak claims support, you run the risk of being a victim of a crippling jury award or, at the very least, increased risk management costs. The AIG companies' claims expertise and financial strength can help any corporation control these problems.

- *No other insurance organization* is more aggressive in pursuing the best claims results for their clients.
- *No other insurance organization* has as many dedicated claims experts.
- *No other insurance organization* gives their clients better access to top legal firms.
- *No other insurance organization* has access to the financial strength of the AIG companies.

Having the AIG companies manage your claims may seem like an unfair advantage, but only if you're the other guy.

Visit us at RIMS booth #1721,
call your insurance broker or contact us
at claimsmanagement@aig.com

AIG® WE KNOW RISK.®