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APIW salutes Abraham as Woman of the Year / 3

California comp reforms slow to yield savings/ 4

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PHOTO, HURRICANE MITCH: NOAA; PHOTO, WILLIAM GRAY: AP WIDE WORLD

Storm warning activity increases

William Gray

Gray, others offer early look at hurricane risk

By MARK A. HOFMANN

The importance of long-range hurricane forecasts can be considerably more psychological than practical.

Forecasts such as those offered by William Gray, who heads a team of forecasters at Colorado State University's Department of Atmospheric Science, serve to underscore the threat presented by hurricanes, risk managers and insurers say. Long-range forecasts, however, don't have much impact on the day-to-day practice of risk management, they say.

But looking ahead, the science that's being constantly upgraded by Mr. Gray is expected to pay dividends.

The Colorado State University team has been forecasting hurricane activity by using a variety of climate and historical measurements. These include such factors as ocean circulation patterns, atmospheric conditions and the presence of such phenomena as El Niño or La Niña.

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Late News

Mississippi approves tort reform measure

Mississippi Gov. Haley Barbour has said he will sign a comprehensive tort reform measure that won final legislative approval last week. Gov. Barbour, a Republican, had called the Legislature into special session last month to complete work on the tort reform package. The measure—H.B. 13—will, among other things, cap noneconomic damages at $1 million, tie punitive damages to a defendant's net worth and replace the system of joint-and-several liability in civil cases with a system based on pure allocation of fault.

Gov. Barbour

Microsoft announces benefit cutbacks

Microsoft Corp. will introduce copayments for some prescription drugs, reduce discounts in its employee stock purchasing plan and narrow the time window for taking parental leave in curbs to its historically generous benefits package. Among the changes, beginning Jan. 1, 2005, the Redmond, Wash.-based software giant will introduce a $40 copayment for brand-name drugs when there is a generic equivalent. Microsoft says it will continue to pay the entire cost of generic drugs and brand-name drugs that do not have a generic equivalent. Microsoft expects that the changes will generate $60 million in savings.

HMO rate hikes down from 2003: Hewitt

U.S. employers negotiating health plan rates for 2005 are seeing average health maintenance organization rate increases of 13.7%, according to Hewitt Associates L.L.C. While remaining in double digits, HMO rate increases are showing signs of moderating from the 17.5% reported at this time last year, said Ken Sperling, market leader for the Eastern region of Hewitt's health management practice. The average HMO rate hike for coverage in 2004 ultimately

See LATE NEWS/page 27

Delay on vote may improve class action bill's outlook

By MARK A. HOFMANN

WASHINGTON—Supporters of class action reform are hopeful that the Senate's delay in considering a major reform bill will actually help their case.

Senate Majority Leader Bill Frist, R-Tenn., had initially scheduled a June 1 vote on whether to invoke cloture and limit preliminary debate on S. 2062, the Class Action Fairness Act. The bill would, among other things, allow the removal to federal court from state court of certain class actions involving defendants and plaintiffs

See CLASS ACTION/page 6

Pay for performance of doctors still limited

By JOANNE WOJCIK

Health care pay-for-performance initiatives spearheaded by employers and insurers in various parts of the country are beginning to pay off.

The programs, some of which were launched in response to a 2001 report from the Institute of Medicine that criticized the health care delivery system, provide financial incentives to doctors who meet certain performance criteria. And at least one of the quality-improvement efforts already has produced savings for its sponsors.

But pay-for-performance initiatives so far have been fairly modest, limited mainly by a lack of financial resources. There are only a few employer/insurer joint initiatives, though individual insurers in some states have their own programs, sources say.

For the pay-for-performance movement to grow outside of its test areas, more employers would have to put some money on the table, which wouldn't be easy in today's economy and with health care costs still soaring, those involved in the initiatives say.

Last week was the deadline for health plans and medical groups participating in the nation's oldest and largest pay-for-performance initiative to submit data regarding their 2003 performance, which will determine 2004 incentive payments.

The program, P4P, which is managed by the Walnut Creek, Calif.-based Integrated Healthcare Assn., began in 2000. However, 2004 is the first year it will make actual payments to providers, according to Tom Williams, executive director of the IHA.

"Because it's so big, there was a strong desire to test the measures first," he explained. "2002 was a test year to give groups time to develop their processes so they'd have a good shot at perform-

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NEWSPAPER

Spotlight report

LONDON MARKET REPORT

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Units of AIG, Aon dispute purchasing group cover

By DOUGLAS McLEOD

BOSTON—Two American International Group Inc. units are seeking a court ruling that they are not liable to an Aon Corp. underwriting subsidiary for more than $35 million in losses under a commercial property owners liability program.

AIG's Lexington Insurance Co. in Boston and New York-based National Union Fire Insurance Co. of Pittsburgh, Pa., filed suit late last month against Aon's Virginia Surety Co. Inc. in U.S. District Court in Boston.

The dispute revolves around whether numerous policies issued by the AIG units to members of a national property owners' purchasing group are excess policies or whether the two insurers acted as co-primary underwriters with Virginia Surety.

While Lexington and National Union argue that they provided coverage only in excess of a $250,000 retention underwritten by Virginia Surety, the Aon unit asserted four years after the program's inception that the three insurers together wrote pro-rata primary coverage and that the AIG companies owe Virginia Surety $35.7 million for paid losses and expenses, according to the lawsuit.

The complaint seeks a declaratory judgment that the AIG policies do not offer primary coverage and that Lexington and National Union do not owe the claimed amounts.

An Aon spokeswoman and a lawyer representing the AIG insurers declined to comment on the suit.

National Union started writing excess liability coverage for members of the National Coalition of Property Owners & Managers/Insurance Purchasing Group Assn. in May 2000, according to the complaint.

National Program Services Inc., a now-defunct Hanover, N.J., insurance broker, produced the program. In a case unrelated to the coverage dispute, NPS principal Vito Gruppuso pleaded guilty in January to state charges that he pocketed more than

See DISPUTE/page 27

APIW Insurance Woman of the Year

United Educators CEO honored for commitment

By GLORIA GONZALEZ

When Janice M. Abraham reflects on her career, the president and chief executive officer of United Educators Insurance appreciates just how far women have come in the business world in the past 20 years.

However, Ms. Abraham is still one of only a handful of female CEOs in the male-dominated insurance industry. "When women begin to head top insurance companies, that will be a real milestone," she said.

Ms. Abraham is the head of United Educators Insurance, a Reciprocal Risk Retention Group. The company, which is based in Chevy Chase, Md., has "made a very real commitment to identifying and promoting women within our ranks," she said. Indeed, two-thirds of United Educators' professional

Ms. Abraham

staff and close to 40% of its board members are women.

This commitment to supporting and advancing the careers of women in the insurance industry is one reason why the Assn. of Professional Insurance Women Inc. has named Ms. Abraham the APIW Insurance Woman of the Year.

"She's a strong advocate for women's advancement, which she has made a reality in her own company," said Ellen Thrower, professor and executive director of the School of Risk Management, Insurance and Actuarial Science at St. John's University in New York, who nominated Ms. Abraham for the award. Ms. Abraham will receive the award at a June 8 reception in New York.

Although there is room for improvement, the business community has become more receptive to women in its ranks than it was when Ms. Abraham began her career more than 20 years ago, she said. "The hurdles earlier in my career were much more significant

See APIW/page 6

PHOTO: EPA/HO

The energy insurance market is wary of efforts to reform Saudi Arabia's insurance regulations.

Saudi Arabian reforms may limit foreign role in insurance programs

By PETA MILLER

RIYADH, Saudi Arabia—International insurers and brokers this week will seek clarification from authorities in Saudi Arabia about recently introduced insurance regulations that they fear could limit the capacity available to foreign energy companies and other companies with large exposures in the country.

While international observers generally welcome the introduction of formal insurance regulations in Saudi Arabia, they say that if the provisions of the law are rigorously enforced—including ones limiting the extent of foreign involvement in insurance programs—Saudi insurers would not have sufficient capacity to cover some of the risks in the country that are currently mostly insured by international markets.

However, several observers are confident that while the local coverage provisions of the law will be enforced for personal lines and small commercial risks, the law will be modified to accommodate the transfer of large risks to international insurers.

The Saudi Arabian Monetary Agency, the country's Riyadh-based financial regulator, published the Cooperative Insurance Companies Control Law earlier this year and recently produced implementing regulations.

While the law theoretically applies to insurance transactions in Saudi Arabia, few of its provisions are being enforced by authorities, observers say.

The First Saudi Insurance Forum, organized by BNG Financial Advisors Group in association with SAMA, is set to take place this week in Jeddah to look at the provisions of the law in detail. Foreign insurance-related

See REGULATIONS/page 23

Inside Business Insurance

Insurers bracing for hard market's end

Insurer CEOs expect proper pricing and underwriting discipline to be more important as the market softens, a survey finds. Page 4

PBGC says it will terminate Enron plans

The PBGC is acting to ensure that some pension assets of Enron are protected in bankruptcy. Page 4

Expect CEO salaries to come under scrutiny

Richard Grasso's nine-figure pay package will spur wider scrutiny, Paul Winston predicts. Page 6

Delaying class action reform a good thing

Postponing a vote on class action reform in the Senate will only improve the measure's chances, one of this week's editorials says. Page 8

U.K. energy proposals may pose new risks

A parliamentary report warns that U.K. plans for offshore wind farms could increase the risk of shipping accidents and collisions. Page 21

Online

• The **Datebook** calendar lists upcoming industry seminars and meetings and allows you to add info on your own event.

• **Searchable directories** of all the industry vendors found in *BI*'s Market Sourcebook.

• New **Opinion Poll** for readers: Do you plan to use the Labor Department model notices to communicate COBRA health care coverage rights to employees?

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REPORTING ON CORPORATE RISK AND EMPLOYEE BENEFIT MANAGEMENT NEWS.

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Comp reform savings fail to impress all

California self-insurers likely to see benefits before insured employers

By ROBERTO CENICEROS

SACREMENTO, Calif.—Insured employers in California should expect average rate cuts of around 10% when workers compensation coverage renews as a result of reforms signed into law earlier this year, insurers and brokers say.

That is substantially less than the 20.9% reduction in pure premium rates recommended by the California Insurance Commissioner late last month, and the 20% cut that some self-insured employers in the state are already including in their budget estimates.

Insurers claim that the smaller reductions expected for the insured comp market are due to the staggered implementation of the reforms and the necessity for new insurers to be attracted to the California market to increase capacity before rates can be lowered more.

Meanwhile, some new insurers may be reluctant to enter the California market if pending legislation to regulate workers comp rates in the state is passed.

Self-insured employers that retain control over their claims management will benefit much sooner and to a greater extent from the workers comp reforms than will insured employers, said Jeff Green, general counsel for Grimmway Enterprises Inc. in Arvin, Calif.

Mr. Green played a leading role in the employer-driven effort to pass the reforms signed into law by Gov. Arnold Schwarzenegger in April. Mr. Green led an effort to organize a ballot initiative to put workers comp reform before voters in the event legislators failed to implement the changes called for by the governor.

"There is no question that a self-insured employer will enjoy the benefits of the reforms more directly and more quickly," Mr. Green said.

Some self-insured companies already have budgeted for 20% cost reductions for 2005 (*BI*, May 3).

But the reforms also are expected to help insured employers, primarily by enticing insurers to commit more capacity to the state's workers comp market, Mr. Green said.

Insurers and brokers say they expect the 2004 reforms, along with reforms adopted in 2003, will allow insurers to reduce their rates for upcoming July 1 renewals.

The 2004 reforms, which were a major feature in Gov. Schwarzenegger's election campaign, are wide-ranging and are expected to slash billions of dollars in costs from the system. Among the many reforms are: changes to the system for awarding some disability payments, the introduction of physician net-

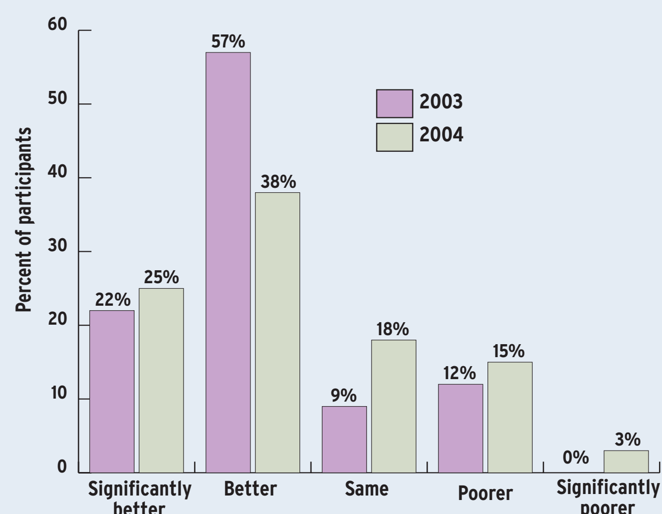
See **CALIFORNIA**/page 24

PHOTO: ZUMA PRESS

California Insurance Commissioner John Garamendi wants to see bigger rate cuts by the state's workers compensation insurers.

OUTLOOK ON P/C PERFORMANCE

American Re asked insurance company CEOs: What best describes the financial outlook for your company during 2004-2005, compared with 2003-2004?



Source: American Re Corp.

Insurer CEOs resolve to keep a tight rein after hard market ends

By SALLY ROBERTS

Although insurance company executives expect their companies' financial results to be better this year than last, most foresee the hard market enduring only through the end of 2004, according to an American Re Corp. survey.

Nonetheless, despite their predictions of an end to rising premiums, the executives are determined more than ever to maintain underwriting discipline and price adequacy, the survey found.

American Re, a unit of Munich Reinsurance Co., surveyed 50 insurer chief executives and senior managers about issues affecting both their own operations and the industry overall. The survey was conducted last month during the 10th Annual CEO Roundtable Forum, held at the reinsurer's Princeton, N.J., headquarters.

Although the market may be softening in certain lines, executives "still feel they're going to have better, if not significantly better, results for the next year or two," said Jack Snyder, chief marketing officer for American Re.

Twenty-five percent of the executives surveyed described the financial outlook for their companies during 2004-2005 as "significantly better" and 38% described it as "better" compared to 2003-2004. Only 18% described their financial outlook as the same; 15% said it was poorer; and 3% said it was significantly poorer.

At the same time, 69% of exec-

See **SURVEY**/page 24

Feds eying actuarial consultants for 'anticompetitive agreements'

By VINEETA ANAND

WASHINGTON — The U.S. Department of Justice has launched a broad investigation of actuarial consulting firms.

A March 25 letter to the firms said the Justice Department's antitrust division is investigating "anticompetitive agreements or understandings relating to contract terms and conditions among providers of actuarial consulting services."

Officials at six of the biggest actuarial consultants confirmed they received the letter: Watson Wyatt & Co. in Washington; Towers Perrin & Co. in Valhalla, N.Y.; The Segal Co. in New York; Milliman USA in Seattle; Aon Corp. in Chicago; and Hewitt Associates in Lincolnshire, Ill.

Officials at all six firms said they are cooperating with the Justice Department's request for records and documents. Officials at two other big players—Mercer Human Resource Consulting in New York, and Buck Consultants Inc. in Pittsburgh—declined to comment.

At issue is whether huge judgments in lawsuits have prompted the actuarial firms to conspire to limit damages. The Justice Department will examine whether there was a conspiracy to force pension funds to accept limits or caps on what they would pay in lawsuits over their work, or to exempt the firms from liability.

Watson Wyatt, Towers Perrin, Milliman and Mercer require their pension fund clients to accept such liability caps. Aon and Segal do not. Officials at Buck and Hewitt would not say if they have liability caps

A Justice Department spokesman declined to comment on the investigation, as did Ann Combs, assistant secretary of the Labor Department, who heads the Employee Benefits Security Administration.

Another issue is that some actuarial firms may have sought to impose these liability limits on their clients because they are co-participants in an insurance pool from which damages for lawsuits are paid, sources allege.

In 1987, Watson Wyatt, Buck, Milliman and Towers Perrin set up a captive insurance company to pro-

See **INVESTIGATION**/page 26

PBGC to close Enron plans to save assets from creditors

By JOANNE WOJCIK

WASHINGTON—The Pension Benefit Guaranty Corp. is taking steps to preserve the benefits of participants in the underfunded pension plans of bankrupt Enron Corp.

By filing a notice of determination to terminate four of Enron's defined benefit pension plans, the PBGC hopes to preserve plan assets that otherwise would flow from the bankrupt company to other creditors, the agency said in a statement.

The four plans, which have roughly 17,000 participants, are underfunded by "a couple hundred million dollars," a PBGC spokesman said.

Hearings on Enron's reorganization plan began today. Under the terms of that plan, the PBGC states, Enron "makes inadequate provision for either maintaining the Enron defined benefit pension plans or placing the pension obligations with a private-sector insurance company. After confirmation, the plans would be left behind with a liquidating trust that is paying out all of its assets to other creditors," according to the statement.

PHOTO: GETTY

Enron Corp. filed for bankruptcy protection in December 2001.

The plans in question are: the Enron Corp. Cash Balance Plan; Garden State Paper Pension Plan; Enron Financial Services Pension Plan; and San Juan Gas Co. Pension Plan.

The action is not expected to affect the PBGC financially.

"We don't expect a loss to PBGC because we believe the action today will bring people to the table, and the outcome, we hope and believe, will be standard termination of the pension plan, which means that all participants will receive the full amount of their benefit, and those eligible for lump sums will receive those," said the PBGC spokesman.

Class action: Vote on bill delayed

Continued from page 1

from different states.

But several Democratic supporters of the bill said that they would vote against cloture unless work had been completed on an unrelated defense authorization bill. Without the support of the Democrats, the bill would have fallen far short of the 60 votes needed to invoke cloture.

An earlier version of the bill fell one vote short of cloture last fall (*BI*, Oct. 27, 2003), but after Sen. Frist and others agreed to some small changes in that measure, three Democratic senators who had voted against cloture agreed to reverse their position in any future votes.

But shortly before the latest vote was scheduled to occur, Sen. Frist agreed to delay consideration of the business-backed class action bill, with the understanding that it would be the first order of business upon completion of the defense bill. That arrangement means that senators will proceed directly to consideration of the bill without having to deal with a cloture vote. Although Sen. Frist expressed some hope that the Senate could begin debate on the class action bill by the end of last week, several senators left for France Thursday to participate in ceremonies commemorating the 60th anniversary of D-Day.

One of the class action bill's most vocal Democratic supporters—Delaware Sen. Tom Carper—said that Sen. Frist "made the right decision" in postponing consideration of the class action bill.

Stanton Anderson, executive vp of the U.S. Chamber of Commerce, also hailed the decision. He said in a statement that "proceeding directly to this important piece of legislation, without the need for a cloture vote, helps clear the way for a full debate on the class action bill, which will eliminate some of the worst abuses in the current class action system."

Insurers also welcomed the delay.

"Despite the fact that the Senate did not consider class action reform legislation today as expected, PCI is pleased the Senate agreed to take up the bill immediately after the defense bill," said Charles Taylor, assistant vp-federal government relations in the Property Casualty Insurers Assn. of America's Washington office.

"In fact, the timing may be better, as this will allow the Senate to focus solely on class action reform. We believe the reform bill has the support of more than 60 senators, and we are looking forward to final action on the measure soon, since it is urgently needed to help curtail forum shopping and frivolous lawsuits," Mr. Taylor said.

The delay is "good news," because it establishes a plan for dealing with the class action reform bill, said Melissa Shelk, vp-federal affairs at the American Insurance Assn. in Washington. "They will finish the defense bill and they will immediately begin consideration of the bill. We do, however, expect a lot of amendments."

The Risk & Insurance Management Society Inc. expressed hope that lawmakers will move quickly on the measure.

"Class action reform is one of RIMS' top priorities, and we are optimistic that the Senate will deal with the Class Action Fairness Act and its merits once the Department of Defense bill is addressed," said Janice Ochenkowski, vp-external affairs for New York-based RIMS. "We are encouraged by Congress' progress on this issue and urge the Senate to adopt legislation as soon as possible.

"RIMS believes that adoption of this legislation will begin the process of correcting the abuses in our legal system and ensuring a healthier economy," said Ms. Ochenkowski, who is also senior vp at Jones Lang LaSalle Inc. in Chicago.

An opponent of the bill, however, thinks the delay will have a minimal impact on the measure's fate.

"I think this was a blunder on Frist's part, and he recovered by pulling the class action bill," said Pamela Gilbert, an attorney in the Washington law firm Cuneo Waldman & Gilbert L.L.P. "The only impact I can see is, when you want to pass something, delay isn't good. The bill has the votes for cloture—everybody knows that. It's getting late in the year to get legislation to President Bush's desk—not impossible, but difficult," said Ms. Gilbert, who represents the National Assn. of Shareholder & Consumer Attorneys, an organization of plaintiffs attorneys.

APIW: Abraham honored

Continued from page 3

than now," she said.

In 1982, Ms. Abraham joined Morgan Guaranty Trust as assistant treasurer and followed that with a four-year stint as executive director of the Cornell Theory Center at Cornell University in Ithaca, N.Y. Prior to joining United Educators in 1998, she was the chief financial officer, treasurer and secretary of board trustees for Whitman College in Walla Walla, Wash.

Despite spending many years in academia, Ms. Abraham was no novice to the insurance industry when she joined United Educators. As Whitman's CFO, she was responsible for risk management and insurance issues and also served on the board of directors for the college's captive insurance company.

In her six-year tenure at United Educators, Ms. Abraham has gained several admirers, including Harry L. Richter Jr., chairman and CEO of Stamford, Conn.-based Genesis Underwriting Management Co., a subsidiary of General Re Corp. that provides reinsurance for United Educators. "She's been a valued client for many years, and we think very highly of her skills as a leader," he said.

Mr. Richter expressed admiration for Ms. Abraham's skillful management of the company's restructuring efforts, which included a reduction in the number of governing boards, a strengthening of capital and the development of United Educators' reinsurance options.

"She did something that will, over time, significantly strengthen the United Educators brand," he said.

A renewed commitment to serving the educational community was a key part of the effort, Ms. Abraham said. United Educators is a licensed insurance company owned and governed by more than 1,100 member colleges, universities, independent schools, public school districts, public school insurance pools and related organizations throughout the United States.

The company, which was created in 1987 to solve what Ms. Abraham refers to as a "liability crisis" in the education field, is developing ways to help the institutions manage their risks, she said. For example, the United Educators holds monthly calls with educational institutions to discuss topics ranging from slips and falls to discrimination, she said.

"We will not eliminate risks," she said. "We serve a population that thinks it's immortal. We do our very best to help the institutions manage the risks. Our first priority is risk management."

In 2000, *Business Insurance* named Ms. Abraham to its list of the 100 Leading Women in the insurance industry. Ms. Abraham holds an MBA from the Wharton School of Business at the University of Pennsylvania in Philadelphia and a bachelor's degree in international studies from American University in Washington.

Ms. Abraham was nominated by three previous APIW award recipients: Ms. Thrower, who won the award in 1993; Kathryn J. McIntyre, former publishing director of *Business Insurance*, who won the award in 1989; and Carol Rennie, the retired chair of Constellation Reinsurance, who won in 1982.

While Ms. Abraham said she is delighted to receive the APIW award, she is quick to pass on credit for her organization's success to her staff members, who she said are passionate about both education and insurance.

"I am thrilled that this has allowed me to shine the light on United Educators," she said. "This is not about Janice Abraham; this is about the great company we have."

Paul Winston

Executive pay in the limelight

After several years in which corporate scandals and public downfalls became almost commonplace, and legislators and regulators worked to encourage more responsible corporate governance, some thought the worst was behind business.

But Elliott Spitzer, the attorney general of New York, is shining a light on another ugly problem in the dark corners of America's boardrooms: unrestrained executive compensation. Before his latest investigation into corporate greed is complete, I expect that many more companies will be forced to examine their pay programs and will face a new tide of shareholder lawsuits alleging inadequate oversight by boards of directors.

Mr. Spitzer did not have to look far for an example of egregious compensation. Last month, he filed suit against Richard Grasso, the former chief executive officer of the New York Stock Exchange, seeking to rescind a $187.5 million multiyear pay package deemed excessive and in violation of the state's laws governing nonprofits. The suit also named a NYSE board member who headed the compensation committee.

Paul Winston

"This case demonstrates everything that can go wrong in setting executive compensation," Mr. Spitzer said in a statement announcing the lawsuit. "The lack of proper information, the stifling of internal debate, the failure of board members to conduct proper inquiry and the unabashed pursuit of personal gain resulted in a wholly inappropriate and illegal compensation package."

Specifically, the lawsuit alleges that:

- The NYSE board of directors was misled about various aspects of Mr. Grasso's compensation contract; in particular, some $18 million in bonus awards were not disclosed to the board by an assistant to Mr. Grasso. Mercer Human Resources Consulting Inc., which was hired to consult on the pay package, admitted that its report to the board was flawed; Mercer has since reached a settlement with Mr. Spitzer's office and agreed to return the fees it charged the NYSE for its work in 2003.
- The formula on which Mr. Grasso's compensation was based was flawed and under his influence. Among other things, Mr. Spitzer charges that Mr. Grasso set the performance targets on which his pay was based, enabling him to exceed those targets. Even so, the suit notes, the NYSE board chose to follow an even more gainful formula in determining Mr. Grasso's pay.
- The compensation provided to Mr. Grasso was not "reasonable" under New York's law governing nonprofits. In fact, the suit notes, the compensation and benefits provided to the head of the NYSE from 1999 to 2001 nearly exceeded the net income of the NYSE during the same period.
- Mr. Grasso's dual roles as regulator and NYSE employee created a conflict of interest. The suit alleges that, as NYSE's top regulator, he oversaw the very companies from which executives were drawn to serve on the board and its compensation committee. The lawsuit cites one example of this conflict in which a compensation committee member who raised concerns about Mr. Grasso's pay allegedly was later personally confronted by the CEO about his misgivings.

There are some unique aspects to this case. For one, it's probably highly unlikely that many other heads of nonprofits are paid such grossly excessive amounts. Indeed, there aren't very many for-profit companies that pay their top executives such sums.

Furthermore, it is not at all common for the pay of a regulator to be determined by the very entities he or she oversees, probably because such a relationship could clearly produce a situation ripe for conflict of interest, as is alleged here.

But excessive compensation and its causes are still commonplace. The reasons include boards that do not critically assess CEO compensation or that use flawed performance measures. Or boards that are given inadequate information in determining pay. Or boards that agree to pay executives far too much when judged by the compensation levels of other companies or the dictates of common sense.

I don't believe anyone is deserving of a nine-figure compensation package, and I am appalled that more of the NYSE board members didn't have the integrity to question that figure. As noted above, I expect CEO pay to come under greater scrutiny in this country in the months to come, forcing companies to justify to regulators, shareholders and customers that their top executives are deserving of rich compensation. More lawsuits are likely.

Directors and officers liability insurance, as a consequence, will probably take another hit in losses. And D&O buyers will face another hike in rates. And insurer CEOs, at least, will say they are earning their seven-figure salaries as this fuels more gains in insurer profits.

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Editorial

Delay aids class action bill

WE'RE NORMALLY NOT big fans of delaying the consideration of important legislation. That's particularly true as Washington enters the long hot summer before national elections. Even the most reasonable bills can die of congressional inertia while the legislative calendar inexorably contracts as the full recess looms.

That being said, we still think that Senate Majority Leader Bill Frist, R-Tenn., did the right thing by holding off action on the Class Action Fairness Act. That's because, had he pushed ahead as planned last week, he certainly would have lost. He would have lost because many of the Democrats who support the bill said they would not vote for cloture—a parliamentary maneuver that limits debate on a given bill—because they wanted work on a defense authorization bill finished first. And had he lost on the cloture vote, there would have been no guarantee that class action reform would win Senate approval this year—or any year.

While there's still no guarantee that the bill will pass, at least it has a chance, thanks to the conditions under which it will be considered. Under the unanimous consent agreement that withdrew the cloture motion, Sen. Frist and his Democratic counterparts agreed that the class action reform bill would be not be subject to an initial cloture vote aimed at blocking its immediate movement to the Senate floor. Instead, senators would be able to consider it on its own merits.

And those merits are considerable. As currently drafted, the bill would go a long way toward curbing what businesses and insurers have considered abusive "forum shopping." That's where plaintiffs seek the most plaintiff-friendly state court jurisdictions in which to file national class action lawsuits. The Class Action Fairness Act would, under certain circumstances, allow the removal of interstate class actions that meet specified criteria to federal court, which many business and legal observers regard as a more-neutral venue. This reform alone—which would bar no one from the courtroom but would, rather, specify in which courtroom the class action would be heard—makes the bill worthy of passage.

We fully expect that numerous amendments will be offered to the bill. Some will, no doubt, be designed not to improve the bill but to scuttle it by weighing it down with provisions that have nothing to do with class actions. We also expect to see amendments deigned to render the measure next to meaningless by creating numerous exceptions to the types of class actions that can be removed to federal court. We hope that these attempts will be resisted, and that the Class Action Fairness Act's self-evident merits will ensure that it wins Senate approval intact. That is certainly worth the week's delay.

Cut California comp rates

AFTER YEARS OF political wrangling and lobbying by business groups, the focus of efforts to cut California's almost out-of-control workers compensation insurance rates is finally resting on insurers.

And they would do well to provide an adequate and appropriate reduction in rates in response the sometimes-tortuous reform process.

The reforms signed into law by Gov. Arnold Schwarzenegger in April provide meaningful relief for insurers and self-insured employers in the state by, among other things, allowing them to take greater control of the system for providing workers comp benefits.

California's Insurance Commissioner John Garamendi has suggested that the reforms should lead to around a 20% cut in pure premium rates at mid-year renewals, but some insurers are already making excuses as to why such a large cut, or perhaps any cut, might not be possible this year.

Self-insured employers in the state already are enjoying the benefits of the reforms and we see little reason why insured employers should not also benefit from what has become a key policy affecting businesses in California.

While we would not advocate insurers' cutting rates to a degree that would place them in financial peril, the systemic nature of the changes should enable them to offer some meaningful rate relief without having to wait for loss data to justify a cut.

Without such action, employers in California and other states enduring workers comp problems may be less willing to stand with insurers next time they press for reform.

Schillerstrom

Letters to the Editor

Drug reimportation will cost insurers billions

To the editor: Are insurers prepared for the billions of dollars of new claims resulting from drug reimportation? Are actuaries running their figures, and underwriters examining their language? Do we even know what lines of insurance will be hit hardest?

The country seems destined to follow the shortsighted strategy of reimporting drugs in order to "save money," even though the government agency in charge of pharmaceutical safety has tried to tell us and Congress over and over that wishful thinking can't make the drugs safe or secure. Random tests by the Food and Drug Administration have found that 80% to 88% of samples of reimported drugs to be wrong in some way, sometimes in what would be very serious or fatal ways.

So, the situation is going to arise that Ms. X gets some drug from her hospital, pharmacy, health maintenance organization, state or employee benefit plan. It causes Ms. X or Baby X some terrible problem because it is not what it should be or was not given proper cooling or whatever in its voyage to the U.S. consumer.

Ms. X (and millions of others) will have justification for multimillion dollar lawsuits against someone. Whom? Some offshore supplier or Web site? Or sue all or some of the state/hospital/doctor/HMO/prescription benefit manager/local pharmacy or employer who put Ms. X in line for these second-rate drugs?

Not only will there be the billions of dollars of direct claims but also megabillions more in punitive damages, because consistent statements from the FDA and others clearly show that a prudent entity would not have subjected its patient/customer/plan participant or state citizen to this shaky supply line. Lawyers won't have trouble convincing juries that entities were negligent or callous in trading patient safety for "saving money."

So, property/casualty insurers will end up paying far more in settlements than is ever "saved" by reimportation.

Fred Hunt
President
Society of Professional Benefit Administrators
Bethesda, Md.

Letters to the Editor

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London Market Report

Spotlight Editor: Sarah Veysey

London eyes changes to improve processing of claims

By SARAH VEYSEY

The past year has seen a raft of measures aimed at improving the claims-paying process in the London market, and additional claims-related changes are expected to be unveiled this month.

In recent years, the London market has been subject to criticism from some quarters about the way that it handles claims, according to Stuart Willoughby, director of claims at Markel International in London.

And while he said some of that criticism has been unfair, "there is clearly room for improvement," said Mr. Willoughby, who serves on the Lloyd's strategy group for claims.

> **'There is clearly room for improvement' in claims-handling processes.**
> *Stuart Willoughby, Markel International*

He added that the complexity of the London market and the subscription nature of many policies underwritten there are key factors as to why the claims process can be a difficult one.

Nick Prettejohn, chief executive of Lloyd's of London, recently estimated that the annual amount spent on incidental claims costs in the Lloyd's market is £500 million ($915.6 million), and that the annual cost for the London market as a whole could be more than £1 billion ($1.83 billion) a year.

Furthermore, according to Mr. Willoughby, the innovative nature of some of the business placed in London has meant that policy wordings may be new, and this, coupled with the large sums of money often involved in such policies, sometimes leads to legal disputes over claims.

But one area in which the process

See CLAIMS/page 12

PHOTO: PA PHOTOS

LARGEST LLOYD'S OF LONDON SYNDICATES

20 largest syndicates operating at Lloyd's, ranked by capacity in 2004

Syndicate number	Managing agent	2004 capacity (in millions of pounds)	Change from 2003
2001	Amlin Underwriting Ltd.	£1,000.0	0.0%
0033	Hiscox Syndicates Ltd.	847.4	0.6
2020	Wellington Underwriting Agencies Ltd.	730.0	4.3
2488	ACE Underwriting Agencies Ltd.	550.0	-24.1
0190	Liberty Syndicate Management Ltd.	541.0	102.6
2999	Limit Underwriting Ltd.	530.0	6.0
0510	R.J. Kiln & Co. Ltd.	508.0	5.0
0386	Limit Underwriting Ltd.	500.0	11.1
2003	Catlin Underwriting Agencies Ltd.	500.0	11.1
2987	Brit Syndicates Ltd.	500.0	0.0
0218	Cox Syndicate Management Ltd.	433.2	0.0
1084	Chaucer Syndicates Ltd.	400.2	12.0
0435	Faraday Underwriting Ltd.	400.0	0.0
2623	Beazley Furlonge Ltd.	396.4	20.2
0623	Beazley Furlonge Ltd.	345.1	4.5
1209	XL London Market Ltd.	340.0	0.0
2791	Managing Agency Partners Ltd.	325.9	0.0
5000	St. Paul Syndicate Management Ltd.	325.0	-25.3
3210	Chaucer Syndicates Ltd.	316.0	26.4
1183	Talbot Underwriting Ltd.	287.5	48.6
2147	SVB Syndicates Ltd.	286.4	0.0

Source: Standard & Poor's Corp.

Participants at Lloyd's mull plan to change capital rules

By SARAH VEYSEY

Managing agents and other players in the Lloyd's of London market are currently reviewing a consultation paper that proposes new assessments of the level of capital that syndicates should hold.

In the paper, the Financial Services Authority, the United Kingdom's financial services regulator, proposes, among other things, that managing agents be subject to enhanced capital requirements and individual capital assessments.

David Strachan, the FSA's insurance sector leader, said in a statement that accompanied publication of the consultation paper that the proposals were intended to ensure that both the senior management at Lloyd's centrally and at Lloyd's managing agents effectively manage the amount of capital needed to support the risks they take on.

> **Proposed capital rules would 'improve protection for policyholders' at Lloyd's.**
> *David Strachan, Financial Services Authority*

"This will, in turn, enhance confidence in the Lloyd's market and improve protection for policyholders," Mr. Strachan added in the statement.

Responses to the consultation paper, "CP04/7 Lloyd's: Integrated Prudential Requirements, and Changes to Auditing and Actuarial Requirements," are due by July 30. And the FSA said it hopes that the proposals will go into effect at the beginning of 2005.

A spokeswoman for Lloyd's said that the market's executives were still considering a response to the paper. And several Lloyd's managing agents also said that they were formulating their reactions to the proposals.

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Many sold on franchise system page 15

Consolidation reshapes market page 17

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Claims: London eyes changes to improve processing

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could be improved, Mr. Willoughby said, is in providing greater certainty on the terms of the insurance contract when policies are underwritten.

"One area where we have fallen short is that when policies have been issued, there hasn't always been certainty," which can give rise to claims disputes, he said.

Mr. Willoughby said that the high-profile coverage dispute between World Trade Center leaseholder Silverstein Properties Inc. and a group of underwriters has brought this issue to the fore. Although the WTC coverage took effect in July 2001, no policy had been issued as of the Sept. 11 attacks that brought down the twin towers, resulting in the dispute over terms.

Faster policy issuance, he said, is an area in which the London market has been making efforts to improve.

Players in the Lloyd's and London company markets also have been taking steps to reduce expenses and to speed up the claims-paying process.

"Of course, the policyholders themselves expect claims to be dealt with professionally and expediently," said Mr. Willoughby.

The Lloyd's strategy group for claims in July plans to present a white paper on claims reforms to the Lloyd's Franchise Board, according to Dane Douetil, deputy chief executive at Brit Insurance Holdings P.L.C. in London.

"That paper consists of suggestions as to how the claims process can be speeded up," said Mr. Douetil, who also serves on the claims strategy group.

Meanwhile, there already have been great strides made in improving the claims process, Mr. Willoughby pointed out, adding that the Lloyd's Franchise Board and the Lloyd's Market Assn.—which represents managing agents operating in the market—have been two driving forces behind those reforms.

One of the major reforms of the claims process was the establishment earlier this year of an electronic claims repository to provide all parties involved in a claim with instant and contemporaneous access to claims files.

Until recently, the London market has been reliant on paper, with a single claim file being circulated among parties involved in a claim by brokers, explained Steven Beard, chief operating officer for XChanging Claims Services, which manages the electronic repository.

The repository eliminates the reliance on the broker to present the claims file to all insurers participating on the risk, Mr. Beard said. By using the system, the parties involved in a claim can access an electronic image of the paper policy, he noted.

The repository is backed by managing agents, which are now signing up to use the system for their syndicates, said Simon Sperryn, chief executive of the Lloyd's Market Assn.

The repository will expedite the claims-handling process within Lloyd's, predicted Mr. Willoughby,

> **'If there is transparency in the (claims process), then that adds a lot of value' to the policyholder.**
>
> *Steven Beard*
> *XChanging Claims Services*

who said it would also help improve the quality of claims information.

"This will be to the benefit of all parties involved—policyholders, brokers and underwriters," he said.

"If there is transparency in the (claims process), then that adds a lot of value" to the policyholder, noted Mr. Beard.

Some clients of XChanging are also now using Web browser-based technology that allows them to track the progress of claims, he added.

Other initiatives under development include the establishment of a common electronic settlement system for claims in the London company market, noted Mr. Sperryn.

"This is all going to fit together to provide the infrastructure for electronic claims management through one system throughout the London market," he said.

"We want to provide a good service to customers. Certainly, here in Lloyd's, we pride ourselves on always paying every valid claim," said Mr. Sperryn. "And so that matters to us and it matters to our customers."

The Sept. 11 terrorist attacks increased awareness of the importance of claims processes, noted Markel's Mr. Willoughby. Additionally, he said, claims directors have been getting a higher profile in some organizations.

Mr. Willoughby added that the reduction in the number of managing agents operating in the Lloyd's market, and the fact that corporate capital—much of it from the United States—now makes up the majority of investment at Lloyd's, has led to a cultural change within the market.

Claims-handling is now seen as a more-strategic issue, he said, where-

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Claims: Processes

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as many companies previously viewed it as a "byproduct" of underwriting.

The investment of capital by North American and Bermudian companies has added to calls for improvements in the standards of claims processing, agreed Mr. Beard.

But in the London market, there is still a need for greater professionalism among claims adjusters, according to David Taylor, a special advisor to the London-based International Underwriting Assn., which represents companies in the London market.

In a speech to the annual meeting of the Assn. of Average Adjusters in London, Mr. Taylor said there is a "crying need for skilled professionals in the market and worldwide."

The association represents marine claims professionals, he explained, who must undergo a difficult examination process to become qualified.

One way to increase the professionalism of marine claims adjusters, he suggested, would be for the association to increase its scope.

Rules: Changes considered

Continued from page 10

But some experts say that the proposed changes could have quite a large impact on the market.

The new measures, if enacted as proposed in the consultation paper, would likely have an effect on the business written in the market, according to Dane Douetil, deputy chief executive at Brit Insurance Holdings P.L.C. in London.

Mr. Douetil said that as companies develop a better understanding of their cost of capital per class of business, they may decide to alter their business mix to reduce their overall capital requirements. Some more volatile classes of business, such as catastrophe retrocessional business, "consume" more capital than do other, less volatile classes, such as auto insurance, he explained.

"Overall, the amount of capital that will be required will increase," Mr. Douetil said, noting that Brit has been planning for such a change for some time.

"I don't think we will see the impact of this overnight. It is something that will happen over a two- to three-year period," he predicted.

Experts say that if the FSA's proposals are enacted, businesses operating at Lloyd's will become subject to several different capital adequacy assessments.

In addition to the FSA's enhanced capital requirements and individual capital adequacy measures, syndicates would continue to be subject to Lloyd's risk-based capital requirements, said Mr. Douetil.

Eventually, it is likely that the most conservative capital measurement will be the one that is used, said Stephen Searby, credit analyst at Standard & Poor's Ratings Services in London.

Mr. Douetil said he is concerned that while Lloyd's participants and the FSA might reach an agreement over the amount of capital syndicates should hold, companies in the market may eventually be required to increase capitalization.

"When we trade at Lloyd's, we may have to put up a potentially higher number—which is" the risk-based capital requirements, he said. "If that is the case, then that makes it an interesting decision about whether it is worthwhile providing more capital to Lloyd's or growing our (London market) insurance company instead," he said.

Eventually, it is likely that the most conservative capital measurement will be the one that is used.

Stephen Searby
Standard & Poor's Ratings Services

And if the amount of capital that rating agencies require to maintain a rating is higher than any of the other measures, then managing agents will likely have to comply with that requirement, Mr. Douetil added.

The introduction of the FSA's proposals would likely create greater awareness among managing agents "of the implications for capital of writing any class of business," noted Miles Trotter, a credit analyst at A.M. Best Co. in London. "The greater prominence of this factor could lead managing agents to change the mix of business written by the syndicates they manage," he noted.

Under the FSA's proposals, managing agents will still be able to use letters of credit as a way to raise capital, sources say.

Had the FSA proposed to remove this facility, "that would have put a lot of pressure on some syndicates," observed Greg Carter, managing director of Fitch Ratings European Insurance Group in London.

Letters of credit give syndicates a certain amount of flexibility to adjust their capital base to underwrite business, he said.

But there will likely be a debate about the use of letters of credit, said Mr. Searby. He noted that while the FSA has said it would permit the ongoing use of letters of credit, the regulator has asked for feedback from market players about the long-term future of this mechanism.

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Lloyd's franchise system wins over some skeptics

Market execs say concerns largely allayed but that true test lies ahead

By PETA MILLER

Senior figures in the Lloyd's of London market generally approve of the new franchise system, though many were skeptical about the system's ability to promote underwriting discipline without stifling innovation.

Lloyd's adopted the new franchise system on Jan. 1, 2003, to oversee managing agents—the franchisees—and to try to prevent recurrences of the underwriting lapses that plagued the market with losses in the not-too-distant past.

The main objective of the Lloyd's franchise system is to "create and maintain a commercial environment at Lloyd's in which the long-term return to all capital providers is maximized...by creating a disciplined marketplace of well-managed businesses," stated a consultation document that was issued by Lloyd's in mid-2002 and later approved by a marketwide vote.

The system entailed the creation of a Franchise Board and a Franchise Performance Directorate. Senior executives in the Lloyd's market sit on the board, which is equivalent to the governing council of the franchise system.

> **'Any reduction in innovation (due to the franchise system) seems to be modest compared with the reduction in risk to the Central Fund.'**
>
> *Anthony Young*
> *Assn. of Lloyd's Members*

Rolf Tolle, a former Lloyd's underwriter, heads the Franchise Performance Directorate, which manages the business-planning process and works with syndicates on following franchise guidelines.

Lloyd's franchise consultation document stressed "there is no intention of preventing franchisees from writing any classes of business—other than those which cannot be justified on prudential or profitability grounds. In particular, the franchiser will recognize that innovation and choice, both of which are reinforced by Lloyd's market structure, are key elements in attracting the right types of business."

In spite of that statement, some in the market feared that the franchise system could not achieve its aim of ensuring underwriting profitability without also stifling innovation and disrupting syndicate business plans.

But now, almost 18 months since the franchise system was launched, several executives say their concerns have mostly been allayed and that they are encouraged by the market's

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Franchise: Concerns about system largely allayed

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performance.

"Before the franchise started, I had some concerns that (the Franchise Board) could stifle innovation in the market as a byproduct of stifling bad underwriting," said Anthony Young, chief executive of the Assn. of Lloyd's Members, which represents individual investors in the market.

But, he said, "any reduction in innovation seems to be modest compared with the reduction in risk to the Central Fund," referring to the fund that pays claims for insolvent syndicates.

"There have been a couple of underwriting operations thrown out of Lloyd's as a result of the Franchise Performance Directorate activities," noted Mr. Young. "They are prepared to be tough in dealing with syndicates that don't operate in a way they feel is" appropriate for the franchise, he said.

John Eltham, a director in the special risks division of Miller Insurance Services Ltd. in London, said he initially had concerns about how the franchise system would respond when the market turned and rates began to decline.

Although certain syndicates have begun to increase their capital allocation to nonstandard business lines—such as contract frustration, event cancellation and war personal accident—"there have not been any real difficulties within the franchise board in writing that business and (syndicates are) beginning to move capital in that direction," Mr. Eltham said.

"Maybe their approach at the outset was not what we would like to have seen," said David Foreman, chief underwriting officer at Wellington Underwriting P.L.C., referring to the Franchise Performance Directorate not consulting with the market before mandating changes.

"With the process of consultation that is now under way, everybody is working well together, there is feedback of information to and from Rolf Tolle and a realization that whatever the franchise directorate gets up to, it is for the overall good of the market," Mr. Foreman said.

"Everything about the franchise is very positive, and what they are doing is good for the market. So far, they are sticking to what they said they would do: to be facilitative rather than prescriptive," said Rob Childs, director of underwriting at Hiscox P.L.C. and chairman of the Lloyd's Market Assn.

"So far, the franchise board has managed to walk a difficult tightrope pretty effectively," said Dane Douetil, deputy chief executive of Brit Insurance Holdings P.L.C.

> **'The directorate works to ensure that we have a marketplace of disciplined and well-managed businesses without blunting entrepreneurial spirit.'**
>
> *Rolf Tolle*
> *Franchise Performance Directorate*

"We found that when we had a case to make, they listened and have (considered the commercial aspects) in what they have looked at; they have been helpful, not overly restrictive," he added.

However, the next 18 to 36 months will be the real test for the franchise, as the market softens, executives agreed.

"What I am concerned about is if the board starts becoming more intrusive on the micromanagement of the business," said Mr. Douetil. "To date, I have not seen that, but we need to guard against it as the market becomes less hard. It will be a true test," he said, noting that the next 18 to 24 months will be critical.

Mr. Douetil also pointed out that there is potential for tension in the franchise's balancing of the market's interests with those of the individual syndicates. This could happen, for example, in cases where syndicates want to expand into classes of business that the Franchise Board judges that Lloyd's as a whole has written enough of, he said.

But, he added: "In some classes of business where underwriters are more concerned about market share and prestigious accounts than bottom-line results, having a quiet word to the chief executive or board of the agency can only be a good thing."

"The trick will be defining quality (business) and managing what makes up the nonstandard area of account," said Mr. Eltham of Miller.

"Managing the downside is what Rolf Tolle has got to do," said Wellington's Mr. Foreman. "That is beginning, but we have still got a market that is well ahead of 1993; we have a way to go before we get down there," he said, referring to the depths of the prior soft market.

Mr. Childs of Hiscox, however, argued that the franchise system already is being tested.

"I think the market conditions are very, very good in lots of areas of business, but (the franchise) is being tested because we are looking at preparing business plans for 2005," he said. "Already the franchise board is talking to directors about that and feeding back to the market details about various lines of business and what the actual progress of lines of business has been in terms of rates and terms and conditions," he said.

Mr. Tolle declined to be interviewed, but said in a statement: "The Franchise Performance Directorate does not seek to micromanage or get involved in the day-to-day running of the syndicates. The directorate works to ensure that we have a marketplace of disciplined and well-managed businesses without blunting entrepreneurial spirit."

Insight and Analysis

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Consolidation reducing London market choices

But recent entrants from Bermuda, Lloyd's helping to meet multinationals' needs

By CAROLYN ALDRED

London's commercial insurance landscape has changed dramatically in recent years, but the London company market still fulfills a vital role for risk managers worldwide, brokers and insurers say.

The London company market of the 21st century is vastly different from the market that existed in its heyday of the 1980s. Buffeted by significant losses in the '80s and '90s, market consolidation and less appetite for underwriting volatility, many companies have withdrawn from the London market and the large speciality and nonstandard risks it is known for.

> **'Companies like General Accident and Commercial Union are no longer around, and their successors Aviva and Royal & SunAlliance are pulling away from writing multinational risks, which require large global networks.'**
>
> *David Gamble*
> *Assn. of Insurance & Risk Managers*

The membership of London's International Underwriting Assn. today, for example, totals just over 40 companies, compared with the more than 150 insurers and reinsurers that comprised the London company market two decades ago.

Major American and European insurers and reinsurers—such as American International Group Inc., Munich Reinsurance Co. and Swiss Reinsurance Co.—still retain a strong presence in the London company market.

But gone are what once were dozens of small London operations of insurers and reinsurers from around the world, and also gone are a host of British insurance and reinsurance companies whose names are now history, owing to consolidation.

Aviva P.L.C., an amalgamation of some of the United Kingdom's biggest multiline insurers—including General Accident P.L.C., Norwich Union P.L.C. and Commercial Union P.L.C.—has abandoned the London market and large commercial business in favor of personal insurance, health and life insurance and small to medium-sized commercial risks.

While Aviva underwrites more than 7,000 small to medium-sized businesses—such as florists and plumbers, as well as some large property accounts, including Manchester United Football Club's famous Old Trafford football ground—the company has opted out of insuring multinational business and the London market business, said a spokesman.

"We decided to withdraw from large commercial business and the London market because of the cyclical market," he said, noting that it chose to concentrate on less-volatile lines, such as household and motor insurance.

The United Kingdom's other remaining major multiline insurer, Royal & SunAlliance P.L.C., has vowed to continue on in the commercial insurance sector and also operates in the London market. In 2003, it pulled out of the U.S. domestic market and is now focusing on multinationals based in the United Kingdom and elsewhere in Europe.

Consolidation in both the London and U.K. markets has resulted in a big reduction in the number of carriers for buyers in a centralized location.

"The reduction of choice is a big issue for risk managers. There are a very small number of players, particularly for certain classes of business, such as directors and officers insurance," said David Gamble, executive director of the Assn. of Insurance & Risk Managers.

"The market has contracted enormously, particularly for multinational companies," agreed David O'Ryan, a partner of JLT Risk Solutions Ltd.

"Companies like General Accident and Commercial Union are no longer around, and their successors Aviva and Royal & SunAlliance are pulling away from writing multinational risks, which require large global networks," he said.

Buyers for multinational companies must either choose from among a much more limited number of global insurers in the London company market today or opt to manage their risks in a less-central-

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Consolidation: London market offering reduced choices

Continued from page 17

ized way, said Mr. O'Ryan.

Despite the reduction in the number of insurers operating in the company market, London continues to be an important market for multinational buyers, said Mr. O'Ryan, pointing out that there remains a concentration of expertise for specialist risks in the Lloyd's and London company market.

Consolidation has meant that brokers and buyers have to work hard at maintaining relationships among the more-limited pool of insurers in the market, he said, explaining that, with fewer choices, buyers and brokers cannot afford to alienate sections of the market.

Brendan McManus, commercial insurance director for London-based Royal & SunAlliance P.L.C., stressed that even though it has realigned its underwriting focus, RSA remains an active participant in the London market and a leading insurer for multinational companies based in the United Kingdom and European Union.

'We are a Bermuda-incorporated company, quoted in the U.S., with our heart and soul in the London and U.K. market.'

Chris O'Kane
Aspen Insurance U.K. Ltd.

"Royal & SunAlliance has operations and partnerships in 130 countries," Mr. McManus said, pointing out that it is able to service its multinational clients throughout the world.

However, while "five years ago, we were looking at multinationals domiciled throughout the world," the company now is focusing on U.K. and European multinationals, he said.

Moreover, "we are looking for clients who want more than just to transfer their risk. We want to be able to risk-engineer, to provide physical and financial risk management," said Mr. McManus.

He denied that RSA's withdrawal from the U.S. domestic market would hinder its ability to service European clients with a strong U.S. presence.

"We are finalizing an arrangement in the U.S. that will allow us to continue to serve our multinational clients in the U.S.," he said, noting that it was too early to provide details of the new arrangements.

Mr. McManus agreed, though, that multinational buyers face a reduction in choice because of "a lot of consolidation in the London market."

However, "there may be some disaggregation" now happening with new capital coming into the London market, said Mr. McManus.

Many of the London market's recent entrants come from Bermuda's growing array of insurers and reinsurers, as well as from Lloyd's of London, as several Lloyd's agents establish separate London-based companies.

One of the new breed of London-market companies is Aspen Insurance U.K. Ltd.

Established two years ago "to meet the needs of the London and wider U.K. market," Aspen now claims to be the largest independent reinsurer in the United Kingdom.

Aspen Holdings Ltd. is based in Bermuda and listed on the New York Stock Exchange last December with $990 million in shareholder equity. The main shareholders of the company are The Blackstone Group, Candover Partners Ltd., Credit Suisse First Boston Private Equity and Lloyd's insurer Wellington Underwriting P.L.C.

Aspen also has set up Aspen Specialty Insurance Co. and Aspen Re America Inc. with offices in New Jersey and Connecticut.

"We are a Bermuda-incorporated company, quoted in the U.S., with our heart and soul in the London and U.K. market," said Chris O'Kane, chief executive officer.

Although the company's premium income currently stands at 70% reinsurance and 30% insurance, Mr. O'Kane predicted that insurance premiums eventually would represent 50% of the group's overall premium volume.

Aspen does not have the global infrastructure of competitors such as AIG or Zurich Financial Services Group, but, with its London market presence, it can provide valuable capacity for multinational companies coming to London, particularly for more-hazardous and difficult-to-place risks, said Mr. O'Kane.

The recent tight property/casualty market also has attracted new companies to the London market to provide capacity for small to medium-sized British companies.

Several of these new players were spawned by the Lloyd's market.

The latest entrant is Catlin Insurance Co. Ltd., which was formed earlier this year to write business incepting June 1, 2004.

The Catlin Group, which is also based in Bermuda, comprises a Lloyd's syndicate, a Bermuda company and the London company.

"We saw a need for capacity and quality underwriting in the U.K. company market after several of the composite insurers merged or pulled out," said a Catlin spokesman.

Most small to medium-sized businesses are unused to dealing with the Lloyd's market and would feel "more comfortable" dealing with a company rather than a Lloyd's syndicate, said the spokesman.

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Commentary

Global warming chiller draws heat

Some people will complain about anything.

There's a lot of quibbling, for instance, over the scientific accuracy of the film "The Day After Tomorrow," in which global warming locks the Northern Hemisphere in a new ice age in the space of about a week, give or take a few days.

Let's face it: Geologic time doesn't lend itself to breakneck storytelling. If greenhouse gases have to melt the polar icecap, disrupting ocean currents and creating superstorms that wreak havoc around the globe before funneling 150-degree-below-zero air from the upper atmosphere to freeze everything, it'd better happen quickly.

Climate experts, possibly including some catastrophe modelers, are apparently laughing up their sleeves at this scenario, but I found it totally convincing. So much about the movie was utterly realistic.

Douglas McLeod

Its paleoclimatologist hero, Jack Hall, for example, first predicts drastic climate change over the course of the next 100 years, then reviews some new data and realizes that it's actually going to happen before his next mortgage payment is due. This level of mathematical certainty should be familiar to anyone who's followed insurance company reserving practices.

With a wall of water descending on Manhattan, it's impossible to find a cab.

Fox News stays on the air through much of the chaos, thanks to the mass of warm air surrounding Sean Hannity and Bill O'Reilly.

Canada remains a relatively cold place.

These are all indications that the filmmakers were serious about documentary realism. Unfortunately, director Roland Emmerich had to stick to his story of Jack Hall slogging across New Jersey to reach his teenage son, Sam—who is rapidly being buried by snow in the New York Public Library—to give the movie the appearance of an actual narrative. Otherwise, he might have expanded it to paint an even more believable picture of people coping with worldwide disaster.

In a movie like that, Larry Silverstein might file property claims for the rest of his New York buildings, arguing that the flood and subsequent freezing are two occurrences.

The National Assn. of Insurance Commissioners, meeting in New York, might be encased in an ice-shrouded hotel. There would be no discernable change in the pace of their work.

President Bush could resume his push for oil drilling in the Arctic National Wildlife Refuge, which would now include most of Texas and Oklahoma.

American International Group Inc. Chairman Maurice R. Greenberg would be in Brazil when catastrophe strikes, but AIG's New York-based senior management would be lost, requiring Mr. Greenberg to remain at AIG's helm throughout the next ice age.

A.M. Best Co. would frantically downgrade ratings of property catastrophe reinsurers until its offices go ominously silent.

Life for risk managers wouldn't necessarily be easier with the Northern Hemisphere turned into a giant glacier.

Anyone whose company had no operations south of the equator would, of course, be out of a job. Loss adjusters would be scarce. Most major captive domiciles would be underwater—along with most captives—leaving Vanuatu as the only viable option.

Conversely—and I don't mean to sound Pollyannaish—think of the things risk managers wouldn't have to worry about any more. Superfund liability reform and the Fairness in Asbestos Injury Resolution Act? Forget them. Runaway juries in Texas state courts? It would be a cold day in those judicial hellholes. Compliance with the Health Insurance Portability and Accountability Act? Not portable to the Southern Hemisphere. And when Sam and his friends at the library have to burn books to stay warm, what are the first to go? Volumes of the U.S. Tax Code.

Still, I don't suppose even the demise of the Assn. of Trial Lawyers of America would tempt many people to have second thoughts about an ecological cataclysm.

That being the case, it's a good thing "The Day After Tomorrow" is just a story. And come to think of it, there may be one or two things about the movie that strain credibility. (I'm not talking about the scene where Sam finds a half-submerged working pay phone to call his dad.)

The script has the Mexican government, for instance, refusing to let hordes of American survivors cross the border until whatever is left of the U.S. government agrees to forgive Mexico's debt. Mexico could easily have held out for the return of California.

The real whopper comes toward the end of the film, though, when the U.S. vice president, clearly modeled on Dick Cheney, delivers a TV address—to the millions of Americans in Mexican refugee camps who don't have TVs—in which he apologizes for being wrong about global warming.

Come on. Do the filmmakers think we were born the day before yesterday?

Senior Editor Douglas McLeod can be reached at dmcleod@businessinsurance.com.

Comings & Goings

Mr. Francis

Mr. Edgren

Mr. Jones

Insurers:

Napa, Calif.-based The Doctors Co., a physician-owned medical malpractice insurer, has named **Robert D. Francis** as chief operating officer. Previously, Mr. Francis was president of Red Mountain Casualty Insurance Co.

Also at The Doctors Co., **David G. Preimesberger** has been named chief financial officer. Previously, Mr. Preimesberger was CFO and senior vp-financial and information technology for Cooperative of American Physicians Inc.-Mutual Protection Trust.

Clarendon Insurance Group has named **Bryan T. McCully** as senior vp of claims. Before his promotion, Mr. McCully was vp of claims, overseeing New York-based Clarendon's commercial and workers compensation programs, and president of Clarendon's third-party claim administrator subsidiary, North American Risk Services Inc.

James E. Taylor will replace Mr. McCully as president of NARS. Previously, Mr. Taylor was vp and director of claims at NARS.

Brokers:

Dennis Webber has joined Fort Worth, Texas-based Wm. Rigg Co. as a senior vp. Mr. Webber was the founder of The Webber Insurance Agency, which was acquired recently by Wm. Rigg Co.

Savannah, Ga.-based Palmer & Cay Inc. has made two senior-level appointments at its Grand Rapids, Mich., office. **Roger C. Edgren** has been named senior vp and branch manager. Previously, he was managing director and benefits practice leader for Marsh USA Inc. Also, **Robert W. Jones** has been named senior vp of the property/casualty division. Previously, Mr. Jones was national coordinator of a group captive for Marsh USA.

Other providers:

Steven R. Wasserman has been named vp and CFO of mbi, a Waltham, Mass.-based provider of health care benefit cards. Before joining mbi, Mr. Wasserman was vp of finance and CFO for ON Technology Corp.

Richard P. Marshall has been named president and CEO of Phoenix-based Camelback Captive & Risk Management Services L.L.C. Previously, Mr. Marshall was captive insurance administrator for the Arizona Department of Insurance.

John Hawkins has been named senior vp-East region manager for the Frank Gates Cos., a national third-party administrator based in Dublin, Ohio. Previously, Mr. Hawkins was vp-East region manager.

Lenexa, Kan.-based LabOne Inc. has promoted **Philip A. Spencer** to the position of executive vp-health care marketing. Previously, Mr. Spencer was senior vp of the diagnostic and case management services provider.

Los Angeles-based claims administration and adjusting firm David Morse & Associates has hired **Adolph Hernandez** to lead its risk services division. Previously, Mr. Hernandez was the manager of the San Bernardino, Calif., branch of Carl Warren & Co.

Jonathan F. Bank has joined the Los Angeles office of law firm Lord, Bissell & Brook L.L.P. as of counsel. He will focus on reinsurance and insurance dispute resolution. Mr. Bank most recently was senior vp of Tawa Associates Ltd., an insurance runoff management company, for which he will remain outside counsel.

New York-based Deloitte & Touche L.L.P. has made two senior-level appointments: **Byron O. Spruell** has been named national director of Deloitte's Business Insurance Consulting group, and **John Sordillo** has been named a principal in the company's Reorganization Services Group. Previously, Mr. Spruell was principal in Deloitte's Houston office, while Mr. Sordillo was senior restructuring advisor for AlixPartners L.L.C.

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Where Is YOUR AD?

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Ireland introduces system to reduce litigation over workplace injuries

By SARAH VEYSEY

DUBLIN, Ireland—A new system for resolving employee injury claims in Ireland is expected to reduce litigation and, ultimately, to lower companies' insurance costs.

The Personal Injuries Assessment Board, which the Irish government set up last year, came into force on June 1 to deal with workplace injury and illness claims.

Under the PIAB's rules, an employee seeking compensation for a work-related injury must, as a first step, file a claim with his or her employer. If the employer and worker cannot agree on a settlement, the claim is then referred to the PIAB, which will determine the appropriate settlement amount if the employer accepts liability for the incident.

PHOTO: REUTERS/ERIKO SUGITA

'Less litigation will result in... cheaper insurance premiums.'

Mary Harney
Department of Enterprise, Trade and Employment

If, after the PIAB's assessment, there is still a dispute over liability or the settlement amount, the claim will then proceed to court.

Under the previous system, disputed claims went straight to court.

"The sole aim of the PIAB is to eliminate expensive litigation costs and so to deliver compensation to claimants more quickly and more cheaply than in the past," Mary Harney, minister for Enterprise, Trade and Employment and the Irish vice prime minister, said in a statement.

"Less litigation will result in a greater proportion in the victim's pocket and in cheaper insurance premiums," she added.

The PIAB will assess claims using a recently developed tool called the "Book of Quantum," a publicly available document that assigns compensation levels for particular injuries. This tool can also be used a guide for individuals seeking to settle claims directly with their employers, the board noted.

Ms. Harney stressed in her statement that the PIAB was set up to reduce litigation costs and not to cut compensation paid to those injured in the workplace.

The PIAB has a 12-member inter-

See PIAB/next page

Australia to boost its regulation of foreign insurers

By ELIZABETH FRY

CANBERRA, Australia—Foreign insurers offering coverage in Australia will face tighter regulatory controls following the release late last month of the recommendations of an official review of offshore insurers.

The review recommended that foreign insurers that lack an Australian branch or subsidiary be allowed to continue to market their products in Australia only if they are based in a country that has insurance regulation comparable to Australia's.

Any direct foreign insurer based in a country not deemed to have regulation comparable to Australia's would have to operate through a branch or subsidiary in Australia regulated by the Australian Prudential Regulation Authority. The government did not indicate which countries would or would not be regarded as having regulatory requirements that are comparable to Australia's.

The review, which was conducted by Gary Potts, a former executive director of the Department of the Treasury, was set up in September 2003 following recommendations from the royal commission that investigated the 2001 collapse of HIH Insurance Ltd.

Currently, "direct offshore foreign insurers," or DOFIs, can sell their products in Australia provided they are sold through licensed brokers or agents. Foreign insurers are exempt from the Insurance Act because they do not operate branches in the country and are not considered to be "carrying on insurance business in Australia."

But according to the review by Mr. Potts, the concept of "carrying on insurance business in Australia" lacks consistency and does not reflect the implications of the internationalization of insurance services.

Mr. Potts concluded that changes were needed with regard to Australia's regulatory approach because the degree of protection afforded to policyholders for exactly the same insurable risk will vary depending on the insurer's home country.

The government said it will implement the recommendations but gave no timetable for the introduction of the changes.

The changes drew criticism from the Insurance Council of Australia, a Sydney-based insurer trade association.

The ICA's deputy chief executive, Dallas Booth, said any company selling insurance into the Australian market should be fully regulated by APRA.

"Following recent changes to the Insurance Act, ICA believes Australia is now a world leader in prudential regulation, and we have reservations about which jurisdictions would be consid-

See CONTROL/next page

PHOTO: NEWSCAST

A parliamentary report warns that the U.K. government's planned locations of offshore wind farms would increase shipping accidents.

Report: Proposed U.K. wind farms a danger to ships

By PETA MILLER

The U.K. government's planned locations of offshore wind farms would increase the risk of shipping accidents, a parliamentary report warns.

The United Kingdom has committed to meeting 10% of its electricity needs from renewable sources by 2010 as part of its agreement to the 1997 Kyoto Protocol, under which participating nations agreed to limit their production of so-called greenhouse gasses.

The U.K. government plans to meet that energy target largely through the use of wind farms, according to a report from the Transport Committee, a cross-party parliamentary committee. However, all of the offshore wind farm sites that have been identified are located on the approach to major ports and, therefore, would pose a collision risk, the committee warns.

"Consents should only be granted to installations which can be shown not to compromise the safety of navigation," states the paper. "If the research needed to achieve this has not yet been done, then the consents will have to be delayed," it continues, noting that the Department for Transport and the Maritime and Coastguard Agency should have been represented on the environmental assessment group that identified potential sites.

The committee also said that plans to deal with collisions should be drawn up, because such incidents are "inevitable" once the wind farms are in place.

World Updates

Former Equitable CEO banned until 2010

The Financial Services Authority has banned Christopher Headdon, former chief executive of Equitable Life Assurance Society, from holding any management position at an FSA-regulated company until 2010. The U.K. regulator said the ban stemmed from Mr. Headdon's failure to disclose to the FSA details of a "side letter" that "raised questions about the true value of a reinsurance contract entered into by Equitable." Mr. Headdon's failure to inform the regulator of the existence of the side letter was deliberate, the FSA statement said. In July 2000, the House of Lords ruled that Equitable owned guaranteed annuity rate policyholders about £1.50 billion ($2.27 billion). The company closed to new business in December of that year.

Bahrain licenses first captive manager

The Bahrain Monetary Agency has granted the first license for a captive management company in the country. Manama, Bahrain-based investment advisory firm Stratum W.L.L. received the license. The BMA said in a statement that rules for establishing captives in the domicile are being developed and are expected to take effect next year.

S&P says reinsurers will alter writings

Reinsurers will likely reduce their exposures in some lines of business as rates continue to soften, according to a report by Standard & Poor's Ratings Services in London. While underwriters will face pressure from brokers, cedents and shareholders to maintain their levels of premium volume, some large reinsurers have already stated their intention to reduce premium volume in certain areas, Stephen Searby, a credit analyst at S&P in London, said in a statement. Such action is necessary "in order to avoid a repeat of the severe damage done to reinsurers' financial strength in the last soft cycle," he said.

Briefly noted

General Re Corp., a unit of Berkshire Hathaway Inc., has been granted a license to operate as a nationwide reinsurer in China. General Re's branch office will be based in Shanghai....London-based broker **Cooper Gay Group** has opened an office in Birmingham, Ala. The office will serve as a hub for the brokerage's wholesale operation for the Southeast United States.

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PIAB: New system

Continued from previous page

im board of management that includes representatives from employer groups, labor unions, and health and safety experts.

Tony Briscoe, assistant director of the Dublin-based Irish Business & Employers Confederation, said employers welcomed the creation of the PIAB.

The system should result in claims being settled more quickly, he said. Mr. Briscoe noted that the PIAB has said it aims to resolve claims within nine months; previously, claims could take as long as four years to progress through the courts, he said.

As a result, new approach should significantly reduce litigation costs, which previously accounted for as much as 40% of some employers liability claims, he said.

"One of the problems that has bedeviled the personal injury system in Ireland has been the high level of legal costs," noted Michael Horan, manager for nonlife insurance at the Dublin-based Irish Insurance Federation.

Employers' legal costs will be significantly reduced under the new system, he said, which "will lower insurers' expenditure. And that, in turn, will lower insurance premiums."

Furthermore, any acceleration of the settlement of claims will help insurers in pricing risks, he noted.

The scope of the PIAB will be extended to public liability and auto claims in the fall, according to the Department of Enterprise, Trade and Employment.

Control: Regulation

Continued from previous page

ered comparable. There is also a question of how much a regulator in another country would take into account the needs of Australian policyholders, particularly in the event of a collapse," he said.

Mr. Booth said there should be a level playing field for APRA-authorized insurers in Australia and DOFIs to protect all policyholders.

But Judy Harriss, insurance manager for Sydney-based utility company AGL Ltd., welcomed the reforms.

"As long as the insurer is domiciled in a country with a similar regulatory regime, they don't need to be regulated here, especially if APRA has an overview," said Ms. Harriss, who is also president of the New South Wales chapter of the Assn. of Risk & Insurance Managers of Australasia Ltd.

But risk managers will still have to conduct their own due diligence of insurers, regardless of the regulatory changes, she said.

A second report, released concurrently with the Potts review, assesses the merits of introducing a limited explicit guarantee into parts of the Australian financial system and how that would work.

The report, prepared by Kevin Davis, professor of finance at the University of Melbourne, does not make any recommendations, but notes that Australia is one of only two countries in the Organization for Economic Cooperation and Development that does not have an explicit guarantee.

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Washington State Ferries (WSF), a division of the Washington State Department of Transportation, operates the largest ferry fleet in the U.S. WSF is seeking Third Party Administrator (TPA) services for the following types of claims: (i) Incident Only Claims; (ii) Cure Only Claims; (iii) Maintenance and Cure Claims; (iv) Assumed Claims; and (v) assistance with Tort Claims, as assigned. WSF requests proposals from firms who have: (i) experience in providing Jones Act claims administration services; and (ii) a local office in Puget Sound, Washington.

The proposal due date/time is 3:00 p.m. on July 7, 2004. On or after June 8, 2004, the RFP Package will be available upon request to the following office for the **non-refundable** fee of $25.00. The RFP will also be posted at **www.wsdot.wa.gov/ferries/contracts** on or after June 8, 2004.

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LEGAL NOTICE

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE PETITION OF MALCOLM L. BUTTERFIELD
AND ANTHONY J. MCMAHON,
AS JOINT PROVISIONAL LIQUIDATORS OF
BELVEDERE INSURANCE COMPANY LIMITED,
DEBTOR IN A FOREIGN PROCEEDING
CASE NO. 98-B-47660 (REG)

NOTICE IS HEREBY GIVEN THAT ON MAY 27, 2004, THE BANKRUPTCY COURT ENTERED AN ORDER (THE "ORDER") CONTINUING THE PRELIMINARY INJUNCTION ORDER PURSUANT TO 11 U.S.C. § 304 ORIGINALLY ENTERED IN THIS CASE ON NOVEMBER 4, 1998. THE ORDER SHALL REMAIN IN EFFECT PENDING A HEARING TO CONSIDER WHETHER IT SHALL BE CONTINUED, WHICH HEARING IS SCHEDULED TO BE HELD ON NOVEMBER 17, 2004 AT 9:45 A.M. (THE "RETURN DATE") BEFORE THE HONORABLE ROBERT E. GERBER, IN ROOM 620 OF THE ALEXANDER HAMILTON CUSTOM HOUSE, ONE BOWLING GREEN, NEW YORK, NEW YORK. ALL PAPERS SUBMITTED FOR THE PURPOSE OF OPPOSING CONTINUATION OF THE ORDER AFTER THE RETURN DATE SHALL BE FILED WITH THE COURT, WITH A COPY TO THE CHAMBERS OF THE HONORABLE ROBERT E. GERBER AND SERVED ON COUNSEL FOR THE PETITIONERS LISTED BELOW, SO AS TO BE RECEIVED AT LEAST FOURTEEN (14) DAYS PRIOR TO THE RETURN DATE. ANY PERSON WISHING TO OBTAIN A COPY OF THE ORDER SHOULD CONTACT COUNSEL TO THE PETITIONERS.

CHADBOURNE & PARKE LLP
ATTORNEYS FOR THE PETITIONERS
30 ROCKEFELLER PLAZA
NEW YORK, NY 10112
(212) 408-5100
ATTN: HOWARD SEIFE, ESQ.

LEGAL NOTICE

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK
In re:
SEFTON PARK INSURANCE LIMITED
(Petition of Malcolm L. Butterfield)
Case No.: 02-12934 (BRL)

PLEASE TAKE NOTICE that on May 25, 2004, the Bankruptcy Court entered an order continuing the Preliminary Injunction Order (the "Order") pursuant to 11 U.S.C. § § 105 and 304(b) originally entered in this case on November 7, 2002. The Order shall remain in effect pending a hearing scheduled for November 17, 2004 at 10:00 a.m. before the Honorable Burton R. Lifland in the Alexander Hamilton Custom House, One Bowling Green, New York, New York. Any person wishing to obtain a copy of the Order should contact Theresa D'Agostino at (212) 610-6300.

ALLEN & OVERY LLP
1221 Avenue of the Americas
New York, New York 10020
Tel: (212) 610-6300
Fax: (212) 610-6399
Attention: Ken Coleman
Stephen Doody

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Regulations: Saudi Arabia seeks to reform market

Continued from page 3

organizations plan to submit their queries and views on the law to the conference.

Under the law, insurance and reinsurance companies have to be licensed by SAMA and meet minimum capital requirements. Service providers such as brokers, actuaries and insurance advisors will also have to be licensed. Previously, there was little regulation of insurers and brokers in the country.

The capital requirements vary depending on the type of business that is written, but the minimum capital for an insurance company is 100 million riyals ($26.6 million) and the minimum capital requirement for a reinsurer or an insurer writing both insurance and reinsurance is 200 million riyals ($53.2 million).

The law also requires that Saudi companies retain 30% of the programs they insure and that they reinsure 30% of the risk with Saudi reinsurers. It is this provision of the law that is causing concern to international insurers and their Saudi-based policyholders, brokers and insurers say. Currently, many large projects in the country are fronted by local insurers, but most of the risk is reinsured in international markets.

Saudi and foreign oil companies with exposures in the country likely will have to be exempted from the local insurance provision, as Saudi insurers will not have sufficient capacity to retain 30% of some of huge energy-related risks, said Mike Bignell, a director of consulting at Miller Insurance Services Ltd. in London.

If the insurance provision is enforced, it could greatly increase the self-insured retentions of energy companies operating in Saudi Arabia, he said.

The London Market Brokers Committee in London last week sent a letter to SAMA to welcome the Saudi initiative on insurance, but also to seek further clarification of what specific provisions of the law mean in practice, said David Hough, executive director of the LMBC in London.

In particular, Mr. Hough said, the LMBC questioned how the requirement to insure and reinsure 30% of programs with Saudi-registered companies would work in practice.

The LMBC is also seeking more information about a provision in the law that requires SAMA to give written approval before Saudi-registered companies can deal with Lloyd's of London brokers or other foreign companies.

Some LMBC members also would prefer to handle reinsurance on a cross-border basis without having a Saudi operation, but are unsure whether that would be possible under the new law, Mr. Hough said.

In general, however, the new regulations are a positive step in the development of an insurance market in Saudi Arabia, said Bob Humphries, former managing director of Aon Saudi Arabia, who is now responsible for developing business in the Middle East out of Aon Ltd.'s London office.

> **'The most radical part is that, until now, there has been no regulation of the insurance market.'**
>
> *Bob Humphries*
> *Aon Ltd.*

"The most radical part is that, until now, there has been no regulation of the insurance market. There was only one company in Saudi Arabia; all the rest were operating from outside, mainly from Bahrain," said Mr. Humphries referring to state-owned insurer National Company for Cooperative Insurance.

"But new regulations are coming in with stringent requirements on capitalization for local insurance companies, and the result is that buyers and brokers will need to maximize the use of the local insurance market before they can look to place any reinsurance outside the kingdom," he said.

Further reforms of the market are expected to lead to an expansion in the number of local insurers.

Though the law seems to include some provision to allow policyholders to seek more coverage outside the county when there is insufficient local capacity, it is not clear how that would be triggered, Mr. Hough of LMBC added.

The new law is a positive development for Saudi Arabia's insurance market, agreed Mr. Bignell of Miller.

The rules and regulations will lift the profile and professionalism of the insurers and brokers conducting business in the country, he said.

But, he suggested "there will be quite a shake out" and the market will get smaller. Major brokers will continue with their existing joint ventures, mostly headquartered in Bahrain, but the regulations may force smaller brokers, including many tiny brokerage operations in Saudi Arabia itself, to withdraw from the market, he said.

Other observers are more critical of the law.

The positioning of the law with respect to insurance is "disappointing" says David Snyder, vice president and assistant general counsel of Washington-based American Insurance Assn., which has also been reviewing the law.

"There are no guarantees about branching, that foreign companies will be able to establish offices in the country without going through the full licensing requirements," he said.

Capitalization requirements also seem quite high and the whole process is not transparent, he said. In addition, a number of articles of the law seem to provide for intrusive government approvals of day-to-day business decisions.

"From what we understand, it falls well short of international norms and the system that would be beneficial for Saudi and foreign players," he said.

The AIA will lobby the U.S. government to seek changes to the law as it participates in negotiations over Saudi Arabia's application to join the World Trade Organization, Mr. Snyder said.

Lloyd's, which has business worth $200 million in gross premiums with the kingdom, declined to comment on the law, saying it is still reviewing the legislation.

Energy companies with exposures in Saudi Arabia declined to comment on the new law.

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The deadline for completed entries is July 26.
To download the EBC rules and entry form, go to www.businessinsurance.com or for an electronic version, **e-mail: bobrien@crain.com**

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Business Insurance

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Survey: Insurers vow pricing, underwriting discipline

Continued from page 4
utives from stock companies, which accounted for 45% of the respondents, said they anticipate a combined ratio below 95% for 2004-2005, while 25% said they expect a combined ratio in the range of 95% to 100%, the survey found. Only 6% said they anticipate a combined ratio between 105% and 110%.

Responses from mutual insurance company executives indicate similar expectations. Seventy-three percent of the mutual respondents said they anticipate combined ratios below 100%, with 21% expecting ratios below 95% and 52% expecting ratios between 95% and 100%. Twenty-six percent of the executives said they expect their combined ratios to be within the range of 100% to 105%.

"The number of companies that are targeting (combined ratios) below 95% is skyrocketing," said Dom Addesso, the president of American Re's direct treaty unit. "Whether or not that is achievable remains to be seen. But, certainly, where they are setting the bar is increasingly aggressive, and that's a good sign."

At the same time that most executives are optimistic about their companies' financial outlook, 40% said they expect the hard market to last only through 2004. Eighteen percent said they believe the hard market is over, while 28% said they expect the market to continue through 2005. The remaining respondents said they expect the hard market to last through 2006 and beyond.

But despite a predicted end to higher premium rates, "there seems to be plenty of resolve to maintain adequate pricing and terms and conditions," Mr. Addesso noted. "To us, that's very good news," he said.

Indeed, when asked about the three most critical issues their companies face, 53% of the executives cited maintaining underwriting discipline and price adequacy. The other two top critical issues identified were maintaining their company ratings and the cost and coverage of their reinsurance programs; both were cited by 30% of the executives.

Meanwhile, 63% of the executives said that an insurer's underwriting capability—defined as its risk selection and pricing—is its main competitive advantage, followed by claims processing and claims management, which was cited by 40% of the respondents. Policy processing and a strong capital position tied for third place; 30% of the executives chose each of those responses.

When asked what three areas of their companies needed improvement, 35% cited underwriting capability, followed by planning, which received a 30% response. Policy processing and a strong capital position were both cited by 28% of the respondents.

When it came to the primary insurance industry in general, 40% of the executives said that the ability to file and use adequate rates in accordance with state regulations is the most critical factor faced by the industry today. Low interest rates and capital market returns were each cited by 38% of the executives as critical factors for the industry currently, while restrictive state regulation was cited by 33% of the executives.

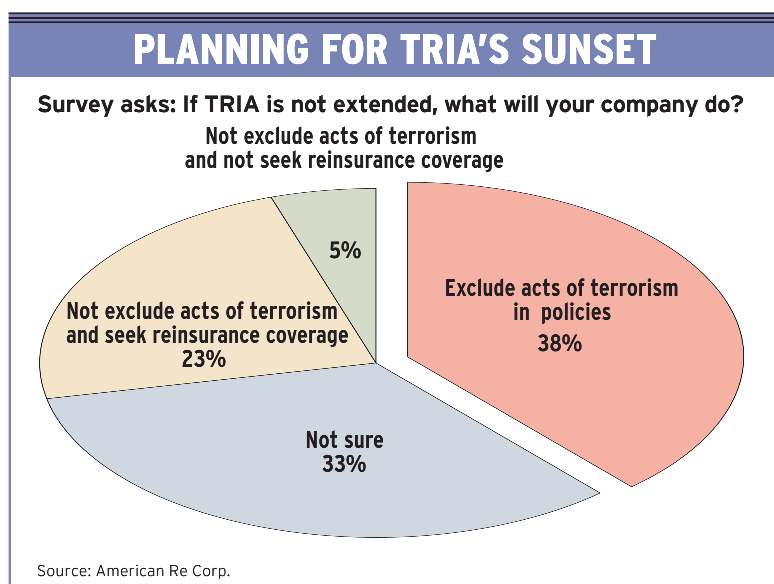
Meanwhile, the executives ranked general tort reform as the highest priority for congressional action. Asbestos liability reform and the reauthorization of the Terrorism Risk Insurance Act tied, being cited as the second-highest congressional priorities. Medical malpractice reform, reform of the Sarbanes-Oxley Act and optional federal chartering of insurers filled out the list.

When asked in more detail about the future of TRIA, 55% of the executives said it should be renewed as it is, while 33% said it should be renewed with modifications. Only 5% said it should be allowed to sunset.

If TRIA were allowed to expire, 38% of the executives said their companies would exclude acts of terrorism in their policies, while 23% said they would not add terrorism exclusions and would seek reinsurance coverage. Thirty-three percent said they were not sure how their companies would respond, while 5% said they would neither exclude acts of terrorism in their policies nor seek reinsurance.

"There really is not much of a resolve to take this on independently," Mr. Addesso said, speaking of terrorism exposures. "No one really has the capital capacity to do that. TRIA certainly was a unique way of covering what could be a very large catastrophic exposure for the industry and any single company. And there's been no industry movement to provide any alternative solutions; therefore, individual companies have (little) choice but to encourage their trades to press the politicians for renewal."

Copies of American Re Corp.'s survey results can be obtained by contacting Christine Skurbe by telephone at 609-243-5558 or by e-mail at cskurbe@amre.com.



Source: American Re Corp.

California: Not all impressed with comp rate savings

Continued from page 4
works for workers comp injuries, and the introduction of approved guidelines for treating occupational injuries.

Many insurers are still calculating midyear renewal rates in light of the reforms.

But some insurers have indicated that they expect to implement rate reductions of about 10%, said Mark Zwickel, executive vp at Lockton Insurance Brokers Inc. in Los Angeles.

Zenith National Insurance Corp. in Woodland Hills, Calif., already has announced that it will cut rates by an average of 10% for workers comp policies renewing July 1.

The insurer's announcement drew criticism from California Insurance Commissioner John Garamendi.

"Some companies, Zenith included, have decided they want to be cautious, which means they want to pocket the savings and take it to their bottom line rather than pass it though," the commissioner said at a recent press conference. "That is wrong."

The commissioner, however, can only issue advisory rates, not mandate what rates insurers must follow.

Zenith's 10% rate cut "is probably going to be the barometer where the industry falls," said Jim Little, chairman, president and chief executive officer for Employers Direct Insurance Co. in Westlake Village, Calif.

Employers Direct plans to comply with Mr. Garamendi's call to reduce pure premium rates by 20.9% for July renewals, he said. The specialty workers comp insurer will achieve that target by lowering its rates another 6% in July, having already cut its rates by about 15% during January 2004 renewals, Mr. Little said.

But Employers Direct is atypical among workers comp insurers in California because it was formed in 2003, with financing from Swiss Reinsurance Co. and other investors, and so does not have years of indemnity claims that it must fund, Mr. Little said.

Others say it is too early to tell how some of the reforms will play out, noting that some reforms do not take effect until Jan. 1, 2005, and regulations for the implementation of other measures have yet to be adopted.

The risk manager for a Los Angeles company insured by CNA Insurance Cos. with a July 1 renewal said she does not expect a rate decrease at renewal. In fact, her broker has told her to expect an increase of about 10%. But that is an improvement over the 30% to 40% increases she has experienced in recent years, said the risk manager, who asked not to be identified.

Because her account is experience-rated, the risk manager said, it will take time for some of the reforms to affect her rates.

"To the extent that all of these wonderful benefits from the reforms will not pan out until future years, you cannot really demand that the insurers give you a reduction now," she said. "You have to show them your experience really got better, then your rates will be adjusted accordingly."

A spokesman for Zurich said the insurer does not expect the reforms to have "a tremendous impact on midyear renewals."

> **'Some companies, Zenith (National Insurance Corp.) included, have decided they want to be cautious, which means they want to pocket the savings and take it to their bottom line rather than pass it through. ...That is wrong.'**
>
> *John Garamendi*
> *California Insurance Commissioner*

"We have strict underwriting guidelines for workers comp in California to begin with...so as far as where rates are going to go, we really have to wait and see how things get implemented," the spokesman said.

St. Paul Travelers Cos. Inc. expects to reduce rates for July renewals, but it is still too early to estimate how large the cuts will be, said Paul Ramont, vp of workers compensation product management in Hartford, Conn.

Some of the reforms will prove more difficult for insurers to implement than for large self-insured employers to do so, said Stanley R. Zax, chairman and president of Zenith National.

For example, beginning Jan. 1, 2005, employers will be able to direct injured employees to medical provider networks established by insurers or employers. But establishing a network for one large self-insured employer with employees concentrated in a few locations will be much easier than for an insurer, such as Zenith, which has 27,000 policyholder scattered across the state, Mr. Zax said.

It is "absurd to assume that an insurer will be able to direct all claimants to network doctors," Mr. Zax said.

Additionally, the reforms call for medical treatments to follow guidelines established by the American College of Occupational and Environmental Medicine.

But it remains to be seen whether doctors in the state will actually follow those guidelines, Mr. Zax said. If doctors already are applying "high standards of medicine" in treating injured employees, then big savings are not likely to result from adopting the guidelines, Mr. Zax said.

Reforms that require the establishment of networks will take time to produce cost reductions, agreed Guy Avagliano, a principal for Milliman USA in San Francisco.

But savings from some reform measures, such as the elimination of vocational rehabilitation benefits and the reduction, under certain circumstances, in the number of weeks that permanent disability benefits are paid, can be quickly determined and passed on to policyholders, he said.

The overall impact of the reforms will likely attract more insurers to California, insurers and brokers say.

Already, several insurers that previously did not write new accounts in California say they are now willing to provide a limited amount of capacity, said Mr. Zwickel of Lockton.

But "there is still a lot of caution on the part of the industry and still a lot of people licking their wounds from the price wars of '90s," said Mr. Little of Employers Direct. "So I don't think there is going to be a rush into the market. But I would say, come 2005, we will see a lot more players in the market and the rates starting to trend down as these reforms really kick in."

Meanwhile, legislative proposals to introduce rate regulation in California could undermine the reform efforts and deter new insurers from entering the state's workers comp market, several sources say.

Currently, there is a bill pending in Sacramento that calls for the creation of a Commission on Workers Comp Rate Regulation that would be authorized to set insurer rates. That measure, S.B.X4 16, is sponsored by Sen. Richard Alarcon, D-San Fernando.

"If the national carriers see an issue where there is going to be price controls and a political environment, I don't think they are coming back to this state," Mr. Little said.

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Forecast: Activity increasing

Continued from page 1

"Basically, we use a lot of history," said Philip J. Klotzbach, the research associate with the Tropical Meteorology Project who prepares the forecasts with Mr. Gray. "We basically look at global climate features that work well in forecasting previous years. Now we have data that goes back as far as 1948—we have more than 50 years of data to look at to see what worked well in forecasting previous years. We assume that what worked well in forecasting previous years will work well in forecasting future years. We look for features that work well in past years and try to explain why those features relate to tropical cyclone activity," he said.

Mr. Klotzbach said that he and Mr. Gray then perform statistical analysis to "try to bring in the physics of why those predictors work."

The team's track record has been generally solid. For example, the team's Dec. 5, 1998, forecast of the 1999 hurricane season predicted nine hurricanes; eight actually formed. The initial forecasts for 2000 and 2003 also deviated by only one hurricane from the number that formed.

But the initial forecast for the 2001 season, issued on Dec. 7, 2000, called for five hurricanes when nine actually formed. The initial 2002 forecast called for eight hurricanes, but only four formed.

"Some years are just a lot harder to forecast than others," said Mr. Klotzbach. "In 2002, we started forecasting a fairly active year and then as we got closer and closer to hurricane season it just looked less and less favorable. It turned out to be a fairly inactive year."

But the 2002 El Niño—a weather phenomenon that depresses Atlantic hurricane activity—turned out to be a lot stronger than initially thought, he said. "Since you're using statistics, there will always be years where you don't forecast well, but in general, they come out pretty well."

"There are always statistical anomalies," said Mr. Klotzbach. "You definitely learn more about how the atmosphere works when you go bust. You have to go back and see why our forecasts did not work. We are learning and improving our forecasts."

Even relatively inactive years like 1992 can pack a punch, he said. Only one major Atlantic hurricane formed that year, but it was Hurricane Andrew, the costliest hurricane in U.S. history.

The forecasts are updated throughout the season. In 2003, for example, the team issued five updates between April 4 and Oct. 2, 2003, in addition to the initial forecast the prior December and the post-season release of an actual tally for the year.

The most recent updated forecast for 2004, issued May 28, called for eight hurricanes forming during the current hurricane season, which began June 1 and lasts until Nov. 30. Three of those will become intense, according to the team. Both the number of hurricanes forecast and the number of intense hurricanes forecast was unchanged from the team's April 2 forecast.

In addition, the team forecast a 71% chance that a major hurricane will make landfall on the Atlantic or Gulf coast during this season, compared to a century average of 52%.

The Colorado State team is not alone in making predictions, though it has the longest track record. London's Tropical Storm Risk, founded in 2000, also issued a forecast on May 28, calling for 13 tropical storms, seven of which will develop into hurricanes. Like the Colorado State team, TRS forecasts three intense hurricanes.

The National Oceanic and Atmospheric Administration's National Hurricane Center began issuing seasonal predictions in 1999. This year, NOAA has predicted—on the basis of a joint project involving the hurricane center and two other NOAA units—between 12 and 15 tropical storms, with six to eight becoming hurricanes and two to four of those growing into major hurricanes.

The importance of the Gray team's forecasts lies in the trends they reveal, said Richard Thomas, senior vp and chief underwriting officer of American International Group Inc. in New York. AIG provides undisclosed financial support for Mr. Gray's research.

"When you look at the data he's collecting, you can discern broad trends," Mr. Thomas said. "Remember what we do as underwriters: we take a look at the past to determine how we can forecast the future. With Gray's work, he's accumulated significant historical data that he uses to makes his forecasts. And that's the value proposition in his work."

AIG sponsors the Gray team's research because "he has a demonstrated expertise and we see that as valuable," said Mr. Thomas.

"Whether he says there's going to be 13 storms this year or 14 storms this year is not the important feature," said Gary Kerney assistant vp of the Insurance Services Office Inc.'s Property Claim Services unit in Jersey City, N.J. "I think the value in what Dr. Gray and others are doing is that we are recognizing that we have been in a period since 1995 when hurricane activity has been significantly above average," he said.

William Gray, right, and his team of researchers at Colorado State University, including Philip J. Klotzbach, left, analyze a variety of climate and historical data to develop their hurricane forecasts.

PHOTO: AP WIDE WORLD

The forecasts "are keeping us mindful of the fact we are in period of time of very active hurricane seasons and will continue to face these kinds of very active hurricane seasons, possibly for another decade," said Mr. Kerney. "From the insurance industry point of view, we should be concerned with the Big Storm or…we should be concerned about a series of hurricanes making landfall and having the same cumulative effect. It's keeping us on our toes," said Mr. Kerney.

"If I'm responsible for some facility on the Atlantic Coast or the Gulf Coast, I should know that I have about one chance in 20 of having a hurricane come within 50 miles of the facility," said Mike Burke, vp and manager of catastrophe exposure for Factory Mutual Insurance Co. in Johnston, R.I.

"In a bad Gray year, maybe those odds drop down to one in 15 and in a good year, maybe they go up to one in 30. But the fact remains that those are all very short odds. If a high season scares you, then a low season should scare you as well. The advice we give our customers is understand what your risk is and understand that the risk is driven very much by weaknesses in the facility and that engineers can identify those weaknesses and there are smart solutions," said Mr. Burke.

"The statement about number of hurricanes being more likely this hurricane season, we believe, is less useful than if you knew the regional impacts of that forecast," said Lewis Rothstein, president and co-chief executive officer of Narragansett, R.I.-based Accurate Environmental Forecasting. The firm uses climate forecast data from NOAA to determine hurricane risks on a regional basis.

"We use a combination of numerical weather prediction technology, and statistical techniques. Dr. Gray's approach results in a regional description that is coarser than ours." he said. "Dr. Gray is certainly someone to be listened to, but we have a different approach," said Mr. Rothstein, who is also a professor of oceanography at the University of Rhode Island.

Risk managers' take on the value of the predictions varies widely.

"As a resident and risk manager residing in Florida, hurricanes present quite a risk to my firm," said Jim Dineen, director-risk management for NetBank Inc. in Jacksonville, Fla. "I do not necessarily follow Professor Gray's predictions—they haven't been all that accurate anyway—or anyone else's simply because predictions mean nothing. It only takes one hurricane to create a financial loss and, as such, we must be prepared to mitigate the loss due to that one event. Predictions as to the number of and possible size of hurricanes do not influence my decision-making process. It is an exercise in futility," he said.

"I've got a more global view—not just on Dr. Gray's predictions that are focused on hurricanes," said Lance J. Ewing, vp-risk management for Caesars Entertainment Inc. in Las Vegas. Caesars has properties in Atlantic City, N.J., and on the Gulf Coast, said Mr. Ewing, who is also immediate past president of the New York-based Risk & Insurance Management Society Inc.

"I'm looking at a broader stroke on weather forecasts. In my particular industry, I think it's necessary that we evaluate any type of potential disaster, and weather sometimes cannot be put in an actuarial box. For example, in California it is not 'if an earthquake,' but 'when an earthquake,' and how we prepare for that when is extremely important. The predictions are a piece of how we prepare," he said.

"Dr. Gray, for a number of years, had some very good insights and his batting average was really good. He seems to be in somewhat of a slump in recent years. That's not to say that we could not come out of that slump—his predictions are a piece of what I look at—it's not the Gospel truth," said Mr. Ewing.

The Gray forecasts are "very informative and useful," said Polly Campbell, manager-corporate insurance for The Cleveland Clinic Foundation, which has several facilities in Florida.

"Florida is a significant exposure for The Cleveland Clinic Foundation and additional information regarding windstorms would be useful in the risk retention decision process," said Ms. Campbell. "As you know, Florida windstorm deductible buybacks can be quite costly. If sufficient documentation is available, there would be more comfort with higher retentions," she said.

"As far as me putting together the board's property program, it doesn't have a direct application in terms of determining limits. I'm obviously much more interested in some of the computer-generated models that are used by underwriters to determine what the board's probable maximum loss is," said Scott Clark, risk manager for the Miami-Dade County public schools system in Miami.

Mr. Clark said the importance of the forecasts is to raise the profile of the hurricane peril to the public.

"People are reminded that a hurricane system is coming and that there could be X number of storms of a certain level that could be a problem," he said. "It creates a reminder that hurricane season is coming and Dr. Gray says we could have these many storms. That puts in people's minds that we have to be prepared," he said

AIG's Mr. Thomas agreed that the Gray forecasts, while not having short-term practical applications for underwriters, do serve a public good. "From a public policy standpoint, he does provide a very worthwhile reminder," he said.

"It's interesting, it does sensitize people that they are at risk and I think it also explains historically why there are long periods of a decade or more where frequency was low, and long periods where frequency was high," said FM Global's Mr. Burke.

"Were getting better scientific understanding of hurricane activity and what fuels it," said PCS' Mr. Kerney. "One of the things that I take away from the forecasts is there's lots of evidence that we have managed to dodge a bullet, particularly in the last five years."

He noted that 1999's Hurricane Floyd was almost as strong as 1992's Hurricane Andrew and much larger, but fortunately it changed directions and dissipated into a much less powerful storm by the time it made landfall. Last year's Hurricane Isabel—a Category 5 storm at its height—also changed course and weakened to a Category 2 storm by the time it made landfall. Had Isabel remained strong and made landfall further to the north, "we may very well have faced a mega-catastrophe," said Mr. Kerney.

"Ten years ago, Dr. Gray was out there all by himself, saying we can predict this," he said, noting that today NOAA and Tropical Storm Risk are also making forecasts.

"I think we're getting closer to an understanding, at least in respect to the peril of hurricanes, of what happens when elements come together," he said.

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Performance: Pay for doctors is still limited

Continued from page 1

ing well. It was also a way to judge whether we had the right measures."

To encourage participation by more than 220 physician groups representing some 30,000 physicians throughout California, the IHA decided to use measures developed by an independent third party, the National Committee on Quality Assurance.

Initially, three performance areas are being judged:

- Clinical, including immunizations, mammography screenings and chronic disease management, all based on the NCQA's measures.
- Patient experience, using a consumer survey developed by the Pacific Business Group on Health.
- Technology, such as the use of so-called "e-prescribing" and electronic medical records.

Each area is being weighted to determine the total score for a medical group, with 50% for clinical performance, 40% for patient experience and 10% for technology. Next year, the weightings will change to 40% clinical, 40% patient experience and 20% technology.

Depending on how they score, provider groups can earn up to 5% of the total capitation payments they are already receiving from the participating health plans, which include Aetna Inc., CIGNA Corp., Blue Cross of California, Blue Shield of California, Health Net Inc. and PacifiCare Health Systems Inc. A total of $50 million is at stake, Mr. Williams said.

Since it is just beginning to examine provider data this year, the IHA has not yet determined whether the program has produced any savings.

"The primary objective is to improve the quality of care, but a fundamental belief is that if you provide better outcomes, then you have the potential to favorably impact costs," Mr. Williams said.

Bridges to Excellence, a joint effort launched by employers, physicians, health plans and the Centers for Medicare and Medicaid Services in April 2003, has already made payments to providers that met two performance criteria: meeting the NCQA quality standard for care of diabetic patients; and "physician office link," a term used to describe the combination of clinical, patient education and case management systems applicable across the entire patient population.

"It doesn't measure how well patients are being treated, but it looks at the process of care and the systems of care in a physician's practice that will help them meet the six aims the IOM has laid out," explained Francois de Brantes, president of the initiative and program leader for corporate health initiatives at General Electric Corp., one of the employers that started the initiative. Other founding members include Ford Motor Co., United Parcel Service Inc., Procter & Gamble Co., and Humana Inc. in its capacity as an employer.

Bridges to Excellence is currently operating in four markets—the entire state of Massachusetts; Cincinnati; Louisville, Ky.; and the Albany-Schenectady region of New York.

So far, only a fraction of the $3 million the employers have pledged in incentive payments has been awarded, the most being $70,000 to an individual medical group, according to Mr. de Brantes.

However, "under the program, there are many physicians that have a very significant potential reward associated with their meeting the performance measures," he said. "Some of them have up to $20,000 per physician, and that represents roughly 10% to 15% of a physician's income."

Worth their while

The payments must be significant if they are to provide any real incentive to physicians to alter their practice methods, observers say.

"Unless the award is 10% to 15% of what you pay the medical group, it won't have much impact," said Dr. Randall W. Crenshaw, executive medical director at ViPS, a Baltimore-based information technology company that provides software and consulting services to health care payers, including Medicare and commercial insurers.

For example, if an insurer pays a participating group $1 million annually in capitation fees, the incentive payment should be $150,000, he said.

> **'Pay for performance means you pay after the performance has been achieved. So we're not prefunding an improvement in performance.'**
>
> *Francois de Brantes*
> *General Electric Corp.*

Mr. de Brantes agreed. "If you think about the difficulty for an individual practice to go through this transformation effort, re-engineer their care processes, this is not a trivial exercise.

"It's very complicated. It's expensive. You have to get new systems in place. Putting in, for example, a fully functional electronic health record with e-prescribing, decision support—all of which are things that we ask—can cost an individual physician upfront probably up to $30,000, and then $10,000 on an ongoing basis to maintain it," he said.

And those figures don't include "the amount of time needed to re-engineer your processes, start inputting all of those dozens or hundreds of folders that have manual charts into electronic charts, re-engineering so you can have nurses think about proactive outreach to patients as opposed to the reactive way of caring for patients," he said.

"We're not looking to fully compensate them for their costs; we're just looking to tip them over the scale, if you will," he said.

But Bridges to Excellence may be the exception.

So far, incentives paid in most of the pay-for-performance programs have been mostly in the range of 1% to 5% of compensation, according to Bradley Strunk, research analyst at the Center for Studying Health System Change in Washington. Mr. Strunk was lead author of the HSC's May 2004 issue brief titled "Paying for Quality: Health Plans Try Carrots Instead of Sticks."

Escalating health care costs, coupled with the sluggish national economy, are to blame for the dearth of funds pledged to pay-for-performance programs, according to David Joiner, senior vp-network management at Blue Shield of California in San Francisco.

"If you were to say, 'Let's create a pay-for-performance pool of money that we're now going to channel to hospitals that do a great job,' the question is, where does the money come from?" he said.

Employers are "already struggling to absorb the existing (cost) increases. To voluntarily put more money into the pool to pay bonuses is just digging the hole even deeper," he said.

But, in at least one case, the money being distributed is coming from the savings resulting from physicians meeting performance criteria.

"Every time we pay out a dollar, we save two," asserts Mr. de Brantes of GE.

"Pay for performance means you pay after the performance has been achieved. So we're not prefunding an improvement in performance. Once that performance has been achieved, the savings have been realized. If the savings have been realized, then we ought to share those savings," he said.

Expanding efforts

While Bridges to Excellence may claim it is saving participants money, there so far is little empirical evidence to support such assertions, and this may pose "a significant barrier" to the development of other pay-for-performance initiatives, according to Mr. Strunk of HSC.

"One of the big unanswered questions is the extent to which employers will buy into the idea of paying for quality," he said. "There's evidence among some of the larger employers, those that are proactive in health care issues… they would be satisfied to be shown by health plans that they are getting better health care for their health care dollars."

However, "one of the other things HSC's research has shown is when you bring in the smaller and midsized employers," they are "less interested in quality than they are about health care costs," Mr. Strunk said.

But employers may have to make some sacrifices if they want to see real improvement in health care quality—a change that many believe is needed to ultimately reduce the overall costs of the system, said Rich Ostuw, a principal at Towers Perrin in Stamford, Conn.

"There's a lot of merit to pay for performance," he said. "There is something wrong with a system that pays everybody the same regardless of their quality, or, in some cases, pays them more in spite of inferior quality.

"Sometimes, the higher-quality providers get substantially less revenue because the ones with quality problems get paid multiple times, because they get paid the first procedure and then they get paid to deal with the complications that come up," he said.

One possible way to encourage more participation is to stick to performance measures that have proved to reduce health care costs, suggested Dr. Crenshaw.

"You have to choose your measures wisely" so that "the behavior that you're encouraging through financial incentives is behavior that will reduce waste and cost in the system," he said.

For example, research has demonstrated that a "4% reduction in hospital admissions for cardiac patients taking ACE inhibitors. If you add a beta blocker, you get another 5% difference. Hospitalization costs about $3,500 for an episode of heart failure," he said.

"That's why Bridges to Excellence is focusing on improvements that will lead to cost savings," said Mr. de Brantes of GE. "We have to continue demonstrating the proof of the program. So, over the next couple of years, we will continue to log progress, inform the public debate about savings and improved outcomes. And then, as those findings make their way into the market, our hope is that health plans can start emulating the program."

"Employers need to ask health plans to emulate these programs, and to measure physician performance on a uniform basis…to truly reward better performance," Mr. de Brantes said. "That's the only way to make it a sustainable effort."

Consultants: Six firms investigated

Continued from page 4

vide malpractice insurance coverage. Buck no longer is a part of the company, known as Professional Consultants Insurance Corp., which is based in Burlington, Vt.

Meanwhile, since the mid-1990s, Towers Perrin, Watson Wyatt and Mercer have been successfully sued for millions of dollars in damages.

"These (insurance) pools are dangerous because the so-called independent auditor is very reluctant to testify because they're in the same pool and share in the losses," said a source who did not wish to be identified.

Milliman, for example, audited the work Towers Perrin did for the $26 billion Los Angeles County Employees Retirement Association in Pasadena, Calif. Milliman discovered Towers Perrin had grossly undercalculated the pension fund's projected liabilities, causing LACERA to contribute far less over 20 years than it should have to cover those liabilities. In a January 2001 lawsuit, the pension fund estimated — based on Milliman's audit — that the mistake amounted to more than $1.1 billion in contributions, or in excess of $2 billion after adding investment earnings.

LACERA had sought more than $2 billion in damages. The suit was settled in April 2003; attorneys for both sides wouldn't discuss the terms.

The Justice Department's investigation also involves concerns expressed by Gene Kalwarski, the then Milliman partner in charge of its mid-Atlantic office in Vienna, Va., that liability limits could be seen as purported collusion with other actuarial firms that participate in PCIC.

In a March 8, 2002, memo to senior partners at Milliman, Mr. Kalwarski said the firm's refusal to bid for a pension fund's actuarial consulting services after the fund had fired Watson Wyatt for seeking to impose liability limits would appear to violate antitrust laws.

"As Watson participates with us in PCIC, there is at least the strong perception that we are in collusion with our insurance pool partners," Mr. Kalwarski wrote in the memo. He asked CMilliman to seek "independent and objective" legal advice. He noted that Milliman's outside counsel, Stephen T. Jacobs, "may be conflicted on the issue, as he represents, I believe, PCIC and possibly our insurance pool partners, so it would least appear to the outside that he may gain financially from any advice he gives to Milliman."

In October 2002, after failing to convince Milliman not to impose the liability limits, Mr. Kalwarski broke off and formed Cheiron Corp., a Washington-based actuarial consulting firm that does not impose liability limits on pension fund clients. Milliman then sued Cheiron for violating a non-compete clause, breach of contract and releasing trade secrets to the public. The suit was settled, but details of the settlement were not released.

Mr. Kalwarski declined to comment for this story.

Vineeta Anand is a Washington reporter for Pensions & Investments, a sister publication of Business Insurance.

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Late News

Continued from page 1

dropped to around 13% because of plan changes, negotiations and terminations, Hewitt said.

Ohio enacts silica dust, asbestos reform bills

Ohio Gov. Robert Taft signed into law two bills that require that claimants seeking damages for exposure to asbestos and silica dust meet certain medical criteria before their claims can proceed. The bills are the first in the nation to set statewide medical criteria for either asbestos or silica exposure claims. The governor indicated that he would pursue further tort reforms later this year. He called the measures "a good start in our tort reform strategy, which is a cornerstone of our job-creation package."

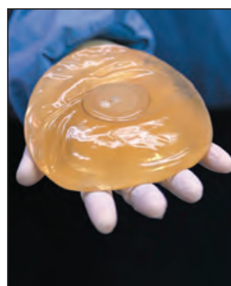
Gov. Taft

Groups call for TRIA extension

A coalition of insurance and financial services industry groups is calling for the Terrorism Risk Insurance Act to be extended for at least two years past its current expiration of Dec. 31, 2005. The appeal came in formal comments filed with the Treasury Department regarding TRIA's so-called "make available" provision—currently set to expire at the end of this year—which requires that insurers participating in the federal government's terrorism insurance backstop program make terrorism coverage available under substantially the same terms and conditions used for other risks. "The make available provision does not have an impact on the amount of capacity that is available to commit to losses from terrorism," the coalition states in its remarks. "Only the backstop fosters the creation of new capacity."

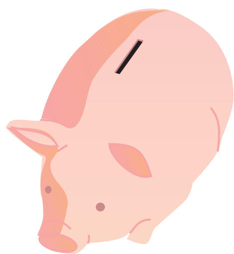
Dow Corning trust to start paying claims

A $2.35 billion Dow Corning Corp. settlement trust will begin paying silicone gel implant claims this month following the company's emergence from nine years of federal bankruptcy protection. The Dow Corning claims facility, funded partly with insurance settlements, will pay out $2.35 billion over the next 15 years to claimants who received implants before 1994. Participating claimants include about 170,000 women who received breast implants and 75,000 people who received other types of implants. The claims facility has set aside $400 million for litigation with nonsettling parties.



Brokers predict big future for HSAs

Employers across the country are showing increasing interest in high-deductible health plans with health savings accounts as a solution to rising employee benefit costs, a survey of insurance brokers shows. Fifty-five percent of brokers responding to the survey by the Council of Insurance Agents & Brokers predicted that HSAs would be a significant or very significant coverage option for private employers, and 29% said they thought the new plans would be a moderately important option for employers.



Sen. Frist urged to renew flood insurance program

Several insurance and financial services interests are urging Senate Majority Leader Bill Frist, R-Tenn., to move swiftly to reauthorize the National Flood Insurance Program. The federally backed NFIP—which covers flood losses not typically insurable through other policies—is slated to expire on June 30. In their June 1 letter, the trade groups and companies note that two reauthorization bills have been introduced that would extend the flood insurance program for five years.

Sen. Frist

Briefly noted

An Oklahoma House committee is meeting in special session to consider whether Insurance Commissioner Carroll Fisher should be impeached. Mr. Fisher and a top aide are currently being prosecuted for several counts of embezzlement and operating a charity illegally. Depending upon the committee's findings, lawmakers may be reconvened for a vote later this summer, according to a spokesman for the commissioner....New Jersey Gov. James E. McGreevey is reviewing legislation designed to reform the state's medical malpractice liability system. Although the measure—New Jersey Medical Care Access and Responsibility and Patients First Act—does not provide caps for noneconomic damages, it does call for creation of a task force to examine the possible impact of caps and other reforms.

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Online Poll

[6/1-6/4]

Have you changed any of your property/casualty insurers due to financial security concerns over the past three years?

Yes	55.8%
No	44.2%

BI Stock Index

[6/1-6/4]

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

Index	Value	Change
BI Stock Index	2272.98	0.63
Dow Jones	10242.80	0.53
S&P 500	122.50	0.16

Largest gains

Zenith National Insurance	5.95%
American Safety Insurance	5.36%
Unitrin	4.49%
Aetna Inc.	4.19%
Axis Capital Holdings Ltd.	3.83%

Largest losses

Trenwick Group Ltd.	-12.50%
Hub International	-3.93%
SCOR	-3.42%
Odyssey Re Holdings	-3.29%
Humana Inc.	-2.99%

Weekly change by market segment

Brokers	0.21%
Insurers/Reinsurers	0.47%
Managed Care Organizations	0.62%

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

Dispute: Purchasing group program

Continued from page 3

$78.8 million in client property premiums intended for several insurers, including Virginia Surety and AIG units.

Mr. Gruppuso, who was originally arrested in May 2002, faces up to 10 years in prison.

Virginia Surety sued NPS for fraud after terminating the program in 2002 and has reported continuing losses on the runoff of the NPS business, Aon has reported in Securities and Exchange Commission filings.

All of the policies National Union issued to purchasing group members were written excess of a $250,000 retention, with Virginia Surety providing primary coverage for the retention, according to the AIG companies' lawsuit.

After the NPS program was cancelled, National Union and Lexington wrote about 77 three-month or one-year excess policies for companies that had been purchasing group members; these policies carried the same retention, and Virginia Surety continued to provide primary coverage, the suit says.

A dispute first arose last year when a Virginia Surety claims official asserted that defense costs would be included in the $250,000 retention layer despite "clear language" in the Virginia Surety policies that these costs were outside policy limits, the AIG insurers allege.

At that time, though, the Virginia Surety official also acknowledged in a letter that National Union's policies would be triggered only when payouts exhausted the retained limits, the suit says.

Then earlier this year, the AIG companies charge, Virginia Surety tried to extend National Union's liabilities further and asserted that National Union's policies provide first-dollar coverage on a pro-rata basis with the Aon unit. Because National Union's excess limit of $1 million per occurrence was four times the Virginia Surety limit, Virginia Surety asserted that National Union must pay 80% of defense and indemnity claims until Virginia Surety's limit is exhausted, the suit says.

The same calculation would presumably apply to Lexington's policies, the suit adds.

On this basis, Virginia Surety claimed National Union owes $35.7 million on losses paid through March 2004, along with 80% of all losses going forward, according to the complaint.

The Aon unit's stance "is contrary to the clear provisions of the National Union and Lexington self-insured retention endorsements, and it is also contrary to the course of dealings between the parties, as Virginia Surety has recognized from the onset of the program that its policies provide the first layer of coverage," the lawsuit charges.

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