BI 07-07-03 A 1 7/3/03 5:42 PM Page 1

*Supreme Court upholds diversity practices* / 3

*Guaranty funds suing Reliance liquidator* / 4

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# Business Insurance®

July 7, 2003

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$4

# Policyholder wins pollution dispute

## New York high court says exclusion doesn't apply in bodily injury case

By MICHAEL BRADFORD

**ALBANY, N.Y.**—A ruling by New York's highest court that the total pollution exclusion is ambiguous and cannot be used to deny coverage for bodily injury from paint fumes is being called a significant policyholder victory.

The New York State Court of Appeals ruled on July 1 that the commercial general liability policy written by TIG Insurance Co. for Belt Painting Corp. did not exclude coverage for injuries to an office worker who inhaled fumes from paint and stripping solution while his workplace was being painted.

Joseph Cinquemani sued Belt Painting and other defendants in 1997, charging that he was injured by the fumes. When Belt Painting sought defense and indemnification from TIG, the insurer relied on the pollution exclusion in the coverage to deny the claim.

Hawaii pollution ruling favors policyholders, page 4

The CGL policy, written to limits of $1 million, contained the standard total pollution exclusion that excludes coverage for "bodily injury or property damage which would not have occurred in whole or part but for the actual, alleged or threatened discharge, dispersal, seepage, migration, release or escape of pollutants at any time." Fumes are among the types of pollutants defined by the exclusion.

See POLLUTION/page 43

# Punitives ruling at center of last high court term

## Health care cases also affect business

By MARK A. HOFMANN

**WASHINGTON**—Employers will long remember the just-ended Supreme Court term for a single decision among the various rulings handed down by the justices.

In an otherwise lackluster term for liability cases, the justices reaffirmed in *State Farm Mutual Automobile Insurance Co. vs. Curtis Campbell et ux.* that a punitive damage award can be so disproportionate to underlying compensatory damages as to violate the Constitution. The case involved a claims-handling dispute in which the Utah Supreme Court reinstated a $145 million punitive damage award levied atop a compensatory award of only $1 million (*BI*, April 14).

But the court didn't stop with merely saying that the awards could be unconstitutionally large—the justices held that under most circumstances, a punitive damage award of double-digit multiples of compensatory damages would cross the line into unconstitutional territory.

See COURT/page 42

PHOTO: REUTERS /KEVIN LAMARQUE

**President Bush discusses proposals to reform the Medicare system at an event held late last month in Miami.**

## Subsidies would bring retiree plan savings

# Employers to benefit from Medicare Rx plan

By JERRY GEISEL

**WASHINGTON**—Employers that agree to continue providing retirees with prescription drug benefits that are as generous as those provided under Medicare expansion legislation passed by the House and Senate last month would receive significant financial help from the government.

Those financial subsidies could reduce employers' prescription drug costs for their Medicare-eligible retirees by as much as 35%, some benefit consultants calculate.

With employers now spending billions of dollars annually on prescription drugs under coverage for retired workers, the subsidies would provide a measure of financial relief for employers battered by surging health care costs.

"There is a lot of excitement about this. We are getting a lot of calls and questions about this issue," said Kathy Bakich, vp and national director of health care compliance at The Segal Co. in Washington.

The two measures differ in how they would

See MEDICARE/page 42

# Late News

## Allegheny buys E&S unit from RSA

Allegheny Corp. has acquired excess and surplus lines underwriting agency Royal Specialty Underwriting Inc. from Royal & SunAlliance Insurance Group P.L.C. for about $115 million. The acquisition, through the company's Allegheny Insurance Holdings L.L.C. subsidiary, includes renewal rights to ongoing business underwritten by Atlanta-based RSUI and the related net unearned premium reserve portfolio of about $320 million. The deal excludes loss reserves associated with business RSUI previously wrote for RSA affiliates.

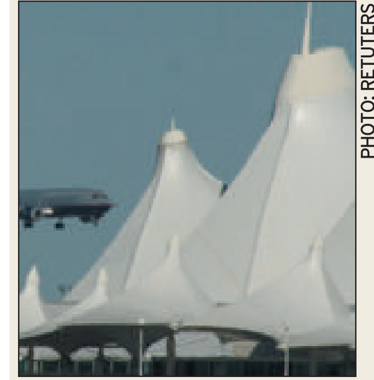


PHOTO: RETUTERS

## Denver facing lawsuit over mold at airport

The city and county of Denver are being targeted in a massive toxic mold suit filed in Denver District Court. The suit, which seeks class-action status, was filed on behalf of two employees of United Airlines who have developed recurring respiratory conditions and other ailments they attribute to toxic mold exposure at Denver International Airport. The suit charges that the city and county breached their "duty to maintain the airport in a reasonably safe condition" by "failing to correct the airport's poor environmental conditions despite having knowledge of such problems."

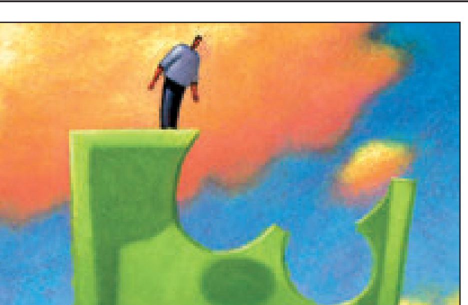
See LATE NEWS/page 43

NEWSPAPER

Spotlight

# MIDYEAR MARKET REPORT

*Begins on page 10*



BI 07-07-03 A 3 7/3/03 4:28 PM Page 1



# Guaranty funds suing Reliance liquidator

By GAVIN SOUTER

**PHILADELPHIA**—Guaranty funds in 25 states are suing the Pennsylvania insurance commissioner, seeking reimbursements for claims payments they have made to Reliance Insurance Co. policyholders with large-deductible insurance programs.

The guaranty funds argue in a suit filed late last week in the Commonwealth Court of Pennsylvania in Philadelphia that they should receive the policyholder reimbursements for claims paid by the funds under the large-deductible programs.

But in a suit filed the same day in the same court, Pennsylvania Insurance Commissioner Diane Koken seeks a declaration that the reimbursements are part of the Reliance estate and should not be given exclusively to the guaranty funds.

**Pennsylvania Insurance Commissioner Diane Koken disputes guaranty funds' demands for policyholder reimbursements made for Reliance claims.**

The payments relate to about 1,400 large-deductible policies written by Reliance prior to its liquidation in October 2001, court documents say.

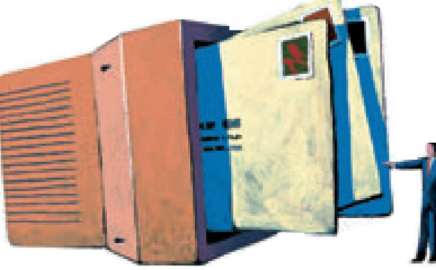
The policies mostly covered workers compensation losses but also included general liability and auto liability coverages. The policies differed in structure but often included deductibles of between $250,000 and $1 million per claim. Those deductibles were paid by Reliance, and the insurer was then reimbursed by the policyholders.

The guaranty funds have paid $875 million to Reliance policyholders since it was placed in liquidation and will likely have to pay an additional $1 billion in claims, "including potentially hundreds of millions of dollars within the deductibles of large-de-

See RELIANCE/page 6

# Flood of e-mails to company is not illegal trespass: Court

By JOANNE WOJCIK



**SAN FRANCISCO**—The California Supreme Court's ruling that unauthorized use of company e-mail systems is not a form of trespassing doesn't mean that employers can't protect themselves from unwanted e-mail, attorneys say.

Employers in the state still have other legal remedies to shield themselves from unauthorized access to their e-mail systems, attorneys say.

Still, the decision came as a disappointment to Intel Corp., which had won the case at both the trial and appellate levels using "trespass to chattels," an ancient legal doctrine that forbids the use of someone else's property without their permission.

The Supreme Court last week overturned those rulings, which had provided an injunction barring a former employee from using the e-mail system of the Santa Clara, Calif.-based technology company to communicate with current employees.

According to court papers, after Kourosh Kenneth Hamidi was fired by Intel in 1995, he began to air grievances about the company through e-mail. Despite Intel's requests that he stop, Mr. Hamidi repeatedly flooded Intel's e-mail system with messages that were sent to as many as 35,000 employees. After the company's security department proved unable to block the e-mails, Intel asked a trial court to issue a permanent injunction stopping the campaign. The company sought no damages.

The trial court granted the injunction, and the appellate court upheld it, ruling that Intel's e-mail system "is private property used for business purposes. Intel's system is not transformed into a public forum merely because it permits some personal use by employees."

It also found that Intel "showed

See E-MAIL/page 40

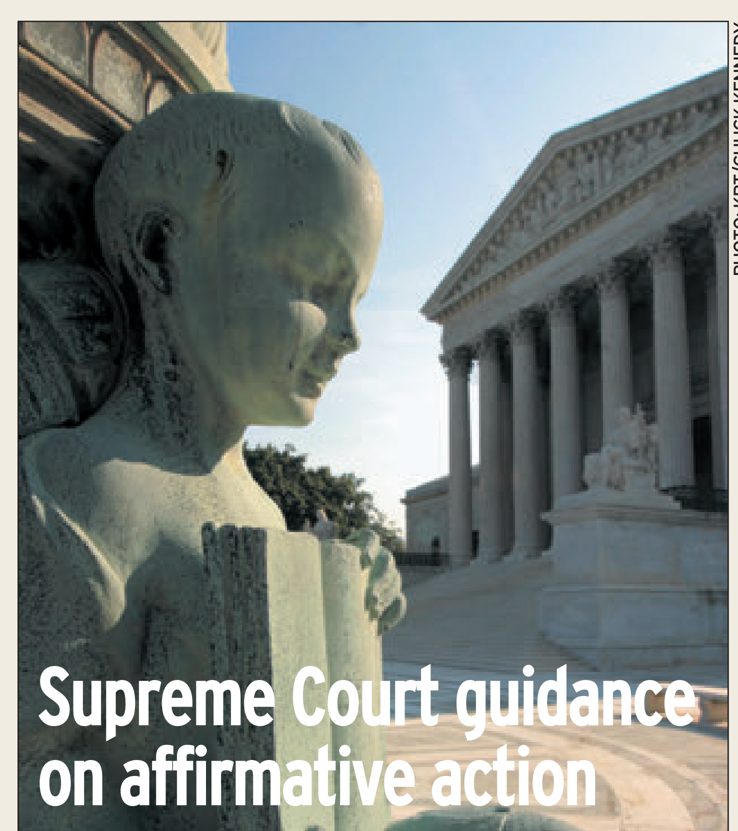


PHOTO: KRT/CHUCK KENNEDY

## Supreme Court guidance on affirmative action

# Employers to review diversity policies

By JUDY GREENWALD

Employers should re-examine their diversity and affirmative action policies in light of the U.S. Supreme Court's decisions in two cases involving the University of Michigan's admissions policies.

In its 5-4 decision in *Grutter vs. Bollinger*, the high court endorsed affirmative action and found that the University of Michigan law school's use of race as a positive factor in individual admission decisions is constitutional.

But in a 6-3 companion decision in *Gratz vs. Bollinger*, the court also held that the university's undergraduate admissions program's use of an automatic point system based on race is unconstitutional. The university has used a selection method under which every applicant from what it considers to be an underrepresented racial or ethnic minority group, including African-Americans, Hispanics and Native Americans, is automatically awarded 20 points of the 100 needed to guarantee admission.

While universities cannot establish admissions quotas for members of racial groups, they can "consider race or ethnicity more flexibly as a 'plus' factor in the context of individualized consideration of each and every applicant," stated Associate Justice Sandra Day O'Connor, writing for the majority in the *Grutter* decision.

Consultants and attorneys say the July 23 decisions are relevant to private employers as well as educational institutions. But they also warn that the complex

See AFFIRMATIVE/page 40

## Inside Business Insurance


### Judge dismisses dotcom investors' suit

A federal judge ruled that investors who lost money on Internet stocks have no grounds to sue Merrill Lynch & Co. and its analysts. Page 4

### Many employer suits preventable: Attorney

Speakers at the Society of Human Resource Management conference offered tips for employers. Page 4

### Putting prudence back in jurisprudence

A judge's candid remarks in dismissing a lawsuit he found meritless are a welcome change, Paul Winston writes. Page 6

### Insurers move to exclude asbestos risks in U.K.

With new U.K. rules set to take effect next year, some insurers are pushing asbestos exclusions. Page 37

### Australian insurer exec charged in HIH failure

Rodney Adler, a former HIH Insurance Ltd. director, has been charged by authorities with making false statements. Page 37


## 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 listings of industry vendors found in *BI*'s Market Sourcebook.
- New **Opinion Poll** for readers: Should a prescription drug benefit be added to the Medicare program?

## Departments


Advertiser Index ....42
Between the Lines ....36
Classifieds ....38
Coming & Goings-Buyers ....40
Insurance Services Guide ....36
International ....37
Letters ....8
Opinions ....8
Paul Winston ....6
Products & Services ....36
Ticker ....43
World Updates ....37


REPORTING ON CORPORATE RISK AND EMPLOYEE BENEFIT MANAGEMENT NEWS.

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BI 07-07-03 A 4 7/3/03 4:31 PM Page 1



# U.S. court rules on Hawaiian pollution cover

By DAVE LENCKUS

**HONOLULU**—With no Hawaii court rulings to guide it and without deciding the meaning of the sudden-and-accidental pollution exclusion, a federal district court has ruled that general liability insurers must defend Hawaiian policyholders facing unexpected gradual pollution losses.

The duty to defend exists for insurers that wrote pre-1986 comprehensive general liability insurance policies containing the exclusion, because there is legal uncertainty over the exclusion's meaning, the court explained. That uncertainty creates a potential insurer duty to indemnify, which triggers the duty to defend, the court ruled without resolving the exclusion's meaning.

In another of several pro-policyholder rulings, the federal court ruled that a government-ordered cleanup qualifies as a covered "suit."

Insurer attorney Laura A. Foggan characterized the ruling as "a wacky holding," because the court established a duty to defend without resolving the legal question of whether the exclusion bars coverage for unexpected gradual pollution. Insurers argue that CGL policies containing the exclusion cover only unexpected losses that occurred abruptly.

While questions of fact are left to a jury or trial judge to decide, courts typically resolve legal questions like the meaning of an exclusion early in a case, said Ms. Foggan, counsel for the insurer-backed Complex Insurance Claims Litigation Assn.

If other courts ruled similarly without resolving the legal issue of the exclusion's meaning, "you'd always have a duty to defend imposed—and that can't be the law," said Ms. Foggan, a partner with Wiley Rein & Fielding L.L.P. in Washington.

Policyholder attorney Robert M. Horkovich disagreed. "An insurance company has a duty to defend unless there's no duty for coverage. So, if it's an open issue, insurance companies should be defending. And that's what policyholders expect," said Mr. Horkovich, a partner with Anderson Kill & Olick P.C. of New York.

Mr. Horkovich applauded the federal judge for showing "a lot of understanding that this was not necessarily his job" to guess how a state court would interpret the exclusion.

The court's June 19 ruling came in a lawsuit that an excess insurer filed after its policyholder and a primary comprehensive general liability insurer reached a $1.5 million settlement over a polluted site in Honolulu. The settlement was triple the policy limits written by the insurer, Island Insurance Co. Ltd. of Honolulu.

The policyholder, diversified manufacturer and service provider Servco

See **HAWAII**/page 40

A federal court in Honolulu held that general liability insurers must defend policyholders facing unexpected gradual pollution claims.

# Wal-Mart anti-discrimination policy extended to homosexual workers

By SALLY ROBERTS

**BENTONVILLE, Ark.**—Wal-Mart Stories Inc. has expanded anti-discrimination protections to its gay and lesbian employees, but still has no plans to extend health benefits to domestic partners of those employees, the company said.

Following the lead of other large employers, the Bentonville, Ark.-based retail giant recently decided to include sexual orientation in its anti-discrimination policy after lobbying by its employees.

"We had associates telling us that they felt it was important to do this to indicate to all 1.1 million associates that under equal protection we would also include sexual orientation" in addition to race, gender, disability and age, the spokesman said.

"We want all associates to feel they are valued and that they are all treated with respect, no exception," he said.

PHOTO:SCOTT OLSON/GETTY

As a result of the move, sexual orientation will be added to Wal-Mart's equal employment protection provision in its associate handbook and to its existing diversity and sexual harassment training, the spokesman said.

While gay and lesbian Wal-Mart employees are now protected under the company's policy, they are for the most part not protected under federal anti-discrimination laws.

A majority of courts have ruled that sexual orientation is not a protected class under Title VII of the Civil Rights Act, said Gerald Maatman Jr., a labor attorney with Seyfarth Shaw in Chicago.

A host of state laws and large municipal city ordinances, however, do provide such protections, he said.

Wal-Mart's move brings to 318 the number of Fortune 500 companies that have non-discrimination policies covering sexual orientation, according to the Human Rights Campaign, a Washington-based gay rights advocacy organization.

But while Wal-Mart has expanded its anti-discrimination protections to gay and lesbian employees, it has no plans to extend health benefits to the partners of those employees.

"We don't extend benefits to partners who are not married regardless of their sexual orientation," the spokesman said.

Of the Fortune 500, 165 companies extend benefits to same-sex partners, including six of the nation's 10 largest companies, according to HRC.

# Judge dismisses dotcom investors' suit

## Federal securities laws not intended as 'speculators' insurance'

By GAVIN SOUTER

**NEW YORK**—Investors who lost money on Internet stocks during the market boom cannot recoup their losses from analysts who recommended the stocks, a federal judge has ruled.

The investors, who sought to recover their losses from Merrill Lynch & Co. Inc., were "high-risk speculators" who were trying "to twist the federal securities laws into a scheme of cost-free speculators' insurance," according to Judge Milton Pollack of the U.S. District Court for the Southern District of New York.

"Seeking to lay the blame for the enormous Internet bubble solely at the feet of a single actor, Merrill Lynch, plaintiffs would have this court conclude that the federal securities laws were meant to underwrite, subsidize and encourage their rash speculation in joining a freewheeling casino that lured thousands obsessed with the fantasy for Olympian riches, but which delivered such riches to only a scant handful of lucky winners," Judge Pollack wrote.

The investors charged that Merrill Lynch and its chief Internet analyst, Henry Blodget, had recommended stocks in order to secure investment banking contracts with Internet companies.

But Judge Pollack ruled that the investors had no grounds for their claims, as they failed to prove that the Merrill Lynch intended to defraud them through material misrepresentations or omissions of facts that caused the loss.

PHOTO: PHOTOGRAPHER SHOWCASE

Merrill Lynch and Henry Blodget, its chief Internet analyst, were sued by investors.

# Employers often face preventable lawsuits

By MICHAEL PRINCE

**ORLANDO, Fla.**—Organizations get sued for many reasons not under their control, but sometimes they get themselves into trouble, says an attorney who has represented employers in suits for decades.

Often, an employer's mistake will turn a case into a slam-dunk for a plaintiff, said James Naughton, partner with Hunton & Williams in Norfolk, Va.

More SHRM coverage on page 34

These mistakes often fall into distinctive categories, Mr. Naughton told attendees at the 55th annual conference of the Society for Human Resource Management, held last month in Orlando, Fla.

For example, employers that fail to regulate e-mail and Internet use in the workplace are inviting trouble, he said.

Many off-color jokes are sent via e-mail, as employees sometimes incorrectly believe their work e-mail account is private or that the message won't wind up in the hands of someone who might be offended. Just one lewd e-mail, however, can prompt a hostile

See **LAWSUITS**/page 34

BI 07-07-03 A 6 7/3/03 4:29 PM Page 1



# Reliance: Guaranty funds sue

Continued from page 3

ductible policies," court documents say.

Because the guaranty funds have assumed the position of Reliance under the terms of the policies, they should receive the large-deductible reimbursements and benefit from collateral posted by policyholders, the funds argue. Reliance holds about $1.4 billion in collateral for the policies.

The commissioner disagrees with the funds. The guaranty funds should not be allowed to remove assets from the Reliance estate for their exclusive benefit, she argues in her suit. If the funds were allowed to do so, the amount of money available to cover claims not covered by guaranty funds will be diluted, the suit contends.

"The dispute is not whether the guaranty associations receive any benefit from the deductible reimbursements, as their status as the largest single policyholder-class creditor will result in a distribution of most of the deductible reimbursements to the guaranty associations. Rather, the guaranty associations maintain they should receive all of the deductible reimbursements, thus reducing the assets of the estate available for distribution," the commissioner's suit states.

But the purpose of the guaranty funds is to reimburse smaller policyholders, rather than the large corporate claims that are not protected by the funds, said Michael L. Browne, a partner at Reed Smith L.L.P. in Philadelphia, who is representing the guaranty funds.

"It really gets down to what a guaranty fund is set up to do, and we think it is to provide a safety net, not to bail out an insolvent insurer," he said.

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# Paul Winston

## *You've got to know when to fold 'em*

How refreshing it was to hear a judge essentially tell a group of investors last week that they have no one but themselves to blame for their stock market losses.

Such candor from the bench is all too rare as judges more often seem to focus not on the merits of a claim, but instead merely on whether the plaintiffs crossed their Ts and dotted their Is. Rather than serve as gatekeepers to the court, it's as if they instead are doormen there only to usher in all manner of silly claims.

That is not to say that companies sometimes are not guilty of defrauding investors, as we have seen repeatedly in recent months. But many more investors (my retirement savings, for example) simply were victims of a longstanding lesson in market dynamics: What goes up must come down.

**Paul Winston**

U.S. District Court Senior Judge Milton Pollack in New York last week dismissed with prejudice a class of plaintiffs who claimed that fraud by a stockbrokerage was to blame for their investment losses, rather than their own gamble on the market.

The June 30 ruling, *In re Merrill Lynch & Co. Inc.*, came in a class-action suit brought by investors who claim they lost money on stock issued by two Internet-related companies because of allegedly fraudulent stock research on the companies by Merrill Lynch & Co. The companies, 24/7 Real Media Inc. and Interliant Inc., had been the subject of research reports issued by Merrill Lynch.

The investors' claims were filed soon after New York attorney general Eliot Spitzer last year launched a widely publicized investigation into allegations that Merrill Lynch and technology analyst Henry Blodgett had issued biased investment reports on stocks to boost its investment banking business. Merrill subsequently settled the state's claims for $100 million, opening the floodgates for private investors to go after the company for its analysts' irrationally exuberant opinions about tech companies.

Judge Pollack said no. And he said it with style.

In his opinion, the judge wrote that "the facts and circumstances fully within this court's proper province to consider on a motion to dismiss show beyond doubt that plaintiffs brought their own losses upon themselves when they knowingly spun an extremely high-risk, high-stakes wheel of fortune."

The judge said the claimants failed to show that they had relied on Merrill Lynch's research reports, let alone even read them. If they had, he noted, they would have seen that analysts had given the two companies a rating of "D," reserved for the riskiest investments.

The plaintiffs relied on the "fraud-on-the-market" theory, which basically holds that if fraud or misrepresentation influences a stock price, rather than typical market forces, an investor can claim to indirectly be a victim of that underlying fraud. Notwithstanding the New York's attorney general's pursuit of Merrill Lynch and Mr. Blodgett, the judge said he was "utterly unconvinced" that the plaintiffs had demonstrated a fraud that caused their losses.

The judge noted that the investors bringing suit were among many who made risky investments to try to profit on "a colossal 'bubble' of panic proportions." Then that bubble burst. But rather than dump their shares, they held on in the hopes of a turnaround, ultimately taking a loss.

"The record clearly reveals that plaintiffs were among the high-risk speculators who, knowing full well or being properly chargeable with appreciation of the unjustifiable risks they were undertaking in the extremely volatile and highly untested stocks at issue, now hope to twist the federal securities laws into a scheme of cost-free speculators' insurance," the judge said.

Judge Pollack's ruling reminds the public of the speculative nature of the stock market and the chances they take betting on unproven stocks. Using words like "casino," "gamble" and "wheel of fortune" to describe the market, one can hardly avoid the judge's view that it is a game of chance, with many losers as winners.

The stock market downturn, the poor economy, a rash of accounting and corporate accounting scandals in recent years and regulatory backlashes have all created an environment in which it is too easy for plaintiffs to claim they were wronged, putting businesses at a disadvantage in defending themselves. This ruling should help restore some balance, standing as a reminder that just because investors suffer losses in the stock market, that does not mean they were cheated.

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## Editorial

# Drug benefit fair to all

WHILE A FINAL congressional agreement on adding a prescription drug benefit to the Medicare program still is a ways off, we're encouraged that both the House and Senate recognize the importance of encouraging employers to retain their retiree prescription drug benefit plans.

Both the House and Senate bills, in somewhat different ways, would give employers financial incentives to offer a prescription drug benefit, as long as that benefit is at least as generous as the drug benefit that would be available to retirees through Medicare.

The incentives are not insignificant. Benefit consultants say that employers keeping their prescription drug plans and collecting payments from the government for doing so could cut their prescription drug costs by up to 35% a year and reduce their overall retiree health care costs by between 10% and 20%.

With some major employers spending hundreds of millions of dollars a year on their retiree health care programs, a 10% or 20% cost reduction adds up to a lot of money.

One might ask why legislators want to encourage, through financial incentives, employers to retain prescription drug benefit plans.

Certainly, one major reason is that there would be far less disruption to retirees—and less administrative hassle for Medicare—if retirees stayed in their current employer-provided prescription drug plan, rather than enrolling in a new program. With 40 million people enrolled in Medicare and eligible for the new benefit, keeping even a few million people in their former employers' health care plans may be the difference between a smooth start to the program and administrative chaos.

While there is no denying that an expanded Medicare program will save money for employers with retiree health care plans, we would not call it a subsidy or a windfall.

These are, after all, employers that voluntarily offer the benefits and that help to fund Medicare through payroll and corporate taxes. Reducing that burden, through the payments government would provide those employers, strikes us as only fair and as benefiting to the government, retirees and employers.

# Market offers opportunity

THE FORECAST for property/casualty insurance rate increases may be cloudy, but there's a silver lining for risk managers.

As our Midyear Market Report beginning on page 10 notes, rates are still rising across most lines of business, and in many cases the amount of coverage available is shrinking. That creates some big challenges for risk managers seeking to transfer their organizations' risks. But it also presents opportunities for risk managers to show why they're important.

With premiums going up and limits falling, policyholders are being forced to retain more risk. For some organizations, loss prevention and loss control perhaps took a back seat during the prolonged soft market, when coverage was readily available and relatively inexpensive. Not anymore.

In the current hard market, organizations are no longer able to transfer all the risk they would like, and insurers are focusing on matching rates to the risks they're underwriting. We think these both are positive developments for the market.

Businesses benefit greatly from professional risk managers' efforts to prevent losses to their organizations' people and property. What employer can afford to go without such valuable workers? Risk managers can make a strong case for job security by developing effective programs and communicating them clearly.

Insurers that abandon the market-share underwriting that was so widely practiced in the soft market are doing risk managers a favor. Basing rates on the risks undertaken not only will strengthen an insurer's financial health, but it also can help reduce the rush to return to volatile and unpredictable pricing.

These are difficult times for risk managers. Striving to meet the challenges head-on, though, will pay big dividends when the market eventually eases.

## Schillerstrom

• BREAK TIME IN MINNESOTA •

## Letters to the Editor

### Health care changes must focus on patients

To the editor: Your June 23 issue on the health care crisis is an outstanding contribution to needed dialogue to address this crisis. However, most contributors only see "trees" to be tweaked. They do not see the "forest" that needs transformation—not reform, as your own editorial suggests.

No one seems to address the need for root-cause analysis. No one seems to understand the need to address this crisis from a *systems* perspective. No one seems to see this issue from the perspective of the patient.

One exception is William Hembree, who recommends the first step in the transformation process, viz., *create a vision for our health care system*. He even contributes an excellent vision statement for consideration—and it's patient focused!

My family physician responded profoundly to my comment on steps we're taking locally to continuously improve our health care system—to the limited extent any community is able. He said, "The outcomes will be what you want only if you focus on the patient!" Most of us focus on the needs of providers, employers, and government—as did Schillerstrom's editorial cartoon in your same issue. Where is the patient in this equation?

Patient focus also implies patient responsibility. If employees don't take steps to manage their own health care—and that of their family members—our system will continue to spiral out of control. Incentives for wellness need to be part of the essential transformation process.

With a viable vision statement, effective root-cause analysis, and patient (employee) focus, the essential transformation of our nation's health care system can be achieved.

Tweaking the current system will only continue our frustration and our increased costs. *Business Insurance* should continue its leadership role in taking this dialogue to the next level of system transformation—the only way our nation can effectively work through this crisis.

**John Pryor**
Bakersfield, Calif.

### Mandatory health cover not the right solution

To the editor: I recently read the Perspectives article, "Mandatory Health Insurance a Fair Solution," by Philip J. Edmundson (*BI*, June 30).

I was taken aback by the tone of this article and because it is one-sided. Does Mr. Edmundson realize that the majority of businesses within the United States are small businesses, as defined by the government? Most of these businesses cannot afford to offer health insurance universally to all of their em-

**See LETTERS/page 39**

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BI 07-07-03 A 10 7/2/03 1:11 PM Page 1



# MIDYEAR MARKET REPORT

Spotlight Editor: Gavin Souter

## Rate hikes continue for D&O

### E&O stabilizing for many risks

By DAVE LENCKUS and RODD ZOLKOS

Directors and officers liability insurers continue to hit buyers with significant rate hikes—albeit somewhat lower than last year—and have begun imposing tougher policy terms and conditions.

Beyond 2003, risk managers should plan for a continuing hard market, based on various legal, regulatory and social factors, according to insurer and broker executives.

In the errors and omissions market, meanwhile, rates are stabilizing

for some classes of business, but problem classes are paying much more for coverage. E&O underwriters, many of which are also significant D&O markets, generally are not imposing tougher policy terms and conditions, satisfied for now with the more restrictive terms they imposed last year.

Capacity is not a significant problem in either market, though risks have to line up many more insurers than were necessary in the past to arrange sufficient limits, market experts say.

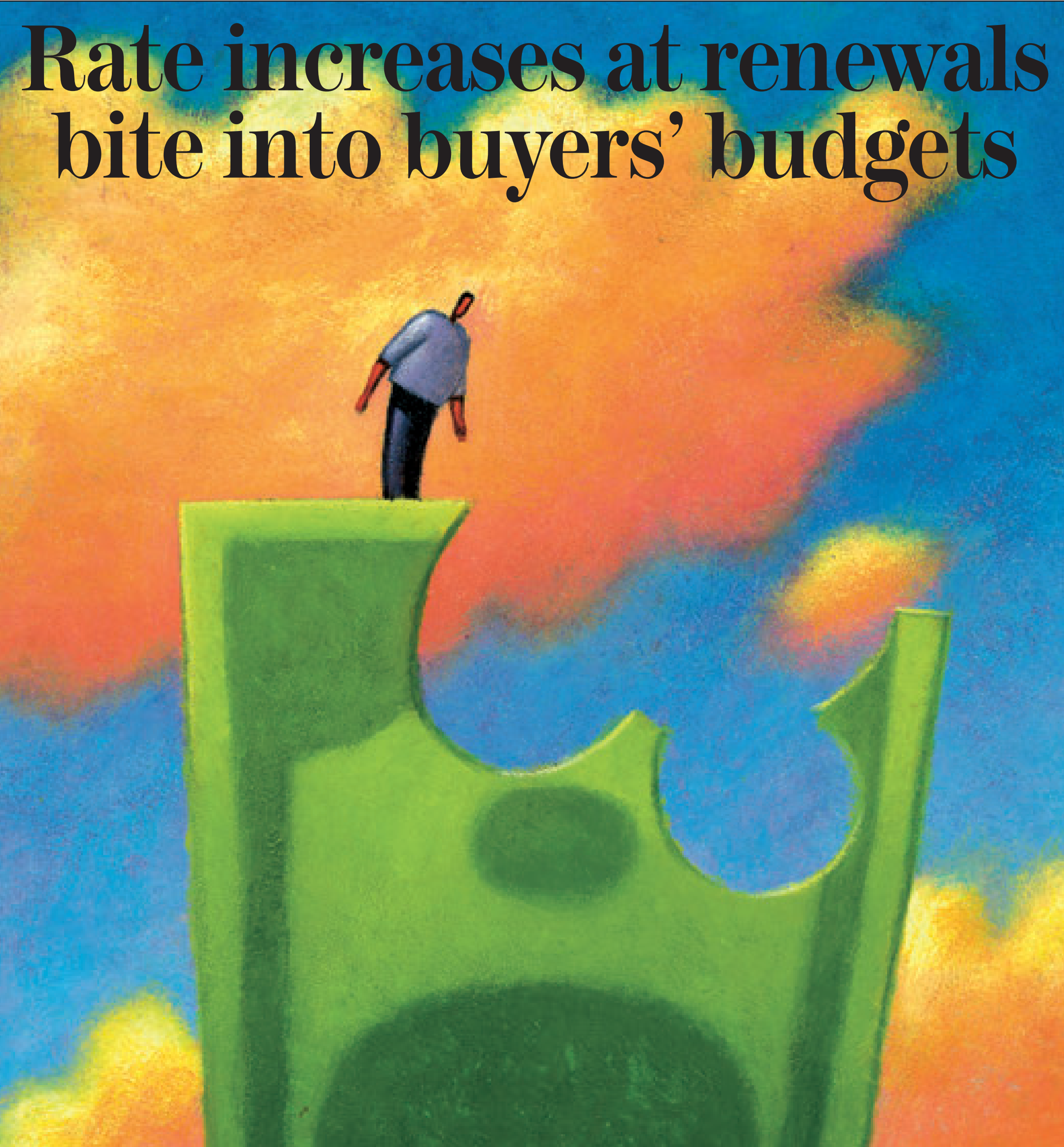
#### Wide variation

Unlike some other segments of the property/casualty insurance market, "there's no softening going on in the D&O area. It's still in crisis circumstances right now," said Jim Swanke, strategic risk financing practice leader for Tillinghast-Towers Perrin in Minneapolis.

Rate increases so far this year have averaged about 100%, insurers and broker executives said.

But the increases have varied widely, depending on each buyer's experience and its industry.

See D&O/page 14




## Property policyholders hoping to build on rate decreases

By MICHAEL BRADFORD and MARK A. HOFMANN

It's a good time to be a good property risk.

While many property buyers are still seeing moderate rate increases, risk managers with clean property loss histories are finding that underwriters are much more willing than last year to lower premiums or renew at flat rates. As the marketplace has settled since the 2001 terrorist attacks and new capital has boosted coverage availability, property prices have stabilized considerably.

In some cases, buyers have landed significant savings.

"We had an increase in limits, a decrease in deductibles and well over a $1 million decrease in premiums," said Lance J. Ewing, executive director of risk management at Park Place Entertainment Corp. in Las Vegas. He said he has heard from colleagues that many of them

are seeing a market softening, with some risks benefiting more than others.

Insurers and brokers report similar situations.

"More consistency and stabilization" characterize the current commercial property market, said Douglas Nelson, president of Liberty Mutual Insurance Co.'s Liberty Mutual Property division in Weston, Mass. "A year ago everything was crazy, given everything that precipitated it."

"For 2003 and most likely 2004, the watchwords will be 'stabilization' and 'sanity,' following an insane period where neither underwriters nor buyers really knew what the baseline should be," said Alexandra Glickman, managing director and practice leader of Gallagher Real Estate & Hospitality Services in Los Angeles, a unit of Arthur J. Gallagher & Co.

See PROPERTY/page 22

## Liability market tightens

### Buyers boosting retentions

By JOANNE WOJCIK and SALLY ROBERTS

Many casualty insurance buyers are experiencing a lot more pain this renewal season than in prior years, especially when purchasing first-layer excess or umbrella liability coverage.

The extent of that pain, though, depends on the line of business, the type of risk and whether the coverage had been priced adequately before the market turned.

"Rates are still increasing, though the percentage of rate change is

probably not as high as it was last year. But when you boil that down on top of last year, it's still a very challenging market for risk managers," said Chuck D'Angelo, president of AIG Global Risk Management in New York, a unit of American International Group Inc.

Because of high prices and more rigorous underwriting guidelines, buyers are assuming higher deductibles and self-insured retentions and are looking at placing more business in captives and other alternative risk-financing vehicles.

Indeed, insurers are being a lot more discriminating about the risks they choose to underwrite, said Don Pickens, senior vp and chief underwriting officer specializing in large companies with multistate operations at Liberty Mutual Insurance Co. in Boston.

"As we look at trying to avoid an overdependence on a certain risk or industry group, risk selection and quality of risk is more important," he said.

The situation won't change by year end, industry observers say.

"I expect that we'll continue to see rate increases throughout this

See LIABILITY/page 12

Containing health care costs page 20

Making comp coverage work page 26

Cedents seeking security page 28

BI 07-07-03 A 12 7/2/03 1:12 PM Page 1



# Liability: Market tightening

Continued from page 10

year and into next year. Loss costs exploded in the late '90s, and many of those trends continue to carry forward to the early part of this decade. As a result, the umbrella market still needs price," said John Doyle, president of American Home Insurance Co. in New York, a unit of AIG that writes first-layer excess and umbrella liability coverage.

"I think management of most of the companies would like to see a little more correction before they are comfortable," said Joe Lombardo, chief market relations officer at Aon Group Inc. in New York.

"Under the threat of losing a piece of business or for the ones that have merited it by continuing to perform well after the last increase, you are getting close to where you can talk about" flat renewals, he said. "But the rule is more the 10% to 15% increases, and then you get into a layer where you need more correction, and then you have the horrors where the risk has just deteriorated. That's generally the theme."

## Paying more for less

While insurers say that 2003 rate hikes range from about 25% to 35% on average for primary liability, and perhaps 45% to 50% for first-layer excess and umbrella coverage, buyers say the rate hikes actually translate into much more because they often are tied to reductions in capacity.

For example, Sumitomo Electric Finance USA Inc. paid $180,000 for $50 million in umbrella coverage excess of $20 million last year. In 2003, it's paying $200,000 for just $25 million in umbrella coverage that attaches at $25 million.

Despite relatively flat sales and no significant change in exposure, this was the best deal the company could find in the market, according to William Hrotho, assistant treasurer at the New York-based manufacturer of automotive and telecommunications parts.

"We got quotes from 13 other markets," he said. "Some had higher attachment points. Some said they don't touch automotive. Some said their treaties don't allow automotive."

Other risk managers related similar horror stories.

"Our deductible quintupled, our premium more than doubled, and we lost franchiser E&O and non-owned auto coverage," said one California risk manager, who asked not to be identified. "We were able to buy back the non-owned auto for $100,000 with a $100,000 deductible—and we only had one claim in the last five years."

Wayne Salen, director of risk management at Home Quality Management in Palm Beach Gardens, Fla., said he can get general liability coverage only if he separates it from the nursing home operator's professional liability exposure.

"They do a dovetail policy for our type of business that includes GL and PL. When you lop off the PL part, it's possible to get some quotes for the GL. But the PL is virtually unobtainable," he said.

"Professional liability is just an exceptionally restricted and nasty environment," said Mr. Salen, who serves as chairman of the external affairs team of the Risk & Insurance Management Society Inc.

"They're all finite-risk programs today, fully self-funded, and the nursing homes are paying fronting fees to insurers to get the paper they need to prove they have insurance."

In addition to fully self-funding its professional liability exposure, HQM pays about $200 per bed per year for general liability coverage, which is up substantially from four or five years ago, he said.

"The fact that we get some risk transfer…is certainly better than nothing at all," Mr. Salen said. "We don't have any umbrella and excess, and I would venture to guess that no one in our industry has it."

Patrick F. Leonardi, director of risk management for Central States Trucking Co. in Bensenville, Ill., is an exception to the trend—the company is expecting its premiums to drop. After receiving a premium reduction last year on Central States' entire insurance program, he expects another decrease when he renews the account in October.

"I want to see a 10% decrease," he said. "My auto liability is doing great," he noted. "Last year, my auto losses were 21% of premium, which is decent for a trucker. This year, I'm down even lower, in the single digits."

Nursing homes, some professional liability areas, heavy products manufacturing, pharmaceuticals and transportation risks are among the risks having the greatest difficulty with renewals this year.

"These are areas where insurers have retrenched and pulled back capacity, and considering the price of coverage and the amount that's available, more companies are retaining it themselves," said Mr. D'Angelo of AIG Global Risk Management.

While the new Bermuda markets are providing some additional excess liability capacity, "they're not giving it away. They are not a source of cheap capacity," said Aon's Mr. Lombardo.

"Even 10% and 20% increases are substantial amounts. So we've seen some people who have lopped off pieces of their protection so they don't totally run a price tag they can't handle," he said.

## Creative approaches

Sometimes, buyers are seeing a gap between the primary and the excess when primary insurers can only go so high and first-layer excess insurers will not drop down far

See LIABILITY/page 14

BI 07-07-03 A 14 7/2/03 1:30 PM Page 1



# Liability: Market tightening

Continued from page 12

enough to meet the primary layer.

In those situations, risk managers are using a combination of insurance and alternative risk financing, such as captives, Mr. D'Angelo said.

"We are seeing, especially on the primary layers, a much more creative approach to using a captive and captive-like alternatives to try to structure their program on the primary, on the excess side, and to fill in the gaps wherever they can," he said.

HQM is among those using a rent-a-captive to fill in holes in its general liability program, according to Mr. Salen.

There is a renewed interest in captives, and that may be in part "because people are leery about the ability to predict some of their insurers' futures," Mr. Lombardo said. "They are still suffering a bit from the Kemper issue," he said, referring to Kemper Insurance Cos.' decision to sell off its insurance operations. "It took most of us by surprise."

Kemper bought the renewal rights to Reliance Insurance Co., and the insurer was successful in retaining about 80% of the Reliance book, Mr. Lombardo said. "So we have clients that went through the Reliance issue and then went to Kemper as the successor."

"I think the existing market has retained most of that business, but I think captives have become a solution for a lot of them," he said.

Many buyers are trying to improve their situations through loss control and more sophisticated risk management techniques.

"We are certainly seeing that our customers are placing more value" on loss prevention, agreed Kristen Albright, vp and chief underwriting officer in the business markets unit of Liberty Mutual Insurance Co.

Mr. Leonardi, for example, is being more selective about hiring.

"Most trucking companies will hire drivers in a day," he said. "It takes me a week, because I run background checks, and that just takes time."

## Going bare

Some buyers are becoming so frustrated with market conditions that they have pretty much thrown in the towel.

"There are certain accounts that are certainly cutting back on the capacity that they've purchased. In fact, we've even had some accounts nonrenew" their lead-layer excess coverage and "go completely bare, which, in this tort environment, is a very, very risky proposition," said Mr. Doyle of American Home.

"They're looking for options," observed Jim Conroy, national sales and marketing director for Stewart Smith Group Inc., the New York-based wholesale subsidiary of Willis Group Holdings Ltd.

"A couple of years ago, the market surprised clients, and this past year clients were more in tune to what was happening in the insurance market.

"So this year, they are contemplating what they want to do and, in doing so, may be purchasing less limits," he said.

# D&O: Rate hikes still hitting

Continued from page 10

Michael Rice, a Denver-based managing director of Aon Financial Services Group, a unit of Aon Corp., said the spread of hikes has been from 10% to more than 100%, compared with a range of 25% to 1,000% last year.

The hardest hit risks continue to be Fortune 500 companies, high technology companies, financial institutions, pharmaceuticals and telecommunications companies, market experts said.

Rate hikes for privately held companies and publicly traded companies with small market capitalization have been significantly lower at 30% to 50%, according to John Keogh, the New York-based president of National Union Fire Insurance Co. of Pittsburgh, Pa., a subsidiary of American International Group Inc.

Excess insurers continue to obtain from 75% to as much as 85% of the rate on the underlying layer, compared with 60% in 2001, market executives said.

Insurers also are seeking larger deductibles for Side B coverage, which reimburses corporations for sums they have paid executives to indemnify them for their losses, and for Side C coverage, more commonly known as entity coverage.

For large risks, insurers want at least seven-figure deductibles, experts said. But some "substantial companies" have assumed deductibles as high as $25 million to $50 million, noted Tony Galban, vp and worldwide D&O underwriting manager for Chubb Specialty Insurance, a unit of Warren, N.J.-based Chubb Corp.

As deductibles grow, more policyholders are considering buying only Side A protection, which covers losses for which a corporation is precluded from indemnifying its executives and which carries no deductible, Mr. Galban and other market experts noted.

Most risks still purchase all three sides, market experts noted. But insurer executives acknowledged that

See D&O/page 16

MH 07-07-03 A 14,16 7/2/03 4:14 PM Page 2



# D&O: Rate hikes still hitting

Continued from page 14

they are pushing policyholders to drop entity coverage. They warn that Side C coverage could hurt executives of bankrupt organizations, because bankruptcy courts have been freezing D&O insurance with entity coverage to safeguard that asset for creditors.

Broker Lou Ann Layton, a managing director and the national D&O practice leader at Marsh Inc. of New York, said she still expects that many companies will continue to purchase entity coverage. Those buyers do not consider themselves bankruptcy risks and do not see the price advantage in dropping the coverage, she said.

Some buyers that have dropped entity coverage also have agreed to preset allocations, under which a prescribed percentage of any loss will be considered attributable to the corporation and, therefore, will not be covered, noted Bill Cotter, chief underwriting officer at National Union.

Severability—an insurer's willingness to cover innocent executives for losses generated by the illegal, and therefore uninsured, acts of other executives—is a hot market topic, particularly regarding losses that lead back to misrepresented financials in insurance applications.

Insurer officials said that severability provisions are available but have restrictions. Officials with Chubb and National Union, for example, stressed that their provisions would protect executives not involved in creating misleading insurance applications but that the insurers would impute the offending executives' actions onto corporations and refuse to provide entity coverage.

In a related policy change, National Union will use a written admission of fraud—such as in a settlement or criminal plea agreement—to deny coverage for an insured executive. Previously, the insurer denied coverage only when fraud was established through adjudication.

Overall, buyers have to be careful in evaluating insurers' policy forms, advised broker Susanne Murray, senior vp and D&O practice leader at Hilb, Rogal & Hamilton Co. of New York.

Ms. Murray noted that several insurers have introduced new forms and reminded buyers that there is no standard D&O form. That means "there is no single form that is clearly the better coverage form, because everybody has something that's better than everybody else, and something that's worse than everybody else."

Working capacity has remained relatively stable at $400 million to $600 million for the largest risks, but insurers typically want to split their capacity among two or more layers, market experts noted.

And, while "there's a whole bunch of people who will play in the excess world," the number of insurers willing to write primary D&O coverage—particularly for Fortune 500 companies—is smaller, said Don Bailey, global practice leader in the Global Financial/Executive Risks Practice at Willis of New York Inc.

Executives agree that rising claim costs—attributable to claim frequency and severity—are driving the hard market.

But there also are other important factors, such as Delaware court rulings that have weakened executives' good business judgment defense, and continued high-profile corporate accounting irregularities nearly a year after the Sarbanes-Oxley Act began requiring top corporate executives to certify the accuracy of their organizations' financial statements, Mr. Keogh said.

For the next few years, "there are a lot of trends that suggest things are going to get worse," he said.

## E&O market 'spotty'

Across the E&O market, "I see a lot of spotty activity," said Clint Johnson, a senior vp at ACE USA in New York. "In some cases, rates are up, and in some cases, I'm actually seeing some softening of the rates."

Overall, he suggested that the E&O market is stabilizing, though "it kind of depends on the class of business."

Market experts say several risks, though, face higher rates: accountants, architects and engineers, lawyers, doctors, technology companies, certain financial consultants and insurance agents.

The settlements between some of the largest investment banks and New York Attorney General Eliot Spitzer over charges of improper business dealings are beginning to generate E&O insurance claims, which is making those banks "uninsurable," Ms. Longmore said.

Some risks are reducing their E&O limits to shave costs, Mr. Johnson noted. "We've seen some people drop covers or cut their limits to meet budgets, saying, 'I've got to pay for my (general liability) somehow.'"

The Big Four accounting firms are relying extensively on captives as part of their solution to E&O coverage. "You can see the captive use is high over there," said Ann M. Longmore, senior vp in Willis' Global Financial/Executive Risks practice.

A coverage issue heating up for various risks is their access to private medical records.

Ms. Longmore said many software developers with such access face exclusions for invasion-of-privacy or personal injury claims. With software clients asking for certification that the developers are covered for the privacy or personal injury risk, the developer and its broker often have to return to the E&O insurer after renewal to try to negotiate coverage of the information privacy exposure, she said.

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BI 07-07-03 A 20 7/2/03 1:15 PM Page 1



# Employers focus on cost control for health savings

## Disease management programs gain favor for improving care, lowering costs

By MICHAEL PRINCE

To rein in rising health care costs, more employers are turning to where the big expenses are.

More than in past years, employers in 2003 are adding disease management programs to their toolbox of cost-control methods. Implementing these programs, in addition to the well-used strategy of shifting costs to employees, is designed to reduce demand for health care services in areas that traditionally ring up huge costs.

As health care benefit costs continue to rise by around 15%, with the same forecast for 2004, employers are searching for new methods to control costs, experts note.

"The status quo is unacceptable," said Ted Chien, managing consultant at Watson Wyatt Worldwide in Minneapolis.

"Employers are saying cost-shifting is working well, but it's not enough. It's not addressing the underlying issue" of people's health, said Richard Sinni, managing director at PricewaterhouseCoopers L.L.P. in New York.

Experts estimate that, in general,

about 80% of health care costs are expended on about 20% of patients.

Many high-cost health conditions, such as asthma and diabetes, can be controlled, simultaneously improving patients' health while slashing treatment costs.

"That's where the big dollars are," Mr. Sinni said.

"Disease management really has the potential for saving money both for the short term and the long term," said John Erb, senior manager at Deloitte & Touche L.L.P. in Miami.

"Employers are looking for proactive ways to help manage medical costs," added Stephen Booma, executive vp at Blue Cross & Blue Shield of Massachusetts in Boston.

Disease management programs generally aim to improve individuals' health through changing their lifestyles, referring them to specialists and helping them adhere to their drug therapy.

To start a disease management program, employers must get people to complete an online health risk appraisal that identifies their health problems, said Kurt Weimer, president-East region at CIGNA HealthCare in New York.

"Employers are more willing than before to offer the use of health risk assessments via the Web to employees, and health plans are in a better position to deliver these assessments and to act upon the results," Mr. Chien said.

But getting people to complete the assessments is often difficult. To encourage them, employers are providing financial incentives for people to join disease management programs, Mr. Erb said. These incentives have included waiving copayments for the programs or even providing some type of gift, he said.

"People need an extra push," added Mr. Chien.

Employers in Massachusetts, for example, are investigating a variety of incentives to get people to join disease management programs to find the one that is most effective, Mr. Booma said.

**'Employers are saying cost-shifting is working well, but it's not enough. It's not addressing the underlying issue' of people's health.**

*Richard Sinni*
*PricewaterhouseCoopers L.L.P.*

"Everything is being explored," he said.

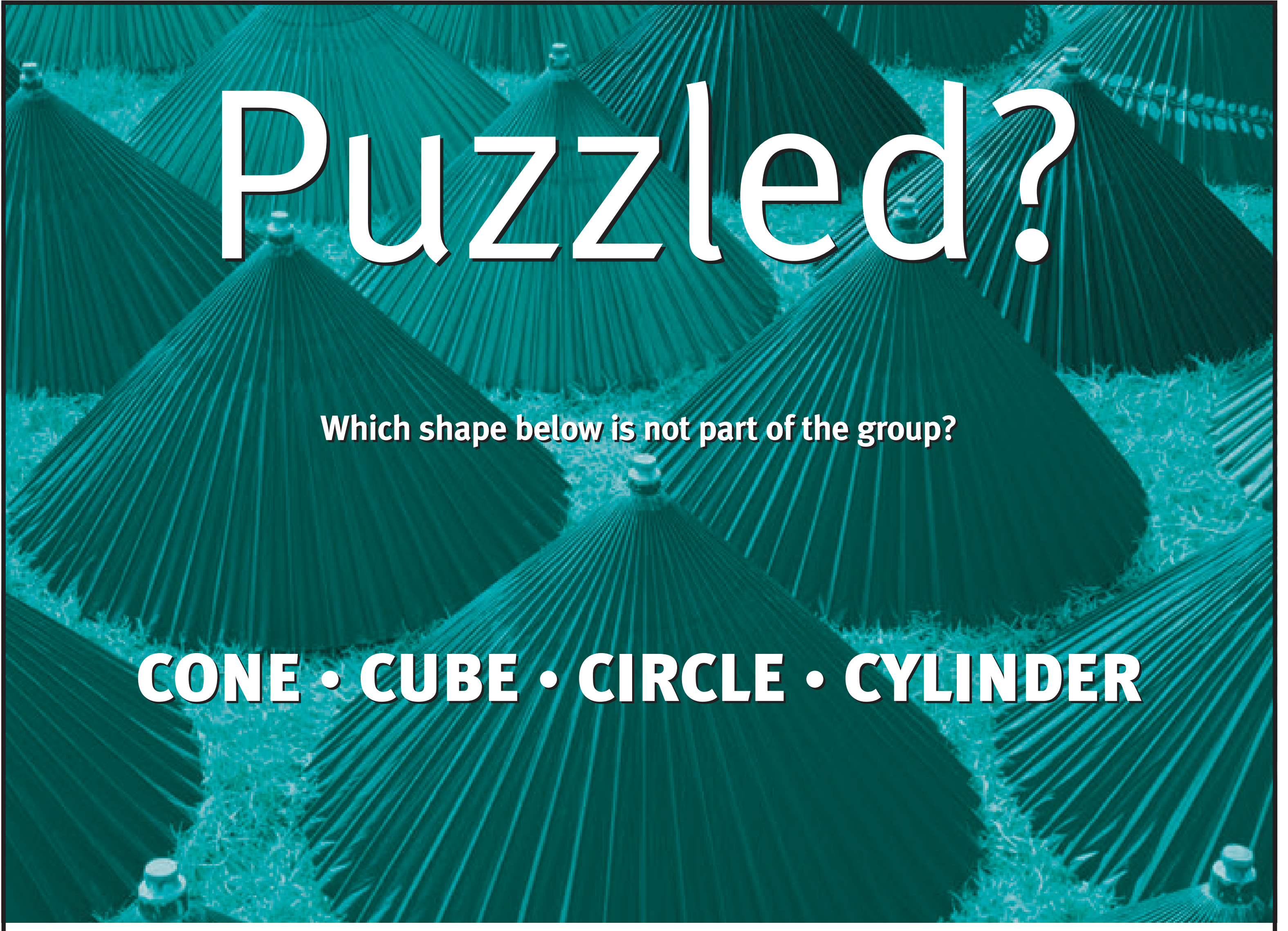
The disease management movement is part of the growing awareness by employers that controlling costs requires more than just adjusting the financial aspects of health plans, said Helen Darling, president of the Washington Business Group on Health.

"They are realizing that health care costs are caused by things that are avoidable, manageable or at least modifiable," she said.

This doesn't mean, however, that employers are getting away from cost shifting. Still, the first and primary response to rising costs is to shift part of them onto employees. Despite this strategy being in use for years, cost-shifting has not lost its ability to help lower costs, as many employers still have $10 copays, Mr. Erb said.

In particular, employers are raising copayments and deductibles with the idea that people who use the system the most should pay the most, said Sally Trude, senior health researcher at the Center for Study-

See HEALTH CARE/page 22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BI 07-07-03 A 22 7/2/03 1:16 PM Page 1



# Health care: Cost control focus

Continued from page 20
ing Health System Change in Washington.

Employers "are falling out of love with first-dollar coverage," she said.

This year has seen many employers replacing copays with coinsurance, "with the objective of having employees knowing the true cost of seeing a doctor," CIGNA'S Mr. Weimer said.

A concern with this strategy is that employers rarely make the switch while providing accompanying information to employees on the cost and quality of health care providers. Employees are therefore left shouldering a greater portion of the health care bill but lacking the tools they might need to select the most cost-effective provider, Ms. Trude explained.

> **Employers 'are falling out of love with first-dollar coverage.'**
>
> *Sally Trude*
> *Center for Studying Health System Change*

Employers this year have also shown greater interest in consumer-driven plans. But while interest is high, few employers are deploying these plans.

Some observers are worried that costs will continue to rise.

Mr. Erb said the cost increases are beginning to look like they stem from the aging of the population, a situation that will only worsen.

And Mr. Booma said a major reason for rising costs in Massachusetts is the lack of Medicaid funds from the state, which forces hospitals to charge the commercial sector more. He said state budget shortfalls would likely preclude a solution to this problem for years.

# Property: Clean risks seeing rates decline

Continued from page 10
"Rates throughout the first six months have stabilized and in many situations are showing reductions over last year," she said, "with the most significant change, I believe, being improved terms and conditions."

## Fortunes vary

Mike Chapman, executive vp at Hub International Ltd. in Wilmington, Mass., said that many risks generating premiums of more than $25,000 are seeing increases of 10% to 20%, about the same as during last year's renewals. Those that have clean loss histories, though, are more likely to see a flat renewal, he noted.

Tough risks, such as transportation companies and others "that are a little more difficult," are seeing rates rise around 20%, Mr. Chapman said.

Other factors also affect this year's renewals.

Gary Marchitello, managing director-national property practice for Aon Corp. in New York, said he sees renewals that generally are "flat to maybe 20% down. "It's case-by-case. The main factor in evaluating the treatment on a renewal is how a particular company, or even an industry sector, fared last year in terms of the kinds of increases they got."

Some risks hit hard with rate increases last year are watching rates go down, he explained. Commercial real estate risks, for example, got "whacked" in 2002, and some are seeing greater reductions at this renewal than are other types of risks, Mr. Marchitello said.

> **'It's case-by-case. The main factor in evaluating the treatment on a renewal is how a particular company, or even an industry sector, fared last year in terms of the kinds of increases they got.'**
>
> *Gary Marchitello*
> *Aon Corp.*

Even when buyers are charged more for coverage, the increases generally are smaller than those seen in recent years.

Excess and surplus lines underwriter Lexington Insurance Co., a unit of American International Group Inc., is increasing rates just over 10% for many property risks, but "that's nothing like it was over the past three years," said John Graham, chief property underwriting officer at AIG.

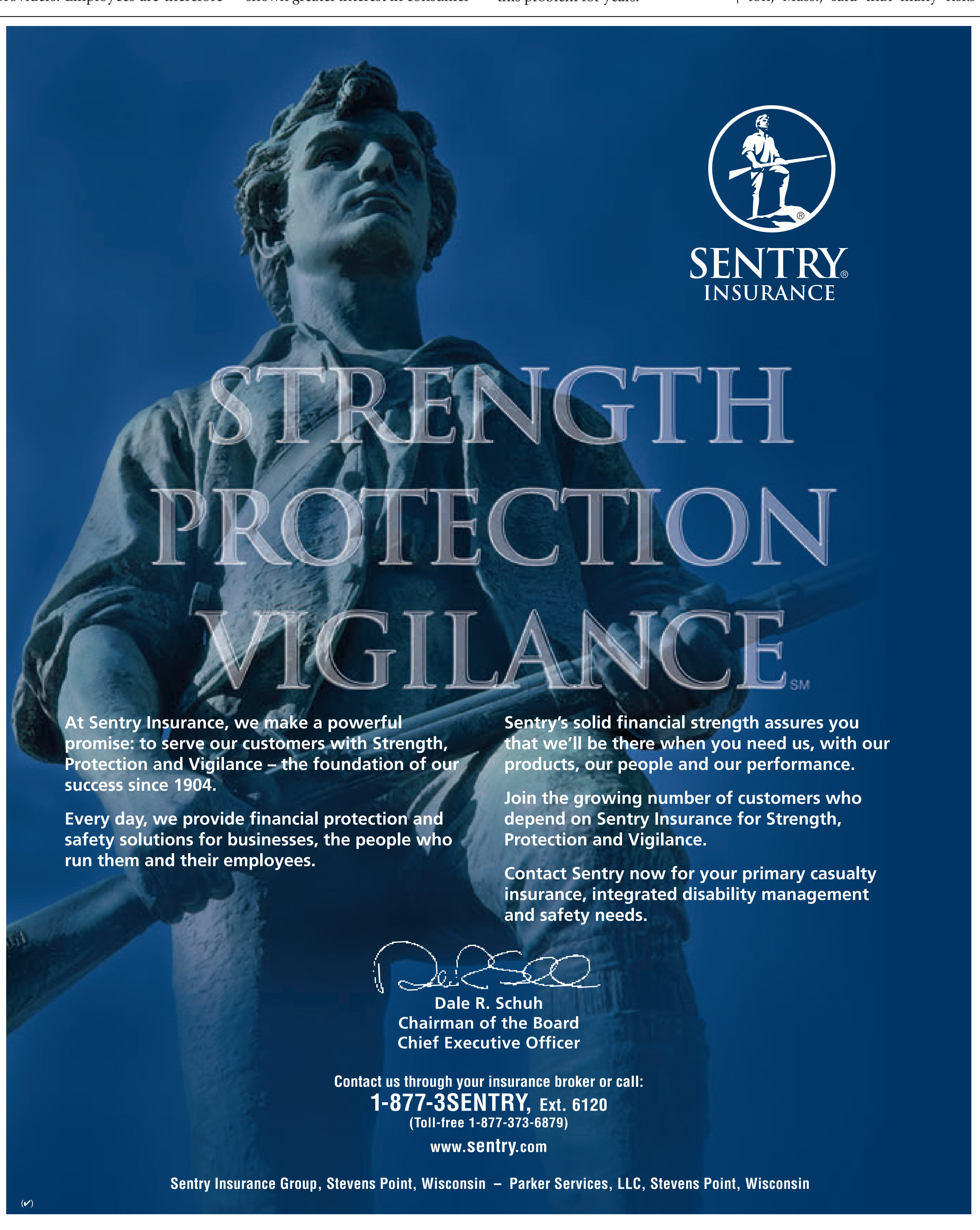
Rate increases in those years reached 30% to 40% for some policyholders, he said.

Lexington generally writes primary coverage of up to $25 million but has written some accounts to $50 million and $100 million this year, according to Mr. Graham. Those high-limit accounts have seen rate increases smaller than 10%, or, in some cases, rate decreases, he confirmed.

From a buyer's perspective, this year's renewals for the most part are a "welcome change," said Randy Schreitmueller, vp at Johnston, R.I.-based Factory Mutual Insurance Co., which does business as FM Global.

"Rate increases are pretty much

See PROPERTY/page 24

BI 07-07-03 B 1 7/2/03 1:10 PM Page 1



# AGENT/BROKER TOPICS

A MONTHLY EDITORIAL SECTION SENT EXCLUSIVELY TO AGENTS, BROKERS AND CONSULTANTS

# Legislative Issues

# Tort reforms at top of industry wish list

## *Producer, insurer groups back reform of asbestos, med mal, class actions*

By ALLISON REYNOLDS

Agents, brokers and insurers have a long list of legislative concerns this year, and at the top of that list is litigation reform.

From asbestos to medical malpractice to class-action litigation, tort reform is one of the most significant legislative battles in Congress today, lobbyists say.

A key issue for producer and insurer groups is reform of the asbestos litigation system, which has led to huge losses for insurers and has driven scores of companies into bankruptcy.

"This is a crisis crying out to be resolved after decades of being a black hole," said Joel Wood, senior vp of government affairs for the Council of Insurance Agents & Brokers in Washington.

An asbestos liability reform bill is being marked up by the Senate Judiciary Committee, though action on the bill has been delayed until lawmakers return from their recess on July 10. A reform package was introduced in the House in March but has not yet been taken up by the House Judiciary Committee.

The Senate bill, the Fairness in Asbestos Injury Resolution Act, S. 1125, would replace the current litigation-based system for compensating victims of asbestos-related diseases with a $108 billion trust fund (*BI*, June 30). Asbestos defendant companies and their insurers would contribute most the money for the trust fund. Claimants who met specified medical criteria would receive awards based on the seriousness of their illnesses, with claims administered by federal courts.

Mr. Wood said the CIAB supports the framework of the asbestos reform bill and is urging lawmakers to pass the measure. He credited strong Senate leadership, such as the bill's author—Judiciary Committee Chairman Sen. Orrin Hatch, R-Utah—with helping to push the issue forward.

Insurer trade groups, including the American Insurance Assn. in Washington and the Alliance of American Insurers in Downers Grove, Ill., also are urging asbestos reform at both the state and federal levels.

"Considering the impact on the industry, (asbestos reform) is a very important issue," said John Lobert, senior vp of state government affairs for the Alliance. "We're supportive of the legislation, assuming that there's fair and equitable funding" of the national trust fund.

Insurance industry groups also are calling for medical malpractice reform.

Growing malpractice litigation has led to costly settlements and huge jury awards, increasing costs for both employers and consumers.

"I've got agents all over the country looking for medical malpractice reform," said Robert Rusbuldt, chief executive officer of the Independent Insurance Agents & Brokers of America in Alexandria, Va. "This is something that's happening all over the country and is really affecting our markets."

The House of Representatives in March passed the Help Efficient, Accessible, Low-Cost Timely Healthcare Act. The measure would cap noneconomic damages in medical malpractice cases at $250,000 and would limit punitive damages to the greater of $250,000 or twice economic damages. In addition, it would limit any one defendant's financial liability to the proportion of its responsibility.

Despite House passage of the bill, its chances for approval in the Senate remain uncertain. The House passed a medical malpractice reform bill in the last congressional session, but the Senate never took up the measure.

Mr. Wood said that the CIAB is hopeful that a medical malpractice reform bill can be passed in the Senate. "We're trying to involve as many Senators as we can to reach the magic 60," he said, referring to the number of votes needed cut off filibusters and bring the HEALTH Act to a full vote.

A third tort reform—changing the class-action system—is also on the legislative agenda of producer and insurer trade groups.

A key concern of class-action reform proponents is the elimination of so-called "forum shopping," which is plaintiff attorneys' practice of selecting the most plaintiff-friendly venues when filing class-action litigation.

Last month, the House passed the bipartisan Class Action Fairness Act of 2003—H.R. 1115—which allows for the removal of some interstate class actions from state court to federal court, provided that plaintiffs and defendants were from different states and that the amount at stake was at least $5 million. (*BI*, June 23)

A similar class-action reform bill, S. 274, cleared the Senate Judiciary Committee in April, and the Senate is expected to take up the bill this summer, observers note.

"We're within shooting distance on class-action reform," said Mr. Wood.

Another legislative issue of importance to brokers and insurers is the reauthorization of the Fair Credit Reporting Act. The law, which expires at the end of this year, was designed to promote accuracy, fairness and privacy of information in the files of every consumer-reporting agency, such as credit bureaus.

Both the National Assn. of Independent Insurers in Des Plaines, Ill., and the Alliance are urging lawmakers to reauthorize the law.

The House Financial Services Subcommittee on Financial Institutions introduced legislation last Thursday to reauthorize the expiring provisions of the FCRA. The bill also would increase the consumer protections against identity theft. The bill will be the subject of a July legislative hearing and markup in the Financial Institutions Subcommittee.

"We're trying to make sure the Fair Credit Reporting Act gets extended so consumers have more options," said a spokesman for the AIA. "There needs to be a balance with the rules so that a company can use consumers' information to help them have more choices but still have that information be private," he said.

The IIABA also supports reauthorization of the FCRA, but Mr. Rusbuldt said that Congress needs to look at the misuse of insurance policy expiration dates and clarify the provisions or add an amendment in the bill to ensure that lenders aren't selling customers' information to third parties.

Regulatory debate divides industry / 22B | Grassroots campaign sees yield / 22D

AGENT/BROKER TOPICS

# Federal regulation of P/C industry unlikely anytime soon

## *Lack of consensus in industry a large barrier to federal charter*

By MICHAEL BRADFORD

There is a clear consensus on the prospects for federal regulation of property/casualty insurers: It won't happen any time soon.

Beyond that, there is a sort of civil war over the issue, with camps of federal regulation backers pitted against those who defend the states' right to control the industry. Then, there are those who support a middle-ground approach that involves both federal and state regulation.

The one thing all sides agree on, though, is that a resolution is some time away.

Congress is expected to hold hearings on federal regulation proposals late this summer, but few think legislation will emerge. "I don't think anything is going to happen this calendar year," said Dave Farmer, Washington-based senior vp at the Alliance of American Insurers. "We're really talking about 2004."

"I don't think Congress is ready for any kind of major regulatory insurance proposal, because there is no consensus in the industry," said Robert A. Rusbuldt, chief executive officer of the Independent Insurance Agents & Brokers of America. Instead, insurers and brokers have split into distinct camps, he noted. "I honestly believe that the industry has to come together and show some unity on the Hill to make any progress."

Insurers and brokers are divided even within their own ranks as to which regulatory direction is the right way to go.

The Alexandria, Va.-based IIABA proposes a middle ground, urging that "federal tools" be developed to foster a more streamlined and uniform system of insurance regulation.

"We share the perspective of everybody else—that the state system needs to be reformed," Mr. Rusbuldt explained. But, he added, "we don't want to throw out a system that needs modernization" and can be updated without being overhauled.

Under the IIABA's proposal,

> **'We agree that state insurance regulation needs more modernization than we have seen.'**
>
> *Dave Farmer*
> *Alliance of American Insurers.*

federal law would mandate certain standards that would fall under the authority of state regulators. "We have to have some national standardization," Mr. Rusbuldt said, to create efficiencies in the insurance distribution process and allow insurers to react more quickly to market conditions.

To speed the introduction of insurance products, for example, the IIABA would like to see a standard that lets insurers use new policy forms no later than 30 days after they have been filed with state insurance departments, as long as they are not disapproved within that time period. Mr. Rusbuldt said insurers have told him it sometimes takes a year or longer to gain approval for a new product.

The IIABA plan also calls for licensing reciprocity in all states and the pre-emption of countersignature laws. The association would like to see the National Assn. of Insurance Commissioners develop a uniform licensing standard that would keep some insurers from migrating toward states with lenient requirements.

The Washington-based Council of Insurance Agents & Brokers, meanwhile, backs the idea of a federal charter that would give insurers the ability to opt out of state regulatory systems.

"We remain a supporter of the charter concept," said Joel Wood, CIAB's senior vp of government affairs. "Ultimately, it is the only reform that will bring us parity with our international counterparts as well as financial service providers in other sectors of the industry."

The American Insurance Assn. is a strong supporter of an optional federal charter.

State regulators have promised to reform their systems, but it hasn't happened, a spokesman for the Washington-based AIA said. The association proposes legislation that would allow insurers to write property/casualty business in any state without being subject to state rate and form regulation. A federal director, based in the Treasury Department, would hold regulatory authority.

Under the AIA proposal, insurers opting for federal regulation would enjoy pre-emption from state laws pertaining to rate and form regulation, licensing, solvency, marketing, claims handling and market conduct. State regulation of federally chartered insurers would be permitted in, among other areas, matters of state and local taxation, participation in residual market mechanisms, corporate governance and mandatory participation in statistical or advisory organizations.

"This is going to be a multiyear effort," the spokesman said of the AIA's work to convince Congress that a federal option is needed. But that gives insurers the opportunity to educate lawmakers on the workings of insurance regulation, he said.

Mr. Wood said the federal option is important because, under the current system, it is "extraordinarily difficult" for insurers to conduct business while complying with myriad regulations in 50 states. The current system bogs down the introduction of new insurance products, he said, and insurers lag far behind other financial services companies that face fewer regulatory burdens in bringing products to the marketplace.

Even with such perceived advantages to a federal charter, some insurers say they want to leave regulation in the hands of the states.

"We agree that state insurance regulation needs more modernization than we have seen," said Mr. Farmer of the Alliance. But a federal charter would simply create a costly dual system, he noted.

He said the Alliance is committed to improving state regulatory systems and is working with the NAIC and state insurance commissioners to do so.

Rate and form approvals in many states "take a significant amount of effort" and slow the competitive process of bringing new products to market, Mr. Farmer noted. Among the Alliance's goals is to see states abandon mandatory forms and adopt regulations under which insurers could file forms that would gain acceptance as long as they met certain standards.

Mr. Farmer said proponents of state modernization have run into problems from "a number of large states that want to do business the way they've done it for a hundred years" rather than updating their regulatory practices.

The Des Plaines, Ill.-based National Assn. of Independent Insurers also opposes federal encroachment into regulation.

"Every state is unique" and each needs to deal with their own "unique insurance issues," said an NAII spokeswoman. Like the Alliance, the NAII is working with the NAIC to urge states to modernize their regulatory schemes.

"It's an ongoing process," she said, and could take "several years." The NAII said it believes Congress should give states plenty of time to change their regulatory systems without the threat of federal intervention.

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*IIABA, Georgia association issue legislative award*

# Agent helps lobbying efforts take root

*Robert E. Fulwider, this year's recipient of the Sidney O. Smith Award, has worked for years to establish what he considers to be the most successful grassroots lobbying effort to deal with farmers' crop insurance problems.*

*As an authority on crop insurance, Mr. Fulwider has worked to ensure that independent agents continue to meet farmers' needs, Ronnie Tubertini, government affairs committee chairman of the Independent Insurance Agents & Brokers of America, said in a statement.*

*The Smith Award is given annually by IIABA and the Independent Insurance Agents of Georgia to an agent or broker for service in government affairs. Mr. Smith was an IIABA president and Georgia agent who focused the association as well as its members on influencing legislation.*

*Mr. Fulwider, an executive committee member of the IIABA and a specialist in crop insurance issues, grew up on a 1,000-acre farm in east-central Iowa and earned a degree in agricultural education from Iowa University. "It becomes a passion with you. You get so involved with it, you really feel and care on the farmers' behalf what's going on with crop insurance," Mr. Fulwider said.*

*From 1994 to 1997, Mr. Fulwider served on IIABA's government affairs committee and chaired the committee from 2000 until 2002. He was appointed as IIABA's representative to U.S. Department of Agriculture's Commission to Improve the Federal Crop Insurance Program in 1989-1990, and he chaired the association's Crop Insurance Task Force.*

*Mr. Fulwider is principal and executive vp of the Ray Wuestenberg Agency Inc. in West Liberty, Iowa, and he is also principal and executive vp of Fulwider Agency Inc. in West Branch, Iowa.*

*He recently spoke with Business Insurance intern Yvonne Teems about his accomplishments.*

**Q: What do you see as the biggest legislative issue affecting most agents and brokers today?**

A: The biggest one that I see coming down the pike is the issue of federal vs. state regulation of insurance. It will probably be several years before everything is completely formalized, but it has a dynamic impact on not only the American agency system in which we participate, but it has a tremendous impact on consumers and everyone nationwide.

**Q: Why do you think this is so significant?**

A: The business itself has changed. We've become a more global society. Our national association has put together a modified version of attempting to allow for some government guidelines to regulation, but (while) maintaining and preserving the regulation at the state level as our basic avenue toward providing insurance in the future.

**Q: What legislative issue affects you personally as an independent agent?**

A: In rural America, we've had a big impact with the crop insurance issues over the past years. The Independent Insurance Agents & Brokers of America have testified and been involved with regulation and law changes regarding federal crop insurance (about 23 different times) since 1980. That's a lot of impact on independent agents to have us in there.

**Q: What specifically are you doing to lobby for your cause?**

A: We have a pretty substantial grassroots lobbying effort when it's totally fired up and at full force. Many agents feel a passion toward it, and so when something happens, they really rally around a solid grassroots effort. Coupled with that is the whole arena that we have in our Washington office for the Independent Insurance Agents & Brokers of America. We have an outstanding lobbying office there and excellent professionals that really understand the program and do it well. A third component is many of our agents are close to the producers, to the farmers themselves, so when the need arises and we need a more heavy foot than we can give, many times we turn to the farmers themselves. They join with us and approach their congressmen and senators to get some changes made.

**Q: In your years as a government affairs representative for the IIABA and in lobbying for Congress, what are you most proud of?**

A: We've had a lot of successes. But what I'm most proud of is the origination of what we feel is the best alternative to federal vs. state regulation.

That's where we're working toward what we call our national treatment issues. Our alternative is maintaining as much regulation as possible at the state level. (We want to) strengthen the regulation of the insurance environment without turning to the federal government.

**Q: How would you generally describe the involvement of independent agents today when it comes to legislative affairs? Are there enough agents involved?**

A: We recognize that our members are extremely busy people with their own operations, so there's…a limit to what a lot of them can do. But they do rally to the cause, and they do come across. Now, one area they need to do a better job of, quite frankly, is supporting our political action campaign. Many agents are receiving advantages from our lobbying efforts, but they're not supporting it with their checkbook.

**Q: Why do you think they're not doing that?**

A: Some of them don't fully understand the significance of it. We've been successful to get the job done on their behalf, so why should they do anything to contribute toward it? Secondly, some don't support political action campaigns. They think it's wrong to do so. Those people don't fully recognize that it's just a sign of the times; this is the way it's done. Many of them also are involved heavily in local and statewide campaigns, so they feel they're doing their part there. Now, our federal PAC is growing; it's at its all-time historical high. It will continue to grow, but we could do much better.

**Q: What do you think is the best way for an agent or broker to get involved in the legislative process?**

A: When asked on the part of a state or national organization to become involved at the grassroots level, do so with whatever power you have. Many people have a direct connection, and that's what makes (their involvement) so strong grassroots-wise. Many of our agents are personal friends of senators and congressmen, both at the state and national level. The thing that's really important in our arena, because we are so close to the customer, is that we, in turn, have a feel for how our customers feel about these things. And we can at least tell them what our customers are saying.

**Q: Have you ever considered running for office?**

A: I felt that I could probably do more for my own discipline as an insurance agent. Part of the reason I haven't sought public office is that in Iowa, many of our state public officials have had local political experience before they ran for the state office. I have always shied away from local political experience because I feel that as an independent businessman, you really have to be careful when you're dealing with the public and you're making decisions on their behalf. It can affect your business, plus your business can affect your (political) decision-making.

Royal & Sun Alliance
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# A/BT briefs

## Educational organization to honor industry CSRs

**AUSTIN, Texas**—The National Alliance for Insurance Education & Research has named the state winners of its 2003 Outstanding CSR of the Year Award.

The award, created in 1991 to recognize the contributions of outstanding insurance industry customer service representatives, this year recognizes individuals in 41 states and Puerto Rico. From the state winners, a national winner of the award will be selected.

To qualify, candidates submitted an essay on customer service skills and had to demonstrate commendable service to their agencies, their industry and their community. A candidate must be an insurance customer service representative or have primary responsibility for insurance customer service duties.

The National Alliance for Insurance Education & Research, based in Austin, Texas, offers advanced professional education for insurance and risk management professionals. For names of the winners and more information, visit *www.scic.com.*

**Agent/Broker Topics**
**ADVERTISER INDEX**
**Issue of July 7**

| ADVERTISER | PAGE # |
|---|---|
| Brownyard Group | 22B |
| Compliance & Filing Solutions | 22D |
| Greater NY Insurance Co. | 22B |
| The Hartford | 22C |

## Insurance educator receives IEF award

**INDIANAPOLIS**—The Insurance Education Foundation has named Marcia E. Allen, a teacher at Murphysboro High School in Murphysboro, Ill., as this year's James L. Osborne Insurance Educator of the Year.

The national award, named for the Indianapolis-based IEF's founder, is presented each year to a teacher who demonstrates excellence and creativity in providing insurance education to high school students.

Eligibility was limited to the 2,130 teachers who have graduated from one of seven insurance education institutes sponsored by IEF over the past 15 years and who have taught insurance during the past school year in a course leading to a high school diploma.

## Briefly noted

Redwood City, Calif.-based **ABD Insurance & Financial Services** recently launched ABDConnect, a new online self-service employee benefits and human resource communications tool that enables its clients to deliver information and functionality to their employees.…**The Leavitt Group,** based in Cedar City, Utah, has been named "Agency of the Year" for the Western division by The Hartford Financial Services Group Inc.…Walnut Creek, Calif.-based **Heffernan Insurance Brokers** recently expanded its operations to the East Coast with the opening of a Wellington, Fla. office.…Old National Bancorp recently closed its deal to acquire the **James L. Will Insurance Agency Inc.** based in Evansville, Ind.

BI 07-07-03 A 24 7/2/03 1:17 PM Page 1



# Property: Clean risks seeing rate reductions

Continued from page 22

as we predicted six months ago," Mr. Schreitmueller said. "The majority of our renewals today are probably flat renewals compared with a year ago, flat or slightly above flat year-to-date."

"Consumers should be saying 'thank God,' because it was a tough 18 months," said Damian R. Testa, president of the New York region for Hub International. "This year, we're seeing property rates drop a lot on the very big risks."

Mr. Ewing said Park Place was able to lower its coverage costs significantly by working hard to present its risk in the proper light. "I give a lot of credit to both of my brokers," Marsh Inc. and Willis Group Ltd., he said.

With his brokers' help, "we put together the best presentation Park Place has ever had," Mr. Ewing explained.

"We laid all of our cards on the table, and I spent a lot of time on planes" meeting with underwriters in London, Paris, New York and other cities to work out coverage layers for around $12 billion in property owned by the casino company, he said.

Mr. Ewing said he found during this year's renewal that underwriters are "truly looking for a commitment to a property conservation program" and aren't interested in a risk if there is a chance claims will be "self-inflicted" because of shoddy loss prevention programs.

Pacific Tomato Growers has gotten the word that its August property renewal will be flat, said Michael Benishek, risk manager at the Palmetto, Fla.-based company. It's the second consecutive year he's seen a flat renewal: Last year's coverage cost went up just $348, although the program's deductible was doubled to $10,000.

Mr. Benishek also carries a $500,000 windstorm deductible on coverage for coastal Florida property. The deductible was raised significantly—from $25,000—over the year before.

"I'm smiling," Mr. Benishek said, although some of his colleagues are not. There still are some tough risks out there, he said. "I talk to my buddies at the (Risk & Insurance Management Society Inc.) luncheons, and I hear some horror stories."

## No rush for terror cover

Buyers in many cases aren't willing to pay a lot of money, if any at all, for terrorism coverage.

Park Place decided not to purchase the costly coverage on its property risks because it feels adequately protected, Mr. Ewing said. Security is constant at casinos that never close, he explained. And, in Las Vegas, the city has emergency services trained to respond to terrorist attacks.

Much of the decision to purchase terrorism coverage has to do with the "risk appetite of the corporation and upper management," Mr. Ewing said.

"Terrorism coverage continues to be driven by lenders' requirements," said Gallagher's Ms. Glickman. The 2002 Terrorism Risk Insurance Act, which created a federal backstop for coverage, "really removed the bogeyman—the fear that many insurers had prior to November of last year. We're seeing terrorism being backed back into many programs."

Mr. Testa said rates for terrorism coverage in midtown Manhattan are "dropping dramatically" as insurers overcome their fears of writing the coverage. Outside of Manhattan, where lenders generally don't require the coverage, many risks don't buy it unless it is very cheap, he said.

Mr. Nelson of Liberty Mutual said around 28% of the insurer's customers are buying terrorism coverage, with most of the purchasing occurring on the East and West coasts. Commercial real estate accounts are interested in the coverage, as are some retail businesses, he said.

FM Global, which writes a lot of manufacturing accounts that are located in areas not considered at a high risk of terrorist activities, has seen a much higher number of policyholders opt for the coverage. Mr. Schreitmueller said 60% to 70% of the insurer's clients buy terrorism insurance.

"We did price it fairly," Mr. Schreitmueller noted, "and I think we communicated more effectively."

PHOTO: ZUMA

Park Place Entertainment Corp., which operates the Paris Casino, among others, said that it did not purchase terrorism coverage in part because of the quality of security and emergency services already in place in Las Vegas, Nev.

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BI 07-07-03 A 26 7/2/03 1:18 PM Page 1



# Double-digit rate hikes continue for workers comp

## Terrorism coverage is a new consideration at renewals for many buyers

By MEG FLETCHER

Workers compensation coverage is seeing double-digit price increases, largely due to rising medical costs, and the issue of terrorism coverage is complicating the renewal process somewhat.

From a coverage standpoint, the 2002 federal terrorism coverage law does not affect most employers, because nearly every state's workers compensation laws provided even broader coverage than that which insurers are required to make available through the Terrorism Risk Insurance Act.

Prior to the Sept. 11, 2001, terrorist attacks, state laws typically required that employers have workers comp insurance that provides protection for workers injured through acts of terrorism—whether caused by domestic or foreign agents—as well as injuries caused by acts of war.

Terrorism coverage "is mandatory for workers comp, so we had no choice" but to provide it for workers, said Jim Crockett, manager of risk and employee benefits for Denver Water in Denver. He is also vice chairman of the Risk & Insurance Management Society Inc.'s External Affairs Committee.

Among the states that require workers comp coverage, only Pennsylvania excluded coverage for acts of war prior to the enactment of TRIA, according to Peter M. Burton, senior division executive-state relations for the Boca Raton, Fla.-based National Council on Compensation Insurance. So, the federal act required insurers there to offer coverage broader than the state's mandates.

From a pricing standpoint, however, insurers for the first time recognized and actuarially analyzed their rate need for the TRIA-defined terrorism risk and priced it separately, Mr. Burton said. In most states that use the NCCI as a guide for what to charge, the TRIA component ranged from 1 cent per $100 of payroll to 5 cents per $100 in the voluntary market or 7 cents per $100 in the assigned-risk plan, Mr. Burton said. The highest rates are in the District of Columbia.

The cost of TRIA is generally considered manageable, and most insurers calculate it as a percentage of "standard premium," while other insurers use slightly different approaches, said Paul Smith, executive vp with New York-based Willis Risk Solutions, a unit of brokerage Willis Group Holdings Ltd.

**'Given the various methodologies that individual insurers use to pass on the cost of TRIA, it may be a benefit to buyers to explore alternative sources of coverage.'**

*Paul Smith*
*Willis Risk Solutions*

The rate an insurer charges for TRIA coverage may vary, however, except in a state's residual market, where servicing insurers are required to charge an established rate, Mr. Burton said. Most insurers use the NCCI's benchmark rates, sources said.

"Given the various methodologies that individual insurers use to pass on the cost of TRIA, it may be a benefit to buyers to explore alternative sources of coverage," Mr. Smith said.

Overall, buyers are facing workers comp rate increases of 10% or more during this renewal period, according to most insurers, brokers and employers. The current average increases of 10% to 15% are less than the 15% to 20% increases buyers saw last year, said Vincent T. Donnelly, president and chief operating officer of PMA Insurance Group in Blue Bell, Pa.

Some policyholders are seeing rate increases of 15% to 30%, Mr. Smith said. Meanwhile, Stephen Kelley, president of Muirfield Underwriters Ltd., a Chicago-based managing general underwriter, reported a broader range of rate changes—from a 5% reduction to a 20% increase. Muirfield is an Aon Corp. affiliate.

"While rates are not coming down, the rate of acceleration may be easing," said Greg Berg, vp for the Hartford Financial Services Group Inc. in Hartford, Conn. No one expects the hard market to end soon, however.

Finding coverage is not a problem for policyholders, especially since states typically have assigned-risk plans that serve as the market of last resort.

Rising medical costs are a major cause of employers' higher premiums. According to the NCCI, workers comp medical cost increases for lost-time claims rose to 12% from 10.7% from 2001 to 2002.

Many policyholders are responding to these market conditions by retaining higher levels of risk, said Brian Melas, senior vp-commercial markets administration with Boston-based Liberty Mutual Insurance Co.

For example, the Miami-Dade County Public School System decided late last month to increase its self-insured retention on its excess compensation policy to $750,000 from $500,000, said Scott B. Clark, risk and benefits officer. It will now pay $1.5 million for that coverage, compared with the proposed $2.4 million premium it would have otherwise faced, he said.

Mr. Clark said the district plans to hire a consultant to help it better manage the most frequent claims in that new retention level, which are primarily filed by workers who help transport disabled children. The system's goal is to prevent permanent total claims by providing alternatives including modified duty and career retraining, he said.


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Duane Morris is pleased to announce the firm's expansion into San Diego and Southern California. We welcome Mitchell L. Lathrop and Thomas R. Newman, nationally recognized insurance industry lawyers, and their colleagues, who bring their national practice and experience to Duane Morris and the firm's Insurance and Reinsurance Industry Practice.

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BI 07-07-03 A 28,30 7/2/03 1:18 PM Page 1



# Tight market conditions continue for reinsurers

## Ceding insurers making demands for additional security

By DOUGLAS McLEOD and JUDY GREENWALD

Market conditions remain tight at midyear for property/casualty reinsurance as reinsurers deal with an emerging trend: demand by ceding insurers for additional security to back reinsurance recoverables.

Ceding insurers, led by American International Group Inc., are increasingly requiring reinsurers to post collateral for outstanding balances, or are demanding contract language that requires reinsurers to take various steps if the reinsurers' financial strength ratings are downgraded.

These steps can include posting letters of credit or other collateral to secure a ceding company's recoverables; allowing the ceding company to demand commutation of the contract; or requiring that the downgraded reinsurer be replaced by another reinsurer on the program, sources report.

Reinsurer reaction to the security demands has been mixed, with some refusing to go along with the demands, others acquiescing and still others studying the matter.

While some contend that so-called "downgrade" or "termination" clauses provide extra protection for ceding insurers, most agree that widespread use of the provisions would create problems for reinsurers, imposing additional costs and reducing investment flexibility.

"From the reinsurers' perspective, I don't see how it could be anything other than a negative," said Robert DeRose, senior financial analyst with A.M. Best Co. in Oldwick, N.J.

The renewal market, meanwhile, remains tight for most buyers, with slower rates of increase in property reinsurance pricing and continued hardening of casualty pricing, especially for such difficult lines as commercial umbrella, professional liability and medical malpractice, reinsurance market sources report.

### Focus on security

AIG has taken the lead in pushing reinsurers for additional security.

At the insurer's annual shareholder meeting in May, Chairman and Chief Executive Officer Maurice R. Greenberg noted that huge insurance and investment losses have led to numerous reinsurer rating downgrades.

"Every reinsurer we do business with has to meet certain standards," Mr. Greenberg said. "As they were downgraded, we have taken them off our credit list. They can only stay on our list if they post collateral—and we don't care if they are domestic or foreign—adequate to meet the exposures we may have to them."

If AIG's list of approved reinsurers shrinks, "so be it," Mr. Greenberg said. "If we keep more business for ourselves, we will do that....We will not reinsure with somebody that might not be around to pay a claim."

To stay on AIG's approved list for certain casualty business, some reinsurers have been asked to collateralize all outstanding recoverables, including incurred-but-not-reported losses, reinsurance market sources say. The insurer's demands have varied, though, from reinsurer to reinsurer, sources add.

An AIG spokesman cited Mr. Greenberg's comments at the annual meeting but did not respond to requests for further details.

A number of ceding insurers—particularly large stock companies—have followed AIG's lead, seeking collateral for outstanding recoverables or demanding downgrade clauses in contracts up for renewal, reinsurers report.

> **'Downgrade clauses sound good, but if everybody has one, it doesn't help them that much.'**
>
> *John Berger*
> *Chubb Re*

There are more downgrade clauses, said John N. Gilbert, president and chief executive officer of New York-based reinsurance intermediary Holborn Corp., a reinsurance intermediary. "They have become quite popular," he said. "I don't want to say they're necessarily standard, but they are in greater use, though some companies and markets view it as potentially creating problems for both parties. There is some resistance to them."

David Priebe, managing director at reinsurance intermediary New York-based Guy Carpenter & Co., said that "it's a growing issue" as to whether reinsurers will support a clause that requires them to post collateral. "From what we're seeing, there are certain reinsurers willing to embrace the concept."

However, "the majority of reinsurers haven't yet agreed to follow that provision. Most of our clients have taken a rather disciplined approach in terms of their market selection and have adopted a variety of techniques to ensure the quality and the performance of their reinsurance contracts, and so I think that's still under discussion and changing," said Mr. Priebe.

In some cases, particularly where a reinsurer is showing financial weakness, the actions make sense, some reinsurers concede. Banks demand added security from riskier borrowers, so, "Why should reinsurance be any different?" said John Berger, president and chief executive officer of Chubb Re in Bernardsville, N.J.

Even reinsurers with A+ Best ratings are being asked for collateral and downgrade clauses, though.

"What it's saying is that they have no confidence in the rating agencies," said James Pilla, CEO of Toa Reinsurance Co. of America in Morristown, N.J., referring specifically to AIG.

Downgrade clauses may not provide the intended extra security if they become too widespread, some reinsurers suggest. If a reinsurer that has the clauses in most of its contracts is downgraded, the sudden obligation to post a large amount of collateral may prove too much for it to handle, some say.

"Downgrade clauses sound good," Mr. Berger said, "but if everybody has one, it doesn't help them that much."

The security demands unquestionably create new headaches for reinsurers, analysts and reinsurance sources agree.

Reinsurers' costs will be driven up by the need to post LOCs, Mr. DeRose noted. Alternatively, if a reinsurer puts funds in trust as security, its investment returns will suffer, because it would likely invest the money in more conservative, lower-yielding instruments.

Downgrade clauses that allow ceding insurers to commute their contracts also could mean significant lost business for affected reinsurers, he added.

"It's an additional cost, it ties up capital and reduces flexibility," observed Mike Hayes, CEO of Alea North America Reinsurance Division in Wilton, Conn.

The extent to which the security provisions will catch on remains uncertain, though some expect them to become more common.

"You're going to see more and more of them," Mr. Berger predicted, adding that the trend will favor the strongest reinsurers. "The smaller, less well-rated companies will really suffer."

Some observers claim the provisions are not new, though. Patrick J. Denzer, president and chief operating officer of reinsurance intermediary John B. Collins Associates in Minneapolis, said his firm's contracts have had standard termination wording in the event of a downgrade, the loss of a certain percentage of surplus, or runoff. "We allow our clients to terminate their position retroactive to inception" of the contract, he said.

"We've probably been a little more forceful in how we advise our clients to apply those clauses, but we've been doing that probably two or three years, I'd say. I think it's getting a little more press, lately, for obvious reasons," said Mr. Denzer.

Guy Carpenter's Mr. Priebe said the intermediary has "historically had provisions in our reinsurance contracts in many cases which gave the client the opportunity to either commute or cancel a reinsurer's position in the event of a change in their financial status, be it a rating downgrade or reduction in capital below a certain threshold, so that's

See REINSURANCE/page 30

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BI 07-07-03 A 28,30 7/2/03 1:19 PM Page 2



# Reinsurance: Ceding insurers ask for more security

Continued from page 28

something that's always been there."

David Cameron, senior vp at reinsurance intermediary Benfield Blanch in Minneapolis, said, "That's been a push for a while for Benfield, both in termination as well as funding clauses, for a couple of years now," although "there's probably been some contracts that had them added this past renewal season."

Others say they have not seen increased evidence of downgrade clauses.

"I'm not seeing a massive rush to that," said Steven Bolland, senior vp at reinsurance intermediary Gill & Roeser in New York. "Obviously, reinsurers don't want it. If you have a large program with a number of reinsurers in it, it would get very clumsy. I haven't seen that as being a big issue."

"We haven't run into that," but that may reflect the reinsurers with which Dallas-based EWI Re deals, said Patrick J. Stangle, its president and chief executive officer.

However, he added, security "is probably one of the most prominent issues in the reinsurance industry," he said. "Ceding companies are being much more selective as to whom they're dealing with. I think that's the key. You have to seriously look at the reinsurers you're dealing with, and I think more ceding companies are being a lot more selective," said Mr. Stangle.

Others agreed the number of reinsurers with which insurers will do business has decreased.

Richard DiClemente, president of New York-based THB Intermediaries Inc., said certain insurers "have begun to restrict the number of reinsurers they're dealing with. Reinsurers that drop below A are being summarily removed from lists, and there's much more concern…about security, and the result of that is a smaller approved list of reinsurers for the major buyers.

"It's also much more difficult to get new markets approved, since a lot of carriers are now taking a larger net positions on account and keeping more risk in house, so there's been some reduction" in reinsurance purchasing because of that as well, said Mr. DiClemente.

Gill & Roeser's Mr. Bolland noted that although there are fewer reinsurers to begin with because of consolidation, "there are a few of the smaller, weaker reinsurers who are going to get squeezed, particularly on the casualty side, where people recognize that you pay the premium today and the payout could be over 15, 20 years or more, and, therefore, compromising on security when you go out 20 years is a big gamble."

Guy Carpenter's Mr. Priebe said there has been a five-year trend toward shortening approved lists of reinsurers on the liability side. Over the past six to 12 months, several reinsurers "have now fallen off those so-called approved lists" in a reflection of the "financial challenges" many have gone through over the past two years, he said.

Mr. Denzer said, "I think that there is a continued flight to quality, that more and more companies are cognizant of the quality of their security and willing to pay maybe a little bit higher price for security."

Apart from the debate over reinsurer security, the midyear renewal season has offered few surprises.

Noncatastrophe property treaty business is seeing modest single-digit price increases, while the "catastrophe market seems to be leveling off around the world," in part because of the influx of new capital devoted to cat risks, said Rick Smith, president and CEO of global property and casualty reinsurance at Overland Park, Kan.-based Employers Reinsurance Corp.

Facultative property placements may be somewhat tougher: American Re-Insurance Corp. is getting an average increase of about 20% on its business, where loss experience tends to be more volatile than in the general run of property treaty, according to Kevin Davidson, president of the reinsurer's direct facultative unit.

The casualty market remains tighter than property, with reinsurers enjoying double-digit price increases even for run-of-the-mill general liability business as they become much choosier about the risks they take on.

Employers Re, for example, has stopped writing pharmaceutical risks and is "extremely selective" in writing national account umbrella, directors and officers liability and professional liability business, Mr. Smith said.

"In general terms, the casualty market has, from a reinsurance perspective, improved year over year from" last July 1, said Peter Zaffino, managing director at Guy Carpenter. "While reinsurers are still monitoring aggregates very closely, there seems to be a little more aggregate available this 7/1" compared with last year.

"General terms and conditions, meaning ceding commissions, are not as stringent as they were last year," said Mr. Zaffino. Having said, that, however, certain segments—including directors and officers liability, errors and omissions, large accounts, lawyers and coverage for large financial institutions—are "still getting hard-market rates and in some cases still experiencing some rate increases," said Mr. Zaffino.

# Surgery raising cost of health care

By KATIE MERX

Demand for procedures that make life easier is rapidly increasing the cost of health care, according to executives at Blue Cross & Blue Shield of Michigan.

Among the most expensive procedures for the Blues plan are the increasingly popular joint and cardiac-valve replacements, major chest surgeries and stomach reductions.

"A lot of what's driving health care costs is a pull rather than a push, because people want to have joint replacements when they can't get around...and their mobility and lifestyle (are) affected," said Dr. Thomas Simmer.

"So many people are getting joint replacements who didn't before," said Dr. Simmer, vp of medical affairs and corporate medical director at the Michigan Blues. "Why? Partly because the joints have gotten so much better."

And because bariatric surgery can be done less invasively, more people are choosing it as well, he said.

The Blues' cost per member for bariatric surgery, which reduces the working capacity of obese patients' stomachs, rose 23.4% in 2002 from 2001, said Michael Connor, director of the Blues' Center for Health Care Quality and Evaluative Studies. The average cost to the Blues for the procedure ranges from $12,000 to $17,000, he said.

The problem, Dr. Simmer said, is that increasing use of those procedures is increasing costs.

The cost per Blues patient for inpatient hospitalization rose 6.4% in 2002 from 2001. And surgical procedures accounted for 45 percent of that increase, Mr. Connor said.

The most costly of those procedures were bariatric surgery, hip and knee replacements, cardiac valve/cardiac defibrillator implants and major chest procedures, Mr. Connor said. Those procedures accounted for 52% of the increase in the Blues' surgical costs last year. Mr. Connor described major chest procedures as noncardiac surgeries to do such things as remove growths from the lungs or treat esophageal cancers.

The average cost to Blue Cross for a hip or knee replacement is $10,650; a cardiac valve or defibrillator implant is $34,300; and for a major chest procedure is $14,550, Mr. Connor reported.

"I remember when I was in training, cataract surgery was a big deal. You had to have all sorts of indications for it. Now, my 90-year-old dad gets a cataract removal so that he can see the golf ball better," Dr. Simmer said. "None of us would argue with it if it (was) our eyes."

The medical community, thanks to new technology, is able to offer people a lot more than it used to, Dr. Simmer said.

"We need to make an adjustment toward understanding that as we age and as we want these things, they cost money and I think we have to be prepared to pay for them," Dr. Simmer said.

But because the new technologies are so expensive, there also is a need to have processes in place to more effectively eliminate waste from the system.

One of the things the Blues is doing is continually evaluating ways to improve quality, cut cost and eliminate unnecessary procedures, Mr. Connor said.

For example, the insurance company is considering creating a network of Blues providers who are approved to do bariatric surgery to cut costs and improve quality.

*Katie Merx is a reporter for Crain's Detroit Business, a sister publication of Business Insurance.*

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MH 07-07-03 A 32 7/2/03 4:13 PM Page 1



# Pension plan sponsors vocal on benchmark proposal

By VINEETA ANAND

**WASHINGTON**—Corporate America is waging a lobbying campaign to avert a Treasury Department proposal that could require many of the nation's top companies to report higher pension liabilities and shovel more money into their pension plans.

The Treasury Department, which has informally discussed its views with lawmakers, is expected to present a formal legislative proposal to Capitol Hill early next week.

Organizations representing employers have enlisted chief executive officers of some of the nation's largest corporations to lobby Treasury Secretary John Snow and the White House directly. They also will present their case to key lawmakers on Capitol Hill, many of whom are openly sympathetic toward them.

By lining up legislators on their side, corporate executives hope the Bush administration will back off its proposal, rather than risk the embarrassment of receiving a cool reaction on Capitol Hill.

The high-stakes fight between employers and the Bush administration is over a permanent replacement for the 30-year Treasury bond as the benchmark for calculating pension fund contributions, lump-sum payments and variable insurance premiums for the Pension Benefit Guaranty Corp.

"Plan sponsors may have to roll Treasury on this," said Brian H. Graff, executive director of the American Society of Pension Actuaries, Arlington, Va., who is lobbying against the Treasury's position. "Once the Treasury side comes out, it's going to throw a wrench in the entire process."

## Lawmakers sympathetic

"There is a lot of sympathy in most of the offices (of lawmakers) we have talked to," added Janice Gregory, vp of the ERISA Industry Committee. She has been accompanying corporate executives on rounds at Capitol Hill.

And James M. Delaplane Jr., partner at the Washington law firm of Davis & Harman, who represents the American Benefits Council, said companies are seriously considering freezing their pension plans. The council, which represents many of the nation's largest plan sponsors, last week urged its members to enroll their CEOs in this fight.

"We understand that there has not been sufficient CEO-level input to Treasury Secretary John Snow…and such input must be received as soon as possible in order for it to be effective," an ABC memo to members urged.

A Treasury spokeswoman declined to comment on the proposal.

While corporations favor a benchmark linked to the four-year weighted average of high-grade corporate bonds, the Bush administration is considering requiring employers to use a range of interest rates, linked to the demographics of their work force and the timing of their benefit payments.

## Demographic idea favored

Thus, manufacturing and old-economy companies with older workers and large numbers of retirees would have to use a lower interest rate to match the shorter duration of their benefit payments than companies that may not have to pay out pensions for years into the future.

This approach also is favored by Steven Kandarian, executive director of the PBGC, which provides insurance to workers when financially weak companies walk away from their pension obligations.

It is also backed by academics and some pension consultants who say a one-size-fits-all approach subsidizes weak companies with underfunded pension plans at the expense of financially stronger companies.

"If a company can't afford to pay its employees' salaries, we don't require other companies to chip in. The same standard should apply to a company that provides part of its employees' pay in the form of pensions," said Lawrence Bader, a retired actuary and previously a consultant with William M. Mercer Inc. in New York.

Mr. Bader has written extensively on the subject, including a paper that apparently influenced the Treasury Department officials. Concurring with Mr. Bader are Zvi Bodie, a professor of finance at Boston University; Jeremy Gold, a New York-based independent actuary; and Michael Peskin, principal in the global pensions group of Morgan Stanley in New York.

But plan sponsors reject that approach, noting that it could spell the death of defined benefit plans. Those already facing the biggest shortfalls would have to calculate pension obligations at the short end of the yield curve.

Lawmakers in the Senate and the House apparently agree with employers.

In May, Sen. Judd Gregg, R-N.H., chairman of the Senate Health, Education, Labor and Pensions Committee, attempted to insert an amendment into the economic stimulus tax package that would substitute high-grade corporate bonds for the 30-year Treasury as the benchmark for five years, starting in 2004. The amendment was dropped from the version that President Bush signed.

A month earlier, a broad pension package was introduced by Reps. Rob Portman, R-Ohio, and Ben Cardin, D-Md., that calls for a new benchmark based on the four-year average of high-grade corporate bonds.

## Backing of unions

Lobbyists say Rep. John Boehner, R-Ohio, chairman of the House Education and the Workforce Committee, supports that position. A legislative aide to Rep. Boehner did not return calls seeking comment.

Pension executives say their case is strengthened by the backing of labor unions, which use pensions as a bargaining chip in contract negotiations and frequently accept higher retirement benefits in lieu of pay raises.

William Samuel, director of the AFL-CIO's legislation department, wrote in a May 9 letter to Rep. William Thomas, R-Calif., chairman of the House Ways and Means Committee, that the labor organization supports the benchmark proposed in the Portman-Cardin legislation, albeit with a small adjustment.

Rep. Thomas, who apparently urged Mr. Snow to present the Bush administration's formal legislative proposal in a recent meeting, is contemplating attaching the Portman-Cardin provision in an international tax bill under consideration. A legislative aide declined to comment.

But some key legislators are still holdouts. Among them are Sen. Chuck Grassley, R-Iowa, the outspoken chairman of the powerful Senate Finance Committee, and Sen. Max Baucus, D-Mont., the ranking Democrat on the committee who generally agrees with Sen. Grassley on pension issues. Sen. Grassley is said to favor the administration's approach of requiring employers to base liabilities on a range of interest rates along a yield curve of corporate bonds. A legislative aide to Sen. Baucus did not return calls.

Liabilities rise when interest rates fall, and employers have seen their pension liabilities soar because of the steep decline in the benchmark Treasury security since the late 1990s; the situation was exacerbated by the administration's plans to stop issuing the 30-year Treasury bond in October 2001, employers say. A temporary change in the law that permitted companies to use a higher interest rate expires at the end of the year.

"I understand there have been CEOs lining into place like a row of ants" outside the offices of senior administration officials, said one source, who did not wish to be identified.

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

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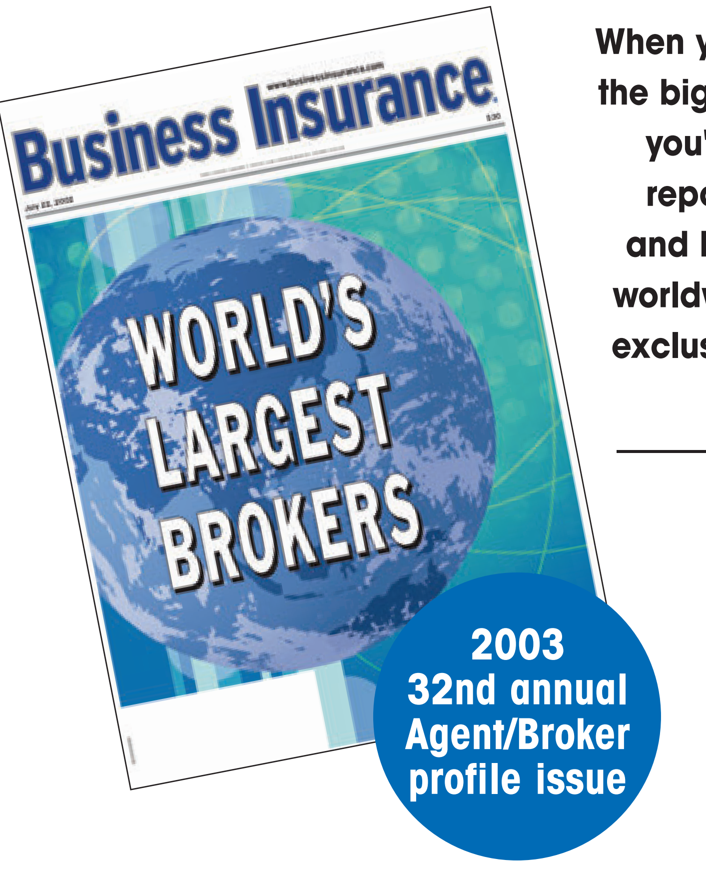


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MH 07-07-03 A 34 7/2/03 4:25 PM Page 1



# Lawsuits: Common mistakes

Continued from page 4

work environment lawsuit that "is next to impossible to defend," he said.

To counter this possibility, employers should create a strict policy that e-mail and Internet usage are subject to monitoring and that use of the system to harass other employees or view pornographic material will not be tolerated.

Another problem is created when employers terminate an employee for engaging in a legally protected action. Such activity includes filing a discrimination claim, filing a whistleblower suit or engaging in a union organizing activity, he said.

"There are probably 50 ways to participate in protected activity," Mr. Naughton said.

Employees participating in such activity are generally shielded from termination or other adverse employment action absent some egregious conduct, he said. But often employees are terminated anyway, leading to suits that are hard to defend against, he said.

A different problem occurs when employers mischaracterize employees as salaried and therefore exempt from federal overtime laws, Mr. Naughton said.

While the line separating exempt from nonexempt employees is fuzzy, the rule to guide employers should be the employees' duties and not their education or job title. In particular, if an employee manages two or more other people or is a professional, that employee is exempt, he said.

"It isn't the job title, it's what they do," he said.

A lawsuit brought by one employee for unpaid overtime usually does not result in a large award. But if there are many similarly treated employees, that lawsuit can become a class action that costs an employer millions of dollars, Mr. Naughton said.

Employers also get in trouble mishandling workplace harassment complaints, he said. A key step in limiting harassment liability is having a written policy and complaint procedure that is distributed to all employees so they know how to file a complaint, he said.

> **'When you fire without management review, without human resources review, you're in trouble.'**
>
> *James Naughton*
> *Hunton & Williams*

In addition, employers need to train supervisors in how to spot and report a harassment situation. Often, Mr. Naughton said he sees supervisors attempting to force employees to withdraw a complaint rather than to pass the complaint along to the proper investigative authority.

"It's crazy if you have supervisors trying to talk employees out of complaints," he said.

With discrimination suits, employers also get in trouble if they punish the victim. This often occurs, he explained, when the complaining employee is transferred to another department or shift, or prevented from working overtime in order to minimize contact with the accused. Unless the victim provides written consent, these changes can be seen as punishment for filing a complaint, adding to the employer's legal troubles, he said.

Employers also create their own problems when a supervisor terminates an employee out of anger.

"When you fire without management review, without human resources review, you're in trouble," he said.

A safer course for employers is to document any performance problems by employees. And supervisors must be told to follow all termination policies, including rules for progressive discipline. A termination should also occur only after a thorough investigation, he said.

"Never fire someone without getting the employees' side of the story," he said.

Finally, employers get in real trouble when a supervisor has an affair with a lower-ranking employee, he said.

While most people realize these affairs create problems, managers still engage in them. When the relationships break up, it sometimes turns messy with the employee accusing the supervisor of requiring sex in exchange for keeping the job.

To avoid this, Mr. Naughton recommends that employers prohibit supervisors from dating their subordinates.

# Employee Benefits Communication Awards July 28 deadline for entries approaching

The deadline is nearing for the 31st annual Employee Benefits Communication Awards.

*Business Insurance* launched the EBC Awards in 1972 to address concerns about the need for better communication on complex benefit issues between employers and employees. The awards acknowledge excellence in communicating employee benefit programs.

All companies in the United States and Canada are eligible to enter their own communication programs in the EBC competition. Benefit consulting firms also are invited to submit programs on behalf of their clients.

The deadline for *Business Insurance* to receive entries is July 28, 2003.

Best of Show awards will be given in the six categories. Awards of Excellence may also be presented in each category.

Winners will be announced in the Dec. 8 issue of *Business Insurance*.

For more information on the EBC Awards, including an entry form and complete rules of the competition, please visit *BI*'s Datebook department online at *www.businessinsurance.com* or call Barbara O'Brien, promotion coordinator, at 212-210-0229.

# New approach urged for employee benefits

## Consider company goals: Consultant

By MICHAEL PRINCE

**ORLANDO, Fla.**—Employers need to develop a strategic approach to providing employee benefits, examining each offering to determine whether it advances the company's larger goals, a benefit consultant says.

Replacing an ad hoc approach with a strategic one allows corporate benefit professionals to better direct their organization's benefits program, said Gary Kushner, president of Kushner & Co. Inc. in Portage, Mich.

Currently, a strategic approach is most urgently needed to hold down double-digit health care costs increases, he said. Such costs are expected to rise next year as rapidly as they did this year, he said. But a strategy that slows cost increases by even a few percentage points can bring significant savings, Mr. Kushner said at a session during the 55th annual conference of the Society for Human Resource Management, held last month in Orlando, Fla.

He said health care costs currently average about $5,000 per employee per year. If costs were to rise by 20% each year, they would reach about $12,400 per employee by 2008.

But if increases were held to 7% per year, per employee costs would average only about $7,000 in 2008, he said. For an organization with 1,000 employees, that amounts to savings of $5.4 million in 2008, he said.

"We're beginning to talk of real dollars," he said.

In response to this environment, employers need to assess each of their offerings with an eye toward what role it plays in the organization's larger benefits strategy, he said.

In addition, plan-design changes should be evaluated in terms of both the benefits strategy and the long-term implications of the changes, Mr. Kushner said. Too often, plan-design changes are made for short-term goals, he said, and organizations fail to establish a plan design that can work for years to come.

"Have a game plan in place with what you want to do over a long period of time," Mr. Kushner said.

Mr. Kushner said that some employers, in adopting a benefits strategy, are beginning to question certain conventional approaches to offering benefits. For example, some are evaluating whether health plans should provide first-dollar coverage, he said. Many employers are now reconsidering that structure, which became common in the 1980s. In many cases, they are moving away from first-dollar coverage and replacing it with a high-deductible plan that provides employees with protection from catastrophic losses.

Employers are also putting greater emphasis on buying the best—rather than the cheapest—health care, he said. As part of this, they are making available to employees information on the quality of doctors and hospitals to help them select the best providers. The strategic goal is that higher quality care will lower health care spending in the long run, he said.

In addition, he noted that a company must provide information to its employees about its benefits strategy. Such education, he said, is often spotty, with companies providing information on benefits just once a year, at open enrollment. Fostering employee understanding of the strategy—and their role in it—should be a year-round educational effort, he said.

# 15,000 attend conference

**ORLANDO, Fla.**–Nearly 15,000 people descended on Orlando, Fla., last month to attend the 55th annual conference of the Society for Human Resource Management.

Besides soaking up the Florida warmth, attendees strolled the meeting's vast exhibit hall, which featured more than 800 exhibitors, and saw presentations from former U.S. Secretary of State Madeline Albright and business authors Jim Collins and Tom Morris.

Next year's SHRM conference will be held in New Orleans on June 27-30, 2004.

For more information, visit *www.shrm.org*.

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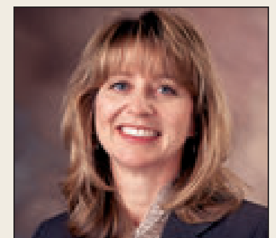
MH 07-07-03 A 36 7/2/03 4:25 PM Page 1



# Between the Lines



*Compiled by Joanne Wojcik*

## Risk manager lends a helping hand

Pima County, Ariz., Risk Manager Dave Parker became a pro bono public adjuster following recent fires that destroyed about 320 homes and eight businesses in the Mount Lemmon communities of Summerhaven and Loma Linda near Tucson, Ariz.

PHOTO: REUTERS

Although the county's losses were limited to a $200,000 transportation department building and a $50,000 restroom complex, Mr. Parker photographed the remaining fire-damaged dwellings and foundations so the owners could document their losses for insurance purposes.

Because few address markers in the remote areas survived, identifying individual properties was difficult, he said. In addition, the local water department had lost records in the blaze. But a longtime employee with a good memory helped piece the information together, Mr. Parker said.

"My satisfaction comes from the fact that homeowners now know whether or not their homes still exist," he said. "That provides a sense of finality for them."

## Haunting irony

A concert tour by 1980s metal band Great White to raise money for families of victims of the Station nightclub fire in West Warwick, R.I., has been called off due to lack of insurance.

Proceeds from the 55-city tour would have gone to the nonprofit Station Family Fund, established to assist the families and survivors of the February fire, which claimed 100 lives after a Great White pyrotechnics display went awry and set the club ablaze. The tour was to begin early last month.

"We had massive insurance problems," said Great White's manager, Charrie Foglio. Insurers were more concerned about the prospect of an angry audience than they were with covering the band's risks, he said. No pyrotechnics were planned for the tour.

PHOTO: PHOTOGRAPHERS SHOWCASE

**Jack Russell, lead singer of Great White**

## Liability for 'acts of God'?

A judge in Kochi, Japan, has rejected a family's claim that organizers of a high school soccer match in 1996 should be held liable for serious injuries sustained by a player who was struck by lightning during the game. Judge Hiromi Kameda rejected the family's claim, saying it was impossible to predict where lightning would strike.

The player, who lost his sight and became paralyzed after he was struck by lightning, and his parents were seeking 300 million yen ($2.5 million) in damages from Tosa Senior High School and the Takatsuki Amateur Sports Assn., saying they should have canceled the match after Japan's Meteorological Agency issued a warning that lightning might strike the area.

## She looked dead to me, your honor

A former governor of the Philippines' Quezon Province has been charged with insurance fraud in California for allegedly filing false life insurance claims, state insurance regulators report.

Former Northridge resident Eduardo Rodriguez had been a fugitive since 1985 when the Los Angeles County District Attorney's Office charged him with collecting on policies covering his wife and mother-in-law, who both were alive at the time. He was brought back to the United States from the Philippines last month by the U.S. Deputy Marshals Office.

Efforts are under way to extradite Mr. Rodriguez's wife, Imelda Rodriguez, to the United States where she will be charged with one count of insurance fraud for her involvement in the scam.

*Tips and feedback from readers are welcomed. Please send information to jwojcik@crain.com.*

# Products & Services

## Disaster recovery classes now available online

**FALLS CHURCH, Va.**—DRI International is offering its entry-level business continuity training courses online.

DRI, formerly known as the Disaster Recovery Institute, provides coursework to risk managers and others who are seeking the Certified Business Continuity Professional designation. By making the courses available through the Internet, Falls Church, Va.-based DRI is able to reach participants who are not close to areas where onsite instruction is available.

Three courses are the first to be offered online, with up to 10 available through the Internet by fall.

DRI said the courses are in demand partly because the Sarbanes-Oxley Act places greater responsibility on corporate management to demonstrate proper recordkeeping and documentation on business continuity.

More information on DRI's offerings is available at *www.drii.org*.

## RRG offers coverage to propane companies

**RICHMOND, Texas**—Jamestown Insurance Co., a newly formed risk retention group, is offering property/casualty coverages to propane gas companies.

The Richmond, Texas-based insurer provides comprehensive general liability, automobile liability, excess umbrella, property and other coverages.

More information on coverage and available limits is available from Paul Brewer, president of Jamestown, at 800-869-6208.

## Mold claims guide to be published

**BLAINE, Wash.**—A new book, "Mold: A Comprehensive Claims Guide," will be published by Specialty Technical Publishers this month.

The book, written by insurer attorney and consultant Barry Zalma, is a claims guide for property owners and managers, inspection companies, insurers, brokers and others in property-related professions. It contains information on identifying and protecting against mold as well as discussions of understanding mold insurance, presenting claims, investigating claims and other topics.

The book costs $380 and includes quarterly updates. Orders or requests for a 30-day trial preview should be directed to Julie Farrell, Specialty Technical Publishers, 800-251-0381.

## MetLife enhances AD&D product

**NEW YORK**—Metropolitan Life Insurance Co. has enhanced its accidental death and dismemberment product for employees.

New features of the AD&D product include increased benefits for a worker's spouse or children to allow them to continue their education. The coverage also pays an increased amount for child care services when a covered employee is killed in an accident.

The product has been enhanced to pay an additional 100% of the amount of coverage if an employee dies from a work-related accident, and additional benefits are available if the worker or a dependent dies while traveling in a passenger vehicle. Prescribed therapeutic counseling and rehabilitative physical therapy also are covered, as are injuries that result in brain damage, coma or third-degree burns.

More information is available from MetLife at 212-578-2211.

## Tennessee Blues offers new options

**CHATTANOOGA, Tenn.**—BlueCross BlueShield of Tennessee is offering employers two new health care plans.

Tennessee employers can choose the insurer's ValuePak or MultiPak health coverage options.

The ValuePak plan offers employers low-cost prepackaged benefit plans that include life insurance, dental coverage and prescription drug coverage. The MultiPak plan provides employers with a choice of prepackaged multiplan options that are made up of some of the insurer's most popular plans.

The multiplan approach allows employers to provide workers with a choice of benefit option levels and can be structured to offer a choice of health plans as well.

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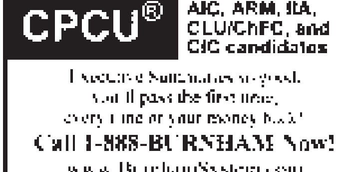


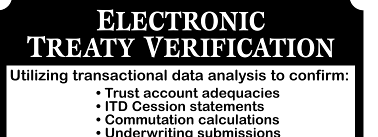


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BI 07-07-03 A 37 7/3/03 3:13 PM Page 1



# Australian regulators charge Adler, others

**SYDNEY, Australia**—Australian authorities have charged Rodney Adler, the former head of FAI Insurance Ltd. and a director of HIH Insurance Ltd., with stock market manipulation and making false statements about HIH shares.

The charges, brought by the Australian Securities and Investments Commission, stem from the 2001 collapse of HIH. The demise of HIH, which had been Australia's second-largest property/casualty insurer, was the country's largest corporate failure (*BI*, March 26, 2001).

The case has been adjourned until November.

Meanwhile, three former executives of FAI appeared in court earlier this week over ASIC charges that they failed to act honestly with regard to reinsurance arrangements FAI entered into with General Cologne Re Australia Ltd. in 1998. HIH's 1999 takeover of FAI, which eventually became insolvent, has been cited as part of the reason for HIH's unraveling.

ASIC charges that "the true substance of those (reinsurance) arrangements was concealed from FAI's auditors" and that they involved no actual risk transfer.

Daniel Wilkie, former chief operating officer of FAI General Insurance Co. Ltd., was charged with two counts of failing to act honestly in the exercise of his powers and discharge of his duties as an officer of the company, and one count of providing false and misleading information.

Timothy Mainprize, former finance director of FAI, faces the same charges.

Stephen Burroughs, FAI's former reinsurance manager, was charged with one count of failing to act honestly in the exercise of his powers and discharge of his duties as an officer of FAI.

The three men were asked not to enter pleas and will reappear in court in September.

In a separate move, the Australian Treasury Department announced it would create a special unit within the Commonwealth Director of Public Prosecutions dedicated to prosecutions and legal proceedings relating to the collapse of HIH. The CDPP will receive an extra $14 million Australian ($9.5 million) in funding over the next three years to investigate claims against those implicated in the collapse of the insurer.

A Royal Commission inquiry earlier this year blamed HIH's demise on mismanagement that left it unprepared for future claims (*BI*, April 21).

In another development, HIH's liquidators announced an agreement in principle with Bradley Cooper, a former shareholder of HIH, over a disputed $1.4 million Australian ($2.1 million) loan made in 1999 by FAI to a company run by Mr. Cooper. Under the terms of the confidential settlement, Mr. Cooper will make a "significant payment,"said HIH liquidators Tony McGrath and Alex Macintosh of KPMG Sydney.

*—By Sarah Veysey*

PHOTO: NEWSPIX

**Rodney Adler, former head of FAI Insurance Ltd., was among execs charged by Australian securities regulators.**

## Insurers cite reinsurer withdrawal of coverage

# U.K. asbestos exclusions likely to spread

**By CAROLYN ALDRED**

**LONDON**—Recent moves by some U.K. public liability insurers have risk managers concerned that they may soon find it difficult to obtain coverage for asbestos liabilities.

Compounding buyers' worries are new asbestos liability reporting rules that take effect in the United Kingdom next year (see related story), which could make a coverage shortage even more trying for companies with such exposures.

In recent months, some insurers have been forced to exclude asbestos from public liability policies, which cover organizations for property damage and bodily injuries suffered by individuals other than their employees, according to a spokesman for the Assn. of British Insurers. Those exclusions were prompted by a withdrawal of asbestos coverage by reinsurers, he explained.

One major insurer that excluded the coverage—but then reversed its position—is AXA Insurance U.K. P.L.C. The London-based insurer last week did an about-face and pledged to provide asbestos liability coverage after initially excluding it from all July 1 renewals. Meanwhile, other insurers are reviewing their position, and risk managers should expect asbestos exclusions to increase, underwriters and brokers say.

The U.K. insurers' move is in response to the introduction of asbestos exclusions by reinsurers on a worldwide basis.

"It is only a matter of time before the market tightens up. No insurance company can continue to offer open cover without reinsurance protection. It is a recipe for disaster. As insurers, protection of our solvency must be the No. 1 priority," said Steve Browne, AXA's U.K. casualty manager.

As part of an effort to reduce future asbestos liabilities, Munich Reinsurance Co., Swiss Reinsurance

See **EXCLUSIONS/page 39**

**Assn. of Local Authority Risk Managers conference**

# New rules to boost asbestos exposures

**By NEIL HODGE**

**MANCHESTER, England**—Local government authorities could face prosecution and unlimited fines if they fail to comply with new regulations that will require them to locate and manage any trace of asbestos in owned premises, an insurer warns.

The Control of Asbestos at Work Regulations 2002, which take effect in May 2004, will impose new duties on landlords of nondomestic properties, which includes office buildings, schools and hospitals, to manage the risk of asbestos exposure. Because local authorities are one of the largest owners of asbestos-contaminated properties in the United Kingdom, they also face one the largest exposures under the law.

"There is every possibility that asbestos will become the biggest financial risk to local authorities once the new regulations come into force next year," said Alan Hunter, technical claims manager at the Aldershot, England, office of Zurich Municipal, unit of Zurich Financial Services Group.

"The amount of property that local authorities have in their charge is enormous and the process of simply reviewing each one for asbestos and writing a report on it—even before any removal work is carried out—could easily make a serious dent in any council's budget," he said at a session during the Assn. of Local Authority Risk Managers' annual conference in Manchester, England, last month.

Currently, all U.K. employers have a duty to prevent asbestos exposure to employees and where this is not possible, to reduce exposure to the lowest level, Mr. Hunter noted.

But he said the new regulations will place an additional duty on U.K. property owners to proactively manage asbestos in their buildings by determining if there is asbestos on the premises, how much there is and what condition it is in. Landlords also must presume that certain building materials contain asbestos unless there is strong evidence that they do not.

The regulations also will require landlords to develop and keep an up-to-date asbestos register that gives the location of any asbestos-containing materials in their properties. Landlords must prepare an plan detailing how they will manage the material and its associated risks—which should be regularly reviewed and monitored—as well as providing information on the location and condition of the material to anyone who is liable to perform work that could disturb it.

The cost of reviewing owned premises—not to mention the expense of performing asbestos remediation work—could be "astronomical," said Mr. Hunter, who said the regulations are "essentially unworkable."

Many local authority risk managers at the meeting admitted they

See **ASBESTOS/next page**

# World Updates

## Revised risk standard proposed Down Under

A joint committee working to develop a revised risk management standard for Australia and New Zealand has circulated a draft for public comment. A final version by the Standards Australia/Standards New Zealand Joint Technical Committee on Risk Management is expected to be published in early 2004. The project, which aims to establish a framework for companies to implement a risk management process, outlines procedures for identifying and analyzing risks. An earlier risk management standard, AS/NZS 4360, was developed in 1995. The revised standard can be viewed at *http://www.airm.org.au/index.cfm?L1=1&L2=4&Item=245*

## Mapfre to expand nonlife business

Spanish insurer Corporacion Mapfre is buying the nonlife insurance operations of Musini Sociedad Anonima de Seguros y Reasseguros for 208 million euros ($239.2 million). Mapfre Caja Madrid Holding, a joint venture between Mapfre and Spanish bank Caja Madrid, won the bidding war for the nonlife operations of Musini, which was a state-run insurer. Madrid-based Musini had a nonlife premium volume of about 333 million euros ($383.0 million) in 2002.

## Markel boosts capital of London unit

Markel Corp. has given a $45 million capital boost to its London unit, Markel International Insurance Co. Ltd., bringing the insurer's capital base to more than $200 million, a spokesman said. A.M. Best Co. has upgraded Markel's rating to A- from B++.

## Challenges lie ahead for Lloyd's, report says

Lloyd's of London faces challenges as it implements proposals designed to modernize the market, according to a report by the reinsurance arm of Willis Group Ltd. In its report, "Lloyd's Review 2003," Willis Re says that a key challenge for the newly created Franchise Performance Directorate will be to monitor the results of poorly performing syndicates and to raise the standards of those syndicates. Willis Re's report notes that the number of syndicates operating at Lloyd's market fell to 71 at the start of 2003 from 86 in 2002. Meanwhile, the number of syndicate managing agents in the marketplace dropped to 43 from 50. In 2003, 87% of the Lloyd's market's record £14.4 billion ($23.74 billion) capacity is provided by corporate backers, up from 86% in 2002, the report notes.

BI 07-07-03 A 38 7/3/03 3:13 PM Page 1



# Asbestos: New duties seen from U.K. rule

Continued from previous page

were unaware of the new regulations and have done little—if anything—to ensure they will be in compliance with the new rules. In a straw poll of attendees, only a handful indicated that they had begun to examine the associated risks and implement the necessary procedures.

Mr. Hunter said "local authorities are going to have to plan very carefully how they deal with the financial, health and human resources risks associated with locating and detailing all the asbestos throughout all their premises."

He also warned that the new regulations could spur claims against local authorities for failing to notify people who come into contact with asbestos in authority-owned properties.

"Councils will need to make sure that their risk management and information sharing processes are thorough enough to ensure that people like plumbers, decorators, construction workers and electricians know that they are working in areas containing asbestos," he said.

"It is uncertain whether the new regulations require local authorities to ensure that contract workers wear the appropriate protective gear to reduce their exposure to asbestos and whether authorities need to provide it at their own cost," he added.

As a result of the new regulations, Mr. Hunter said that it is likely that liability insurers "are going to want to reduce their exposure to asbestos-related claims" and may even "cap their liability in any policies they write" so that "local authorities take on a greater degree of risk themselves."

Aidan Thomson, partner in the environmental group at law firm Barlow Lyde & Gilbert in London, said that one of the biggest concerns for local authorities will come from internal sources, rather than external ones, like contractors.

Local authorities could face employee "backlash" once they "are told that the building they have been working in for the past 20 years is full of asbestos," he said.

Mr. Thomson said this could result in a large increase in the number of stress claims from employees. "It is not unsurprising that the word 'asbestos' causes people to panic and when employees realize that they may have been exposed to the substance for a long period, absence due to stress could very well increase," he said.

Assn. of Local Authority Risk Managers conference

# Public sector market tough

By NEIL HODGE

**MANCHESTER, England**—The public sector insurance market is dominated by a handful of insurers, and rates are unlikely to decrease anytime soon regardless of risk mitigation efforts, say local authority risk managers.

Although brokers often advise public and private organizations to highlight their internal control and risk management actions to insurers to obtain lower premiums, insurers seldom reward public sector risk managers for their risk mitigation efforts, they say.

Their efforts are stymied by a "monopolistic" market and a belief by insurers that internal control in local authorities lags behind that in the private sector.

Speaking at the Assn. of Local Authority Risk Managers' annual conference in Manchester last week, Robin Powell, corporate risk manager for the Sandwell, England, Metropolitan Borough Council, said that for some local authorities there is little reason to demonstrate their understanding of risk management because "councils need to purchase cover from the same provider anyway due to a lack of competition in the market."

"It is coming to the point that there are currently so few players in the public sector insurance market—and there is even speculation that some of these players are unhappy taking on more public sector work than they already cater for—that insurers can charge local authorities whatever they like for cover," said Mr. Powell.

ALARM MANAGING RISK

"The insurance market is a virtual monopoly, and bearing that in mind, the idea that demonstrating to your broker that you have a good controls environment in place to reduce premiums becomes wishful thinking," he added.

According to local authority risk managers, insurers are afraid of increasing their exposure to emerging public sector risks, such as compliance with the Control of Asbestos at Work regulations that take effect in May 2004. Those regulations require all landlords of nondomestic properties to conduct a review to monitor the amount of asbestos-containing material that is present in the buildings they own.

But brokers say local authorities could obtain lower premiums if they took higher retentions.

"While local authority risk management and internal audit departments have improved their risk identification processes and how they prioritize risk, many still are not putting their risk management skills into practice, which means that insurance is still being used as a major risk management tool for small-scale or low-probability risks and that insurers are providing cover for too many risks on the register," said Simon Rowlinson, a consultant at Aon Risk Consulting in London.

"If local authorities are to cut their insurance costs, their risk management departments need to be more proactive about dealing with the risks themselves, rather than trying to pass any possible liabilities onto the insurer," he said.

Local authorities could also consider alternative risk transfer mechanisms if they are unhappy with the traditional market, said Bill Sulman, a director in the public sector practice at Heath Lambert Group in London.

"Local authorities are increasingly beginning to look at other funding arrangements as a way of cutting costs and achieving better cover, though different methods such as finite risk financing, using aggregate stops and paying claims direct from revenue streams pose other significant risks that need to be checked," said Mr. Sulman.


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BI 07-07-03 A 39 7/3/03 3:16 PM Page 1



# Exclusions: Reinsurers blamed

Continued from page 37

Co. and other reinsurers last year introduced asbestos exclusions into many non-U.S. public/product liability treaties beginning or renewing on Jan. 1, 2003. However, some insurers renewing in January, such as AXA, were provided with reinsurance protection for this exposure until July, when other insurers renew.

In the wake of the reinsurers' action, AXA notified brokers last month that primary policies renewing July 1 would contain asbestos exclusions. However, after AXA realized that other large primary insurers had not made similar moves, it reinstated the coverage, Mr. Browne confirmed.

"The market is still making its mind up, and we did not want to go it alone with a total exclusion," he said. But the insurer will closely watch the level of coverage provided under each policy and will be talking again with reinsurers, he added.

Mr. Browne said he doesn't know how long risk managers can expect insurers to provide such coverage, given reinsurers' stance and the increasing likelihood of asbestos claims.

Of particular concern are new rules, the Control of Asbestos at Work Regulations, due to take effect in 2004. Those regulations will require, among other things, that property owners monitor and manage asbestos found in their buildings.

"I believe we will see more asbestos litigation hitting public liability policies going forward, and no company, property owner or tenant can opt out of its responsibilities with the new asbestos regulations," said Mr. Browne.

Birmingham, England-based Zurich U.K. Commercial, a unit of Zurich Financial Services Group, said that it is not yet excluding asbestos exposures from its product and public liability policies but confirmed that it "is reviewing its policies as a result of reinsurance exclusions."

Aviva P.L.C. unit Norwich Union Insurance also is reviewing its public and product liability policies, which ultimately will likely reflect the outcome of its current negotiations with reinsurers, said Mark Hynes, London-based head of casualty underwriting.

Royal & SunAlliance Insurance Group P.L.C. has not introduced a total asbestos exclusion but has introduced policy wording that excludes all claims arising from a "fear of asbestos," said Phil Bell, technical insurances manager. He added that the insurer no longer underwrites any company with a known asbestos exposure.

Members of the London-based Assn. of Insurance & Risk Managers are "concerned about the introduction of exclusions and are closely monitoring the situation," said AIRMIC Executive Director David Gamble, noting that members are meeting this week to discuss the situation.

"From July 1, asbestos exclusions are likely to become more extensive and indiscriminate," said David Thomas, European environment practice leader at broker Willis Group Ltd. in London. "Clients are not happy—particularly in the U.K., which has new asbestos regulations."

Defense attorney David McIntosh, a senior partner of London law firm Davies Arnold Cooper who represents both insurers and policyholders, said that the government needs to make the issue of asbestos coverage a priority, as a lack of coverage will only increase the extreme pressures companies are under from rapidly increasing insurance costs and gaps in cover.

"This is not a cyclical issue. Asbestos is being excluded, and reinsurers will not start writing it again," he said, adding that "the government here is doing nothing about it, and it could have disastrous consequences for employers."

According to a report published by Willis earlier this year, "major reinsurers have been aiming to implement a total asbestos exclusion" internationally since the fall of 2002. Until now, asbestos exclusions in European, Australian and other international markets have been far less common than they are in the United States.

In addition, several reinsurers have indicated that asbestos exclusions will need to be introduced by insurers for professional indemnity and directors and officers policies from 2004, according to the Willis report.

In a statement, Munich Re noted that it "is seeking, and has done so successfully, to exclude asbestos from public liability policies in all countries, and we are in constant discussions with our U.K. clients about this topic."

Although the main asbestos exposure in the United Kingdom is through employers liability insurance policies, Munich Re's move to exclude asbestos from public liability policies "was imperative in light of the new asbestos regulations coming into force in the U.K. in 2004," the Munich Re statement noted.

Swiss Re noted that "globally, Swiss Re continues with its policy to avoid new asbestos exposures by either applying an asbestos exclusion or—in special cases—other types of limitations in its contracts."

## Letters to the Editor

Continued from page 8

ployees, especially at an employer rate of 75% of the total cost.

However, he is correct in saying that this could cause teetering business to shut their doors, but it could also negatively impact those that are doing OK or even well. He has obviously never owned his own business, and if he has, then he must have had a tremendous amount of working capital to absorb the cost of health insurance.

While he indicates that other employers would more than gladly increase their number of employees to meet the demand for the products or services discontinued by those out of business, he doesn't mention that competition would be decreased, thus possibly increasing the costs of goods and services. Nor does he mention that the costs of goods and services would also be increased by the health care costs that the employer must pass on to customers in the way of price. Would increased prices help the consumer in the long run?

Not once in the article did I see a reference to any study showing support for his theory. While I am a supporter of health care reform, I do not believe this is the best way to proceed.

**Tiffany Reiner**
Underwriting Manager
Ohio Casualty Group
Fairfield, Ohio

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BI 07-07-03 A 40 7/3/03 5:43 PM Page 1



# Affirmative: Ruling impacts employer diversity plans

Continued from page 3

rulings defy easy applicability.

Indeed, employers need to analyze their affirmative action and diversity programs in light of the decisions, said Ann M. Longmore, senior vp and product manager for Willis of New York Inc. They "need to read the decision very closely and then make a lot of leaps of faith and judgment in terms of whether or not the particular facts and circumstances seem closer to the justices' approval" of the use of race as a "plus" factor in individual decisions, or to the use of an automatic point system, she said.

"There's no bright-line test," Ms. Longmore said. "It's going to be difficult to determine which of the two (rulings) one is closer to, and therefore which outcome would apply in any given instance," she said. "It's going to take another case or two—or more—to give us any sense of certainty as to how we should read this decision."

Observers also note the court's decision was based on the Constitution's equal protection clause, while businesses are governed by Title VII of the Civil Rights Act of 1964. But many say the decision is nevertheless significant for employers.

The Supreme Court has said that a diverse workforce is a "legitimate goal that is legal, and you can take race into account in hiring," said Maria Blanco, Sacramento, Calif.-based national senior counsel for the Mexican American Legal Defense and Education Fund.

Until now, Ms. Blanco said, there has been debate as to whether employers could take race into account only to remedy past discrimination. But, she said, the court "has moved away from that notion" with its Michigan decisions "and I think that's very good for employers that want to hire diverse work forces."

David DeBruin, an attorney with Jenner & Block in Washington, said the firm's clients "were not so much concerned with the legal impact upon them" as with "their ability to go to leading colleges and universities and hire individuals who had been trained in a diverse environment, the same kind of environment in which their employees work." Jenner & Block filed an amicus brief on behalf of 65 companies in support of the university's admissions policies.

The *Grutter* decision in particular "will allow employers to continue their various diversity plans and operations," said Lawrence Z. Lorber, an attorney with Proskauer Rose in Washington. He said he is unaware of any employers that have hiring practices that resemble the University of Michigan undergraduate program's point system.

Gerald L. Maatman Jr., an employment attorney with Seyfarth Shaw in Chicago, said that because the decisions address the issues of race and affirmative action, they are "an important guidepost for employers who wish to use race in hiring and promotional decisions."

> **The decisions indicate to employers that they need to be aware of diversity, that they should recognize it and embrace it, and 'that they need to improve their programs around it.'**
>
> *Tom Casey*
> *Buck Consultants Inc.*

Although the issue still needs to be litigated in the lower courts, "there are signals in these rulings that…may support use of identification of race in making hiring and promotional decisions in certain circumstances," Mr. Maatman said. Employers, he added, now should "sit tight and see what happens."

Karen Berdin, an attorney with Ford & Harrison in Denver, said that although the decisions won't have a significant immediate impact, "I think what we'll see is probably more of a consensus surrounding the federal laws that mandate affirmative action for private employers." Employers with federal contracts or subcontracts that generate at least $50,000 in annual revenue are required to have written affirmative action programs, noted Ms. Berdin.

"There have been some attempts to roll back those requirements," and opponents of affirmative action "certainly won't take any comfort form these decisions," Ms. Berdin said.

"I think this is going to be significant," said Tom Casey, a principal with Buck Consultants Inc. in Boston. The decisions indicate to employers that they need to be aware of diversity, that they should recognize it and embrace it, and "that they need to improve their programs around it," Mr. Casey said. The high court's rulings are a "wake-up call that organizations need to be more proactive in their diversity practices," he said.

Frank Scruggs, an attorney with Greenberg Traurig in Fort Lauderdale, Fla., said that, in the wake of the decisions, poorly designed diversity programs "are likely to be closely scrutinized" to determine whether they are in line with the principles outlined in the rulings.

"The question is not whether one may embark upon a race-conscious diversity initiative. The more likely question is whether the particular manner in which such an initiative is designed and implemented comports with requirements of law, so to the extent an employer is doing more than teaching the work force about tolerance and helping to expand perspective, employers will need to assure their designs are thoughtfully carried through in operation," Mr. Scruggs said.

Mathew B. Halpern, an attorney with Jackson Lewis in Woodbury, N.Y., who coordinates his firm's affirmative action and diversity practice, said employers "should carefully look at the language that describes their programs and make sure in their eagerness to portray themselves as enlightened employers that celebrate diversity they don't create situations where their language, their descriptions come back later to haunt them in a reverse-discrimination case."

*Grutter vs. Bollinger et al., 02-241; and Gratz et al. vs. Bollinger et al., 02-516, United States Supreme Court.*

# E-mail: E-mail not trespassing

Continued from page 3

it was hurt by the loss of productivity caused by the thousands of employees distracted from their work and by the time its security department spent trying to halt the distractions after Hamidi refused to respect Intel's request to stop invading its internal, proprietary e-mail system by sending unwanted e-mails to thousands of Intel's employees on the system."

The state Supreme Court disagreed, however, finding that "the metaphorical application of real property rules would not, by itself, transform a physically harmless electronic intrusion on a computer server into a trespass.

The is because, under California law, intangible intrusions on land, including electromagnetic transmissions, are not actionable as trespasses (thought they may be as nuisances) unless they cause physical damage to the real property."

"Since Intel does not claim Hamidi's electronically transmitted messages physically damaged its servers, it could not prove a trespass to land even were we to treat the computers as a type of real property," the court ruled.

"We were disappointed in the court's ruling," an Intel spokesman said. "We believed that we could make the case—and we did through two levels of appeals—but clearly the majority of the Supreme Court didn't agree with us."

He added that Intel was evaluating the ruling and considering "what options we have available to us should Mr. Hamidi begin spamming again."

The American Civil Liberties Union, which represented Mr. Hamidi in the case, hailed the decision.

"A loss would have been devastating, because a loss would have said employers can censor all incoming e-mail to their employees," said Chris Hansen, senior staff counsel at the ACLU in New York.

"Employers, for the most part, don't try to censor all incoming mail, and shouldn't try to censor incoming e-mail. So, in that sense, although a loss would have been devastating, a win mostly preserves the status quo," he said.

Attorneys following the case noted that although the court ruling blocked one kind of legal remedy for employers, several others are available.

While the California Supreme Court "stood the decision of the appellate court on its head…hope is not lost for employers," said Brian Ashe, a partner in the San Francisco office of Sayfarth Shaw who regularly represents employers.

"The Supreme Court focused only on trespass as a specific tort, and there are a host of other torts that are available to employers to protect their employees from this sort of nuisance," he added.

"It's a very narrow decision," concurred Raymond Hixson, a partner in the employment and labor law group at Fenwich & West in Mountain View, Calif.

"This should not give former disgruntled employees a false sense of security. Likewise, it should not cause employers to feel that they are powerless. They still have a lot of legal weapons in the arsenal that they can use to combat this type of behavior. This only struck down the applicability of one particular kind of claim under these particular facts," he said.

For example, employers could still bring defamation and trade libel claims if there are false accusations made in e-mails that injure the reputation of the company, or they could charge unfair competition if there's a showing that an employee is doing something with a willful intent to harm the company, he said.

"So there are a host of different kinds of claims that can be brought. This decision made it clear that it was not addressing whether you could bring those other claims. In fact, it said those other claims may very well exist," Mr. Hixson observed.

"This is not at all an anti-corporate or anti-employer decision," said William M. McSwain, an associate at Dechert L.L.P. in Philadelphia who argued the case on behalf of Mr. Hamidi and the ACLU. Intel was simply overreaching, he said.

"They were asking for radical revision of Internet law when they don't need it, and the court rightly rejected it," Mr. McSwain said. "Trespass is just too powerful of a remedy. Employers have lots of bazookas they can use. They don't need the nuclear weapon of trespass law."

*Intel Corp.vs. Kourosh Kenneth Hamidi, Supreme Court of California, S103781.*

# Hawaii: Court rejects insurer definition

Continued from page 4

Pacific Inc. of Honolulu, next asked its excess insurer for defense coverage for its legal costs related to ongoing state environmental regulatory hearings over the pollution site.

The excess insurer, Pacific Employers Insurance Co. of Visalia, Calif., denied the requests on various grounds.

Invoking the sudden-and-accidental pollution exclusion, Pacific Employers argued that Servco lacks evidence that the pollution incident central to the coverage dispute occurred abruptly. Therefore, the excess insurer argues, it has no duty to defend or indemnify Servco.

But in ruling that the meaning of the exclusion "is hardly settled," U.S. District Court Judge Samuel P. King in Honolulu cited several state supreme and appellate court rulings as well as a federal appellate court's decision that "sudden" means an unexpected event, not an incident that occurs abruptly.

Given the ambiguity of the exclusion's meaning and the lack of case law precedence in Hawaii, "there is a potential for coverage under Hawaii law," Judge King ruled. Therefore, Pacific Employers must defend Servco from the date Servco settled with its primary insurer, the judge ruled.

Judge King, however, agreed with Servco that any decision on the meaning of "sudden"—and on Pacific Employers' resulting duty to indemnify—should be delayed until state regulatory proceedings over the site's remediation are concluded.

Pacific Employers' duty to defend also rests on whether Servco faces a "suit" within the meaning of the excess insurer's policy.

The excess insurer argued that the state environmental regulatory hearings do not constitute a covered "suit" because they are not court actions.

Judge King, however, ruled that he is convinced that Hawaiian courts—which have not ruled on this issue either—would reject the excess insurer's argument, as have the majority of courts in other states in similar coverage disputes.

Judge King issued his rulings on the meanings of "sudden" and "suit" after determining that Servco's settlement with its primary insurer first triggered the excess insurer's duty to defend its policyholder, even though the primary insurer has not yet paid its settlement.

The judge also ruled that the settlement exhausted the primary insurer's limits, even though the settlement did not specifically allocate any insurance proceeds to defense and cleanup costs.

Attorneys for Pacific Employers and Servco would not comment.

*Pacific Employers Insurance Co. vs. Servco Pacific Inc. and Island Insurance Co. Ltd., U.S. District Court for Hawaii, June 19; No. 01-00252 SPK/KSC.*

BI 07-07-03 A 42 7/3/03 5:42 PM Page 1



# Court: Rulings offer mixed results for businesses

**Continued from page 1**

Then the justices took the matter further by holding that punitive damages must reflect the harm the defendant did to the individual plaintiff and that the wealth of the defendant should not be taken into account when determining punitive damage awards.

"This is the blockbuster business case," said Robin Conrad, senior vp of the Washington-based National Chamber Litigation Center Inc., which handles litigation for the U.S. Chamber of Commerce.

"Far and away, the *State Farm* decision overshadows all of the other business cases," she said.

"That decision has done more than probably all the tort reform legislation on punitive damages to date," said Victor E. Schwartz, general counsel of the American Tort Reform Assn. in Washington. State laws can be overturned, but the high court's decision "is the law of the land," he said.

"Clearly, this term the punitive damages decision was far and away the major positive decision for manufacturers," said Quentin Riegel, vp-litigation for the National Assn. of Manufacturers in Washington. "It has already affected a handful of cases at the Supreme Court and is beginning to affect many cases in the lower courts," he said.

Two of the cases affected by the *State Farm* decision involved product liability claims against Ford Motor Co., he noted (*BI*, May 26). That move clarified that the court's rationale applied to all sorts of punitive damages, including those in product liability cases, he pointed out.

He added that health care also received the high court's attention this term, and not necessarily to an end employers applauded.

Mr. Riegel said that not only did the high court give health care "considerable attention" this year, but also "we can expect that to happen more frequently in the years ahead, as cost pressures and regulations and the economy create stresses that require legal resolution." In *Kentucky Assn. of Health Plans vs. Miller,* the high court said that the state's "any willing provider law" did not violate the Employee Retirement Income Security Act (*BI*, April 7). Mr. Riegel said that such laws undercut "the ability of companies to better manage and control health care costs."

He said another case—*PhRMA vs. Walsh*—"is more difficult to analyze." In that case, the majority held that Maine could proceed with its discount prescription drug plan, which benefits Medicaid recipients and other poor or moderate-income residents. Some observers fear that the law—which the high court said still must survive lower court and administrative challenges—could ultimately increase drug benefit costs for employer medical plans (*BI*, May 26).

Employers did win a victory in the court's decision in *Black & Decker Disability Plan vs. Nord*, said Mr. Riegel. In that case, the high court said that Social Security's so-called "treating physician" rule, which requires that a patient's treating physician should enjoy deference in determining the extent of a patient's disability, does not apply to ERISA plans (*BI*, June 2).

In a case that combined health care and liability questions, the high court disappointed employers by holding that the Federal Employers' Liability Act does not ban victims of non-cancerous asbestos-related diseases from seeking damages for their fear of developing asbestos-related cancers (*BI*, March 17). The court's decision in *Norfolk & Southern Railway Co. vs. Freeman Ayers et al.*, led business groups to step up their lobbying efforts to enact a federal asbestos liability reform law.

In its decision in *Dow Chemical Co. vs. Stephenson*, the court also gave the green light for veterans claiming to suffer from Agent Orange-related illnesses to pursue claims against manufacturers of the Vietnam era defoliant despite a 1984 class-action settlement of such claims (*BI*, June 16).

The high court told state governments in *Nevada Department of Human Resources vs. Hibbs* that states did not enjoy sovereign immunity against suits brought by state workers under the federal Family and Medical Leave Act.

Gerald L. Maatman Jr., a partner in the Chicago law firm Seyfarth Shaw, said employers should not ignore the potential impact of two other high-profile decisions that did not appear to deal directly with employment law.

"Overall, there were some remarkable decisions, especially regarding affirmative action and gay rights, and although they probably say less about the direction of the court, they certainly reflect the direction of the country on these cutting-edge issues," he said.

The first decision, in *Grutter vs. Bollinger et al.*, upheld the University of Michigan's practice of taking race into account when reviewing applicants to the school's law school. (See story, page 3)

"The University of Michigan case signals for businesses that insofar as they have a compelling interest to promote diversity in the workplace, there may be circumstances where race may be used as a factor in hiring or promotion decisions," he said.

The gay rights case struck down Texas' anti-sodomy law and appeared to void most others as well. "The gay rights case—*Lawrence vs. Texas*—adds fuel to the fire regarding the protection against sexual orientation discrimination in the workplace," he said.

"The seminal case for businesses this term, however, is the *State Farm* case, reining in punitive damages. This has a bottom-line impact on workplace litigation," he said.

PHOTO: AP/EVAN VUCCI

**William Hibbs, with his wife, won the right to sue the state of Nevada over denial of leave under the Family and Medical Leave Act.**

# Medicare: Bills would retain employer role

**Continued from page 1**

provide the subsidies, as well the generosity of those subsidies. Under the House bill, employers that retain prescription drug coverage would receive a subsidy equal to 28% of the cost of prescriptions filled for Medicare-eligible retirees, after a $250 deductible with a $5,000 ceiling. The subsidy, consultants estimate, could represent between 20% and 25% of prescription drug costs, consultants say.

The subsidy in the Senate bill is more complicated. It would be equal to 70% of the total premium for the prescription drug benefit and then would be modified by certain factors, such as where an employer's retirees reside. Still, the subsidy could amount to as much as 25% to 35% of costs, consultants say.

But, no one is certain whether the House or Senate version of the employer subsidy, or perhaps a third version, will be agreed upon by congressional conferees.

Conferees are expected to work throughout July to bridge the many differences in the two bills.

Given the one-vote margin in the House's passage, working out a compromise that both House and Senate will accept will not be easy.

Still, an agreement is likely, given the political capital that the Bush administration and the congressional leadership have invested in the issue, said Frank McArdle, a consultant with Hewitt Associates Inc. in Washington.

And if a final agreement is reached, it will almost certainly contain some type of employer subsidy, observers say. In recent weeks, some Senate Republicans have even been discussing the possibility of increasing the subsidy.

> **Legislators see the value of employer-provided retiree benefits and 'want to keep employers in the game.'**
>
> *Mark Ugoretz*
> *ERISA Industry Committee*

Congress' current interest in encouraging employers to retain prescription drug benefits is a contrast to 15 years ago, when Congress significantly expanded Medicare.

Then, the congressional attitude toward the role of employers' retiree health care plans was just the opposite. Not only were employers not encouraged to retain retiree health care benefits, the 1988 law would have required employers—for a two-year period—to return any savings they achieved when they eliminated benefits that would have duplicated those provided by an expanded Medicare program. The law was repealed just one year after enactment amid protests from higher-income retirees that the tax bite they would have incurred to pay for the benefits was too great.

The changed attitude, experts say, is because legislators now recognize the value of employer-provided retiree health care plans.

"They (legislators) want to keep employers in the game," said Mark Ugoretz, president of the ERISA Industry Committee, a Washington-based organization representing large employers on benefit issues.

One major benefit to the government of employers retaining prescription drug coverage is that retirees would face much less disruption if they could stay in their current benefits program rather than have to choose among plans that would contract with Medicare to provide prescription drug benefits.

"This would be a lot less disruptive," said Mark Hamelburg, an attorney with Mercer Human Resource Consulting in Washington.

Similarly, a continuation of coverage, especially by large national employers, could avert problems for retirees in rural areas, where Medicare might find it difficult to find health plans willing to offer the benefit, Mr. Hamelburg added.

Additionally, with their big blocks of retiree prescription drug business, employers could encourage more health plans to offer Medicare prescription drug coverage, Hewitt's Mr. McArdle said.

Employers do have options other than continuing their current coverage. Some, for example, might choose to offer prescription drug benefits that wrap around the benefit offered through Medicare.

The appeal of that approach is that the employer would have fewer direct dealings with the government—and the potential hassle associated with that—such as reporting their prescription drug costs, noted Joseph Martingale, national leader for health care strategy at Watson Wyatt Worldwide in New York.

Government subsidies would not be available for employers that took that approach, but employers would be less exposed to prescription drug costs.

If Medicare is expanded to cover a portion of retirees' prescription drug costs, employers might decide that it is no longer necessary for them to offer any coverage at all. Indeed, the Congressional Budget Office projects that more than 4 million retirees in employer plans would lose coverage if Medicare is expanded to cover prescription drugs. The CBO estimate, which has come under criticism from some members of Congress, does not break out how many of those retirees would have lost coverage anyway, such as through employer termination of plans, if Medicare were not expanded.

Until the legislation is finalized, though, and employers know what the rules are, it is too soon to say what strategy employers will take, Mr. Ugoretz said.

## ADVERTISER INDEX

### Issue of July 7


| ADVERTISER | PAGE # |
|---|---|
| Acordia Inc. | 16 |
| Aetna Corporate | 13 |
| American Institute for CPCU | 6 |
| American Reinsurance | 27 |
| Aon Corporation | 2 |
| Benesight | 34 |
| Burnham Systems | 36 |
| Business Insurance | 23, 32, 39, 41 |
| Carvill America Inc. | 30 |
| CNA Insurance | 25 |
| Corporate Systems Corp. | 32 |
| Corvel Corporation | 21 |
| Dickstein Shapiro Morin & Oshinsky | 20 |
| Duane Morris LLC | 26 |
| Endurance Re | 24 |
| First State Management Group | 12 |
| FM Global | 18/19 |
| Folksamerica Reinsurance | 15 |
| Group Health Inc. | 23R |
| Hub International | 33 |
| Hunter-Alliance Group | 36 |
| Marsh Inc. | 9 |
| Old Republic Risk Management | 17 |
| Partner Reinsurance | 35 |
| Pinnacol Assurance | 23R |
| PMA Reinsurance | 31 |
| Renaissance Reinsurance | 23R |
| Royal & SunAlliance | 44 |
| SAP | 5 |
| Sentry Insurance | 22 |
| Sonnenschein, Nath & Rosenthal | 14 |
| Sprint Communications | 11 |
| Swett & Crawford | 29 |
| Valley Oak Systems | 28 |
| XL Insurance | 7 |

BI 07-07-03 A 43 7/3/03 5:43 PM Page 1



# Late News

Continued from page 1

## Factory Mutual sued for Sept. 11 coverage

The U.S. Postal Service filed a lawsuit last week against Factory Mutual Insurance Co. for failing to pay for damages to facilities caused by the Sept. 11, 2001, terrorist attacks. The Postal Service's suit charges that Factory Mutual, which does business as FM Global, has denied its business interruption claims and claims for removing debris and decontaminating its offices located near the World Trade Center site. According to the suit, the offices were uninhabitable after burning debris from the WTC fell into the building through shattered windows, causing fires, smoke damage and sprinkler flooding.

## AIA warns against added asbestos fund levy

American Insurance Assn. President Robert E. Vagley has warned Senate Judiciary Committee Chairman Orrin Hatch, R-Utah, that insurers cannot support the Fairness in Asbestos Injury Resolution Act if it strays too far from Sen. Hatch's original proposal. The bill—S.1125—would replace the current litigation-based system for compensating victims of asbestos-related diseases with a national no-fault $108 billion trust fund. Insurers would be responsible for as much as $45 billion of the fund.

Mr. Vagley

## Goshawk exploring changes after profit warning

Goshawk Insurance Holdings P.L.C. is reviewing options for its underwriting businesses following a warning that its profits for 2003 will be lower than expected. The London-based group said it has "decided to review all strategic options regarding future direction." Those options include expanding the group's successful Bermuda-based arm—Goshawk Re—or putting the whole company up for sale, among other changes, a spokesman for the group said.

## Bermuda's AXIS launches IPO

AXIS Capital Holdings Ltd. raised $473 million in its initial public offering last week. The Pembroke, Bermuda-based insurer and reinsurer priced the offering of 21.5 million shares at $22 per share. The shares, which included 8.1 million shares offered by private shareholders, represent around 15% of the company's equity. The shares are trading under the symbol AXS on the New York Stock Exchange.

## HRH creates E&S wholesaler

Hilb, Rogal & Hamilton Co. has created an excess and surplus lines wholesale brokerage operation. Bryan W. Sanders has been named president of the new Dominion Specialty Group Inc., which will be based in Lake Mary, Fla. Mr. Sanders formerly headed Brown & Brown's MacDuff Underwriters Inc. wholesale division.

## Dual International buys ACE unit

Underwriting agency Dual International has acquired ACE Corporate Risks Ltd. for an undisclosed sum. The company, now known as Dual Corporate Risks, specializes in directors and officers and professional indemnity coverage. XL London Market's syndicate 1209 provides 100% of Dual's capacity of 75 million euros ($86.3 million).

## SCOR selling alternative risk unit

SCOR S.A. has signed a letter of intent to sell its Commercial Risk Partners Ltd. unit to an undisclosed buyer. The potential buyer has exclusive rights to the sale until July 31, SCOR said. A spokeswoman for Paris-based SCOR declined to provide further details. SCOR said in January that it planned to sell the Bermuda-based alternative risk financing operation, which has been plagued by losses, as part of a restructuring of the group.

SCOR

## Briefly noted

A group of **deep vein thrombosis** claimants has lost its appeal to seek compensation from 18 airlines. The Court of Appeal in London upheld an earlier court ruling that said the airlines were not liable because DVT cannot be classified as an accident under the terms of the 1929 Warsaw Convention. The 24 claimants, who said that they or a family member developed the circulatory condition from sitting in cramped conditions on long-distance flights, said they would take their case to the House of Lords, the highest U.K. court.

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# Pollution: Policyholder wins dispute

Continued from page 1

"This decision indicates that anybody who has this policy with this language is going to be insured," said Paul Golden, an attorney with Hagan, Coury & Associates in Brooklyn, which represented Belt Painting. "It indicates that the insurance company cannot use this (exclusion) as a back-door means of escaping" the duty to provide coverage, he said.

The ruling is part of a trend by the courts to favor policyholders in such cases, according to Lorelie S. Masters, a policyholder attorney with Jenner & Block L.L.C. in Washington. With last month's District of Columbia Appeals Court ruling that restricts the scope of the absolute pollution exclusion (*BI*, June 23), "these two decisions continue that trend," she said.

The total pollution exclusion and the absolute pollution exclusion differ slightly but are generally considered similar enough that a ruling regarding one will impact cases involving the other.

Thomas R. Newman of the New York firm Duane Morris, which represented TIG, acknowledged that the ruling, "in New York, at least, means insurers probably will have to write another exclusion."

Mr. Golden warned, though, that if insurers drastically restrict coverage, "no one will sign such an insurance agreement."

The decision is important, too, because it comes from a New York court, sources say.

"That's probably the most significant part of it," said Ms. Masters. A state court has now definitively answered the question of ambiguity with regard to the exclusion, she said. "People like me will be citing it outside of New York. Absolutely."

"To see the New York State Court of Appeals—which is not the most friendly for policyholders—come out and make some sense of this nonsense is a very good sign," agreed William Passannante, co-chairman of the insurance coverage group at Anderson Kill & Olick P.C. in New York. The firm filed a brief on behalf of United Policyholders, a nonprofit insurance consumer organization, supporting Belt Painting's position in the case.

"To the extent that the New York State Court of Appeals is seen as prestigious, this decision will be influential elsewhere," said Randy J. Maniloff, an insurer attorney with Christie, Pabarue, Mortensen & Young P.C. in Philadelphia.

The case began wending its way through the New York courts when Belt Painting sought summary judgment in New York Supreme Court that TIG was obligated to defend and indemnify the claim. The trial court ruled for TIG, rejecting the plaintiff's contention that the exclusion was inapplicable because the injury was not caused by environmental or industrial pollution.

Insurers and policyholders have long battled over the exclusion's applicability, with policyholders contending it applies only in cases of environmental or industrial pollution.

The Appellate Division reversed the lower court ruling, saying the exclusion applies only where damages are "truly environmental in nature" or the result of "pollution of the environment." The high court agreed that the exclusion does not apply to the underlying personal injury action.

> **'To see the New York State Court of Appeals...come out and make some sense of this nonsense is a very good sign.'**
>
> *William Passannante*
> *Anderson Kill & Olick P.C.*

TIG argued that the paint and solvent fumes that caused Mr. Cinquemani's injuries are well within the definition of pollutants in the exclusion and emphasized that fumes are a part of the definition. The insurer further argued that the exclusion does not include language that has led courts in prior cases to rule such exclusions are ambiguous. That language states that the exclusion applies to pollutants released "into or upon the land, the atmosphere or any water course or body of water."

The state court of appeals stated in its ruling that even though fumes are defined as pollutants in the exclusion, the exclusion applies only if the injury is caused by "discharge, dispersal, seepage, migration, release or escape" of the fumes. "It cannot be said that this language unambiguously applies to ordinary paint or solvent fumes that drifted a short distance from the area of the insured's intended use and allegedly caused inhalation injuries to a bystander," the court ruled.

The court further ruled that the absence of language regarding a release into land, atmosphere or water "simply removes a redundancy in the exclusion" because any pollution would involve a discharge into one of the three.

Mr. Passannante of Anderson Kill praised the decision, saying the court looked at "the real purpose behind insurance" in its decision. The ruling backs up the reasoning by companies like Belt Painting for purchasing CGL coverage, he said, which is to protect their businesses from liability that is incurred while providing their services.

*Belt Painting Corp. vs. TIG Insurance Co., New York State Court of Appeals; July 1, 2003.*

## Online Poll

[ 6/30 - 7/3 ]

**Would you support a surcharge on commercial insurance policyholders to capitalize a new trust fund to pay asbestos liability claims?**

| | |
|---|---|
| Yes | 33% |
| No | 67% |

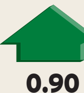
## *BI* Stock Index

**[ 6/30 - 7/3 ]**

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

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

**BI Stock Index** 1958.68 1.61

**Dow Jones** 9070.21  0.90

**S&P 500** 985.70 0.97

**Largest gains**

| | |
|---|---|
| Philadelphia Consol. | 6.90% |
| Allmerica Financial Co. | 6.69% |
| Navigators Group | 6.09% |
| Hub International | 5.29% |
| RLI Corp. | 4.53% |

**Largest losses**

| | |
|---|---|
| ProAssurance | -7.38% |
| Gainsco Inc. | -7.14% |
| Vesta Insurance Co. | -6.20% |
| Meadowbrook Ins. Group | -5.04% |
| Odyssey Re Holdings | -3.94% |

**Weekly change by market segment**

| | |
|---|---|
| Brokers | 0.82% |
| Insurers/Reinsurers | 0.56% |
| Managed Care Organizations | 0.61% |

Source: CNET Investor (investor.cnet.com)