

## BACKGROUND CHECKS

Steps employers should consider to comply with the Equal Employment Opportunity Commission's policy on criminal background checks of current or prospective employees.

- Remove questions about criminal history from employment forms.
- Review hiring processes to make sure they are in accordance with EEOC guidelines.
- Do not automatically rule out an employee with a criminal background unless it relates directly to a potential job.
- Set objective guidelines for which convictions would disqualify an applicant.

## EMPLOYMENT PRACTICES

### Background check rules raise concerns

BY JUDY GREENWALD

Employers are struggling to ensure their workers' and customers' safety yet comply with an Equal Employment Opportunity Commission policy on criminal background checks that legal experts say is vague and onerous.

In addition to failing to establish clear guidelines, the EEOC's insistence on an individualized inquiry into applicants' and workers' criminal backgrounds is particularly problematic for large employers that must process applications from numerous applicants.

The EEOC in April updated enforcement guidance on employers' use of arrest and conviction records. The guidance called on employers to consider the nature and gravity of the offense when

See **BACKGROUND** page 29

## WORKERS COMPENSATION

### HEALTH CARE WORKERS RISK BECOMING PATIENTS

High injury rates worry employers, insurers



BY ROBERTO CENICEROS

Health care facilities are increasingly drawing attention for their unique exposures, which drive more worker injuries than occur in either manufacturing or construction operations.

More obese patients requiring lifting, dementia-related alterations driven by an aging patient population, and an older workforce are contributing to a disproportionate number of employee injuries and losses at hospitals and nursing homes, experts say.

In response, health care companies have ramped up risk mitigation efforts amid increasing injury costs, as well as union, regulator and insurer recognition of the problems.

Loss mitigation efforts to curb employee injuries across the

See **WORKERS** page 32

#### HEALTH CARE WORKERS' INJURIES

According to data released Aug. 6 by the National Institute for Occupational Safety and Health, the health care industry employs more than 18 million workers. Here is what the 2011 data on injuries causing missed work days show about hospital workers:

**38.7:10,000**

- They suffered 38.7 falls, slips, and trips per 10,000 full-time employees, in contrast to a rate of 26.1 per 10,000 for all other workers.

**23:10,000**

- Overextension in lifting caused 23 injuries per 10,000 hospital workers, while all other workers experienced them at a rate of 13 per 10,000 employees.

**13.4:10,000**

- Violence and "other injuries by persons" drove 13.4 injuries per 10,000 workers in contrast to 2.7 per 10,000 for all other industries.

## MERGERS & ACQUISITIONS

### Gallagher's Bollinger buy follows trend

Larger brokerages step up M&A activity to diversify, expand

BY BILL KENEALY

Arthur J. Gallagher & Co.'s \$276.5 million acquisition of Bollinger Inc. exemplifies the trend of insurance brokerages using sizeable acquisitions to diversify their operations.

While growth via acquisition has long helped brokerages bolster their core businesses, many recent deals have focused on acquiring companies that add ancillary operations in areas such as consulting and handling claims, said John L. Ward, Loveland, Ohio-based CEO of private equity firm Cincinnati Partners L.L.C.

"One trend we are seeing is the big brokers diversifying outside of the core U.S. brokerage business," Mr. Ward said. "The Bollinger acquisition by Gallagher is an example, because Bollinger is a very diverse business."

In announcing its biggest buyout ever this month, Itasca, Ill.-based Gallagher highlighted Short Hills, N.J.-based Bollinger's sports programs division, a managing general underwriter for golf and country clubs across the United States on a retail and wholesale basis that is expected to generate more than \$10 million in annual revenue. And Bollinger will add \$20 million worth of annual revenue in

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NEWS

HEALTH CARE REFORM

COST-SHIFTING, SLOW ECONOMY RESTRICT HEALTH COST INCREASES

Employees put off medical procedures to save money

BY JERRY GEISEL

Group health care plan costs continue to increase modestly with no sign that premiums will spike again anytime soon.

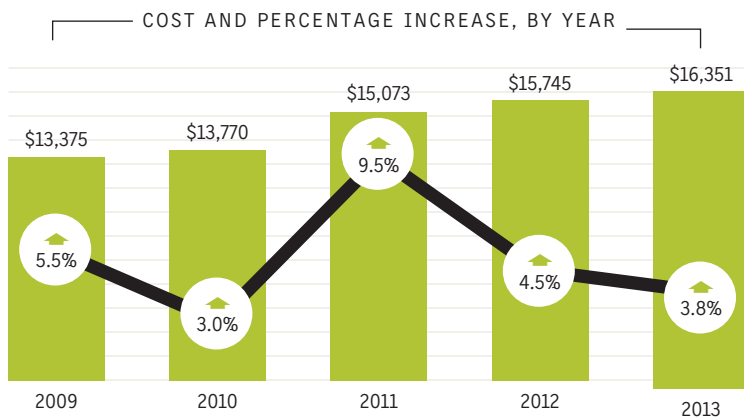
In 2013, group health care premiums for family coverage increased just 3.8%, rising to an average of \$16,351 per employee, according to a Kaiser Family Foundation survey of more than 2,000 employers released last week.

That 3.8% increase is the fourth time during the past five years that annual premium increases have remained less than 6%. During that five-year period, cost increases moved out of the 3% to 5.5% range only in 2011. That year, group health care costs increased an average of 9.5%, which Kaiser President and CEO Drew Altman said at the time was an "aberration" and some Obama administration officials attributed the increase at least in part to insurers' miscalculations on the effect of the health care reform law.

With cost increases running well below 5% in 2012 and 2013, "The critics will have a much harder time blaming big premium increases in employer insurance on Obamacare ... because there aren't any big premium increases," Mr. Altman said last week at a news briefing.

GROUP HEALTH CARE COSTS

Except for a one-year blip in 2011, annual increases in group health care premiums for family coverage have stayed in a fairly narrow range over the past five years.



Source: Kaiser Family Foundation

Benefits experts say there are several key reasons why cost increases have remained modest even as employers have had to beef up their health care plans, such as offering coverage to employees' adult children up to age 26 to comply with health care reform requirements.

The most significant factor keeping cost increases in check is the sluggish economy, experts say. "The economy still is flat on its

back. Employees feel they can't afford to use more services," said Helen Darling, president of the National Business Group on Health in Washington.

"As Americans have faced economic pressures, they have put off using medical services and that certainly has helped to keep costs in check," said Tracy Perez, an account executive and vice president in the Denver office of Lockton Cos. L.L.C

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RISK MANAGEMENT

Drunk patient case raises risk management issues

BY MATT DUNNING

A recent court ruling should motivate hospital risk managers to conduct a careful periodic review of their facility's procedures and legal obligations when it comes to treating intoxicated patients.

In a June ruling, the New York State Court of Appeals — the state's highest court — upheld a lower court's dismissal of a 2007 lawsuit that had accused Poughkeepsie-based St. Francis Hospital and Health Centers of medical malpractice and negligence for

CASE DISMISSED

On June 26, The New York State Court of Appeals ruled 5-2 to dismiss Kevin Kowalski's medical malpractice lawsuit against St. Francis Hospital and Health Centers, Dr. Chandra Chintapalli and Emergency Physician Services of New York Inc. A Dutchess County Supreme Court judge cleared the suit for trial in 2011, but the court's Appellate Division dismissed it last year. In its ruling, the Appeals Court held that:

- The state's mental hygiene law makes no provision for involuntary retention of patients who come to a hospital voluntarily, and there is no principle of common law that would permit the restraint of a patient based on the facts in evidence.
- Moreover, the court held that "there can be no duty to do that which the law forbids."
- Neither the hospital staff's failure to consult the record of Mr. Kowalski's previous admission, during which he professed to contemplating suicide, nor Dr. Chintapalli's decision not to inform police of Mr. Kowalski's decision to leave the hospital without being discharged equate to negligence, as state law does not compel either action under the circumstances of the case.

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MERGERS & ACQUISITIONS

Demand surges for transactional risk insurance

Products attractive to buyers and sellers

BY JOANNE WOJCIK

Sales of representations and warranties insurance have been surging globally as more midsize businesses and investors discover its effectiveness in facilitating a clean exit for sellers and reducing post-closing liabilities for buyers involved in mergers and acquisitions.

The total policy limits for this and other forms of transactional risk insurance products purchased by clients of broker Marsh Inc. increased 41% over 2011 to \$4 billion in 2012. The biggest increase in policy limits for transactional risk insurance was in North America, where it grew 86% during 2012, Marsh reported.

Marsh also reported that the vast majority — 60% — of transactional risk insurance policies placed worldwide last year were for corporate sellers or buyers, which are typically more cautious on the amount of warranty protection they require in a transaction than their private-equity counterparts.

"We have seen a pretty rapid increase in the use of that product in the past couple of years," said Jay Rittberg, vice president for mergers and acquisitions insurance at New York-based American International Group Inc. "Reps and warranty represents the majority of our (transactional risk insurance) business," he said. "There's more widespread acceptance of the product in the M&A world now. We've basically doubled the number of policies that we've written."

The "sweet spot" for representations and warranties insurance purchases "is transactions that have purchase prices between \$15 million and \$1.5 billion," said Craig Schioppo, Marsh's New York-based transactional risk practice leader. While "sellers purchase the policies when they're on the hook for a significant indemnity post-closing," he said, "buyers are using it strategically in competitive scenarios so they can ask for lower indemnities from the seller to make their bids look more attractive."

For example, "if we were each bidding \$100 million on a company and asking for a \$20 million

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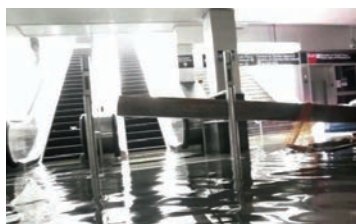
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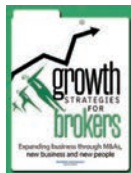
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**NEWS**

**CAPTIVE INSURERS**

**GROWTH IN CAPTIVE DOMICILES  
CREATES CHOICES FOR OWNERS**

Regulatory issues, infrastructure scrutinized

BY RODD ZOLKOS

BURLINGTON, Vt. — Prospective captive owners have more choice than ever in terms of available domiciles, but the key factors in their decisions typically remain regulatory quality and available captive infrastructure, according to many captive experts.

While new domiciles continue to form, some wonder whether they'll be able to provide the needed level of regulatory support or be able to achieve a critical mass of captive formations needed to ultimately compete with established domiciles.

Peter Mullen, Pembroke, Bermuda-based CEO of Aon Global Risk Consulting's captive and insurance management operations, suggested keeping a close eye on all the new domiciles. "We would have a concern that they could all support the right level of regulatory infrastructure," said Mr. Mullen.

Many of the new domiciles, including New Jersey, North Carolina and Texas, are looking to attract the captives formed by businesses that are based in the state, Mr. Mullen said. "But that's finite."

Established domiciles have a



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This year's Vermont Captive Insurance Association conference drew more than 1,100 attendees to Burlington, Vt.

track record prospective captive owners can consider, Mr. Mullen said, something the new domiciles lack. The newer domiciles also

potentially face a "dearth of regulatory talent," Mr. Mullen said,

See **VCIA** page 28

**WORKERS COMPENSATION**

**High prices, inefficiencies hit comp costs**

BY KATE SHEPHERD

Unnecessary medical expenditures and how they affect workers compensation were a key focus of *Business Insurance's* fourth annual Worker's Compensation Virtual Conference.

The Aug. 22 virtual conference centered on solutions to optimize comp claims management.

A 2009 study by the Institute of Medicine found there were \$700 billion in unnecessary costs in the U.S. health care system, said keynote speaker Dr. Richard A. Victor, executive director of the Workers' Compensation Research Institute.

He highlighted the main reasons for the excess costs: unnecessary care, too-high prices and inefficiently delivered medical services.

The three factors alone account for nearly \$500 billion in unnecessary medical expenditures, said Dr. Victor, who said his main area of interest currently is abuse of prescription opioid medications.

"It's very common for injured workers to receive at least one opioid prescription," Dr. Victor said during the presentation. "The question is how long does their treatment for opioids last?"

Periodic and random drug testing and psychiatric evaluations and treatments are ways to decrease long-term abuse of opioid painkillers among comp claimants, Dr. Victor said.

Sessions during the virtual conference provided strategies and advice to control comp costs.

"Getting the Best Results from Workers Comp Claims Management" featured David Donn, president of David Donn Consulting Inc.; Mark E. Field, risk manager of Raley's Inc.; and David North, president and CEO of Sedgwick Claims Management Services Inc.

"Relying on Health Advocacy for Improved Results" featured Kimberly George, senior vice president of managed care practices and client services at Sedgwick.

"How to Avoid Complications in Medicare Secondary Payer Act Compliance" featured Roy Franco, principal of Franco Signor L.L.C.; Aaron Frederickson, director of Medicare Secondary Payer compliance at Allsup Inc.; and Craig Storey, business development executive at Rising Medical Solutions.

The free virtual conference is available on demand online at [www.businessinsurance.com/2013/wcconference](http://www.businessinsurance.com/2013/wcconference).

**WORKERS COMPENSATION**

**Quick mental health interventions can reduce long-term comp costs**

BY ROBERTO CENIGEROS

ATLANTA — Early intervention for employees suffering from mental health issues can reduce worker disability durations and costs by preventing illnesses from advancing to more serious conditions, experts say.

That may require employers to integrate a mental health early intervention program into their disability management programs. Fortunately, there is a growing awareness about the need to address employee absenteeism and employer disability costs

through mental health efforts, and an increasing number of practical solutions for treating mental illness.

For instance, patient self-rating questionnaires can collect information beyond what's normally gathered by an attending physician to help learn whether a psychiatrist is needed to provide appropriate treatment.

Such measures used early can help employees return to work, or even remain at work while receiving treatment before a problem

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**BUYERS CHOICE AWARDS**

*Business Insurance* invites insurance decision-makers to participate in a short survey to determine the most important insurance decision drivers among commercial insurance or employee benefits buyers. Find out the qualities peers rank as crucial drivers when selecting insurers, brokers and third-party administrators in the Nov. 18 issue. Contact Director of Research Angelina Villarreal at [avillarreal@businessinsurance.com](mailto:avillarreal@businessinsurance.com) to receive a survey. Those who complete the survey will get two free *Business Insurance* white papers and a chance to win a prize valued at \$600.

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# SHINING THE LIGHT ON RISKS FROM SOLAR EQUIPMENT

## Contractor general liability cover for defects tied to property damage

BY MATT DUNNING

As solar energy becomes more popular in the United States, reports suggesting an increase in equipment failures could lead to a sudden spike in solar contractors seeking coverage for defective building materials.

From 1999 to 2009, failure rates as high as 15% were measured along key metrics within the International Electrotechnical Commission's design qualification and safety testing regimen, according to a pair of reports published in July by the Solar America Board for Codes and Standards, an advisory coalition for the solar industry funded by the U.S. Department of Energy.

In a 2011 sample study of 204 solar panel modules that included 53 separate designs, approximately 17% experienced failures qualifying for warranty returns, according to one of the reports.

The upward trend in solar panel failure rates should be of immediate concern to small and midsize installation contractors, attorneys say, particularly as market conditions continue to pressure domestic and foreign solar panel manufacturers to cut costs by using cheaper components, assembly methods and shipping safeguards.

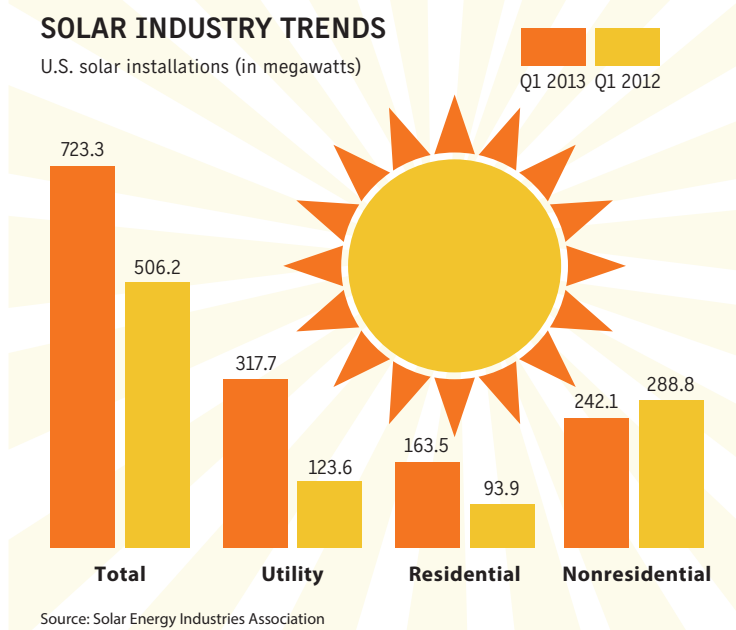
In turn, smaller general contrac-

tors and subcontractors — themselves under pressure to deliver timely completion of their work on much thinner operating margins than in years past — could expose themselves to financial liability stemming from defective, low-cost solar panels.

"It's something that policyholders should be thinking about," said Scott Turner, a Washington-based insurance recovery attorney at Anderson Kill & Olick P.C. "If (the failure trend) continues to bloom and develop, I would think there are a number of commercial buyers of these solar products out there that would have millions of dollars potentially at stake."

"If those (failure rates) are legitimate, then yes, you're likely to see a rise in defective building materials claims," said Amy Joseph Coles, a Pittsburgh-based partner at Duane Morris L.L.P. "It looks to me like we're still in a mounting-up period, and I can't tell how or when that spike will hit, or how significant it will be."

The extent to which an installation contractor would be able to recover losses stemming from defective solar panels through a commercial general liability or builder's risk insurance policy will depend largely on the nature of the panels' failure and, in most cases,



whether that failure resulted in physical property damage, attorneys say.

Many of the solar panel failures outlined in the Solar America Board for Codes and Standards' reports were due to either an initial shortfall or accelerated reduction in wattage output, as opposed to a mechanical or physical defect. In those circumstances, coverage attorneys say, installation contractors likely would be hard-pressed to find coverage under their traditional commercial general liability or builder's risk policies for underperforming solar equipment, especially if the losses incurred are economic in nature.

"Whether it's a GL policy that requires an occurrence and then resulting property damage, or a builder's risk policy that's going to have an exclusion for faulty or defective workmanship or latent defects, you're not going to find a lot of relief in terms of coverage for economic losses," said Steven Ginsburg, an Atlanta-based partner at Duane Morris.

In the event that an installation contractor's dispute over coverage for losses stemming from defective solar panels reaches the litigation stage, the jurisdiction in which the case is tried could be a crucial factor in that contractor's success,

attorneys say. State and federal judicial districts have come to a variety of decisions when it comes to providing defective building materials relief for contractors under general liability policies.

"There are states that will consider 'property damage' to include any damage caused by the removal and replacement of a solar panel, but other states won't recognize that as covered damage," said William Knowles, a Seattle-based insurance coverage and claims attorney at Cozen O'Connor.

As an alternative to seeking coverage under a traditional general liability or builder's risk policy, solar contractors may be able to leverage market conditions to require panel makers to buy manufacturers and system-level performance warranty insurance policies, which can be tailored to provide contractors and project owners with an additional layer of financial protection against costs associated with defective solar power systems or components.

"The lesson to be learned here is that if you're purchasing and installing these systems, the market is at a place right now where you may well be able to get what you need from the manufacturer to protect yourself," Ms. Coles said.

## EXCLUSIONS CAN LIMIT RECOVERY

Under standard commercial general liability policies, contractors may struggle to recover losses related to defective solar panel systems and modules depending on the nature and physical condition of the defect.

Common exclusions that may thwart a solar contractor's successful recovery include:

### Business risk

Commercial general liability policies generally do not provide coverage for physical damage done to a contractor's own work or property, or for costs incurred by a contractor related to repair, removal or replacement of an insured's defective work or product. However, courts in some states have interpreted the policies to include coverage for damage done to third-party property in the course of repairing or replacing defective work or products.

### Contractual risk

In most cases, general liability policies do not cover damages for which a contractor has assumed liability via a contract or agreement with a project owner or other third party. When a solar panel system or module, once installed, fails to meet contractually specified performance metrics without having been physically damaged, "there is an overarching concern that a lot of these claim scenarios could be more likely to manifest as breach-of-contract claims," said Steven Ginsburg, an Atlanta-based partner at Duane Morris L.L.P.

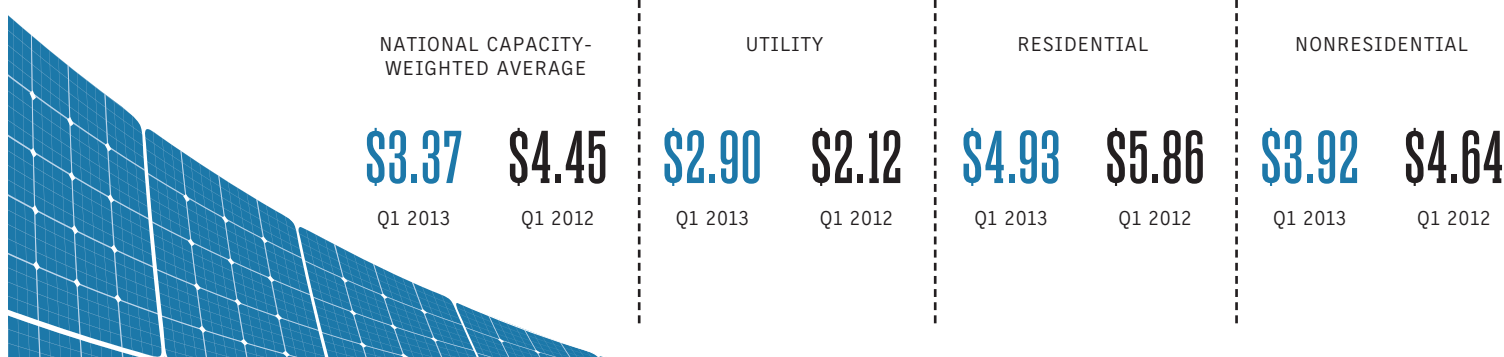
### Property vs. economic damage

Coverage under standard general liability policies is triggered by an occurrence that results in property damage, typically defined as physical damage to or the loss of use of tangible property. If a defective solar panel module or system has not damaged any real property, or underperformed to the extent it prevents a third party's use of their property, "that's going to be more along the lines of a warranty claim, and those are generally not covered under CGL," said William Knowles, a Seattle-based insurance coverage and claims attorney at Cozen O'Connor.

By Matt Dunning

## SOLAR CAPACITY AND PRICING

U.S. installed pricing, per watt



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# AUTOMATIC ENROLLMENT FOR RETIREMENT SAVING GETS TRACTION

Participation rates climb as mid-market firms add feature to 401(k) plans

BY JERRY GEISEL

Mid-market employers are embracing automatic enrollment, the biggest 401(k) plan design change since the plans first were launched three decades ago.

Automatic enrollment is aimed at employees who don't respond when they are asked whether they want to participate in their company's 401(k) plan. They are told that, unless they object, they will be automatically enrolled in the plan.

Among employers with between 500 and 2,500 participants in their 401(k) plans, 43% now offer an automatic enrollment feature, according to research by Fidelity Investments. That's up from just 28% four years ago and isn't that much lower than the automatic enrollment adoption rate — now 50%, according to Fidelity — among employers sponsoring the largest 401(k) plans with more than 25,000 participants.

"There has been a definite uptick in the percentage of plans offering automatic enrollment," said Jeanne Thompson, Fidelity's vice president of thought leadership in Boston.

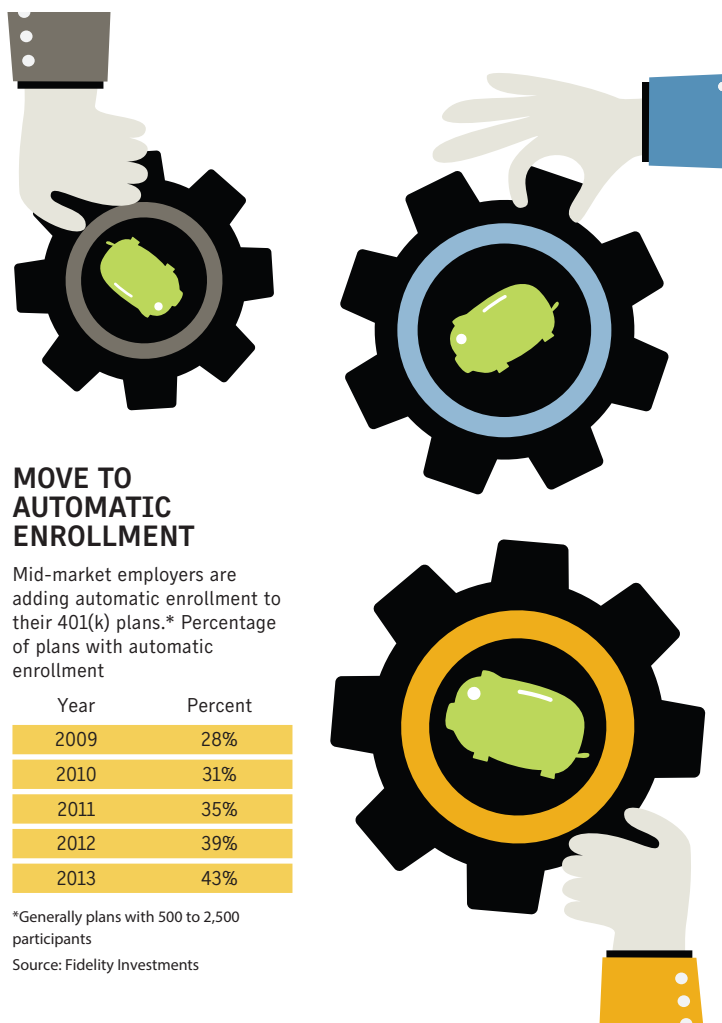
The biggest factor driving mid-market employers to add automatic enrollment to their 401(k) plans is that it's a sure-fire way to boost the percentage of employees participating in the plans.

"Automatic enrollment really does change behavior," said Michael Weddell, a principal with Mercer L.L.C. in Detroit.

Experiences of middle-market employers that have added automatic enrollment features to their 401(k) plans provide real-world examples of that behavior change.

Prior to adding automatic enrollment to its 401(k) plan roughly two years ago, PFSweb Inc. had an anemic participation rate. Just 22% of eligible employees participated in the plan, said Jennifer Davis, vice president of human resources for the Allen, Texas-based e-commerce solutions provider, which has about 1,000 U.S. employees. But with that one simple change, the participation rate jumped to 85%.

"This has been huge," Ms. Davis said, referring to the effect of automatic enrollment on the plan participation rate.



Other mid-market employers also have calculated how automatic enrollment has boosted 401(k) plan participation rates.

Before adding automatic enrollment in January 2009 at Sanden International (USA) Inc., a Wylie, Texas-based manufacturer of automotive air compressors with about 500 employees, between 55% and 60% of eligible employees participated in its 401(k) plan.

Now, with automatic enrollment in place for several years, about 80% of eligible employees participate in the plan, said Stephanie Caraway, Sanden's senior human resources manager.

"We want to do what we can to help ensure that employees have sufficient retirement plan savings," Ms. Caraway said.

Such increases in 401(k) plan participation rates after an automatic enrollment program is added are common, benefits consultants say.

"It is not unusual for a company that had a 50% to 60% participation

rate before automatic enrollment to see the enrollment rate hit 90%," said David Altimont, a senior vice president and practice leader with Lockton Retirement Services in Dallas.

"You see significant increases in participation. Eighty percent is a common goal," said Alan Vorchheimer, a principal with Buck Consultants L.L.C. in New York.

There are costs to adding an automatic enrollment feature to a 401(k) plan. Typically, because employers at least partially match employees' salary deferrals, employer contributions will increase to the extent employee participation increases. There are several key benefits resulting from automatic enrollment that help to offset those costs.

One is that by increasing employee participation, the likelihood that a 401(k) plan will fail nondiscrimination tests will decrease. Under those tests, plan contributions made by higher-paid employees

cannot, on average, exceed those of lower-paid employees by an amount set under the Tax Reform Act of 1986.

When a 401(k) plan fails the nondiscrimination tests, contributions have to be returned to higher-paid employees, which is administratively complicated for employers and harmful to employee morale, because affected employees will have a higher taxable income than they expected and less tax-favored retirement savings.

Because lower-paid employees are less likely to sign up to participate in 401(k) plans, adding an automatic enrollment will bring in more of them and reduce the likelihood of a plan failing the nondiscrimination tests.

"Automatic enrollment is a help in passing the nondiscrimination tests," said Jack Abraham, a principal with PricewaterhouseCoopers L.L.P. in Chicago.

Automatic enrollment also helps to offset another big retirement plan trend: employers freezing defined benefit pension plans.

When those plans are frozen, 401(k) plans typically become an employee's sole employment-based retirement plan. If employees don't contribute to 401(k) plans after a pension freeze, the likelihood they will not have accumulated sufficient savings to retire increases significantly.

This has negative consequences for employers. If employees remain working longer than they or their employers expected because they can't afford to retire, the movement of younger employees to more senior positions in a company can be disrupted.

"Employees can outstay their welcome, if they stay longer than either they or their employers want," Lockton's Mr. Altimont said.

The likelihood of that scenario is somewhat reduced if employees who didn't sign up for their company's 401(k) plan are automatically enrolled.

"There is a value in helping employees save for retirement," said Joleen Workman, assistant vice president of retirement services with the Principal Financial Group Inc. in Des Moines.

## PLANS AT NONPROFITS ARE CATCHING UP

Middle-market sponsors of 403(b) plans haven't embraced automatic enrollment as quickly as their private-sector counterparts with 401(k) plans, but interest is growing.

In 2012, just under 25% of 403(b) plans — the nonprofit world's rough equivalent of 401(k) plans — with between 200 and 999 participants offered automatic enrollment. In contrast, nearly 46% of 401(k) plans with between 250 and 999 participants had an automatic enrollment feature, according to surveys conducted by the Plan Sponsor Council of America in Chicago.

But more 403(b) plan sponsors, especially colleges, universities and nonprofit health care systems, are considering adding automatic enrollment, said Terry Richardson, a principal with PricewaterhouseCoopers L.L.P. in Dallas.

One of those educational institutions is Seattle Pacific University in Seattle. "It is a way of increasing the likelihood that employees will have enough savings to retire," said Don Mortenson, the university's senior vice president for planning and administration.

Yet some have offered them for years. At the eight institutions making up The Claremont Colleges, automatic enrollment was added in 2008 to their 403(b) plans "to eliminate the risk that some employees may not enroll in the plan on their own," said Robert Bloomer, director of benefits administration with the Claremont University Consortium in Claremont, Calif.

By Jerry Geisel

## MOVE AWAY FROM DEFINED BENEFIT PLANS

Getting employees working for mid-market employers to participate in 401(k) and other defined contribution plans has assumed greater importance as those employers have moved away from traditional defined benefit pension plans.

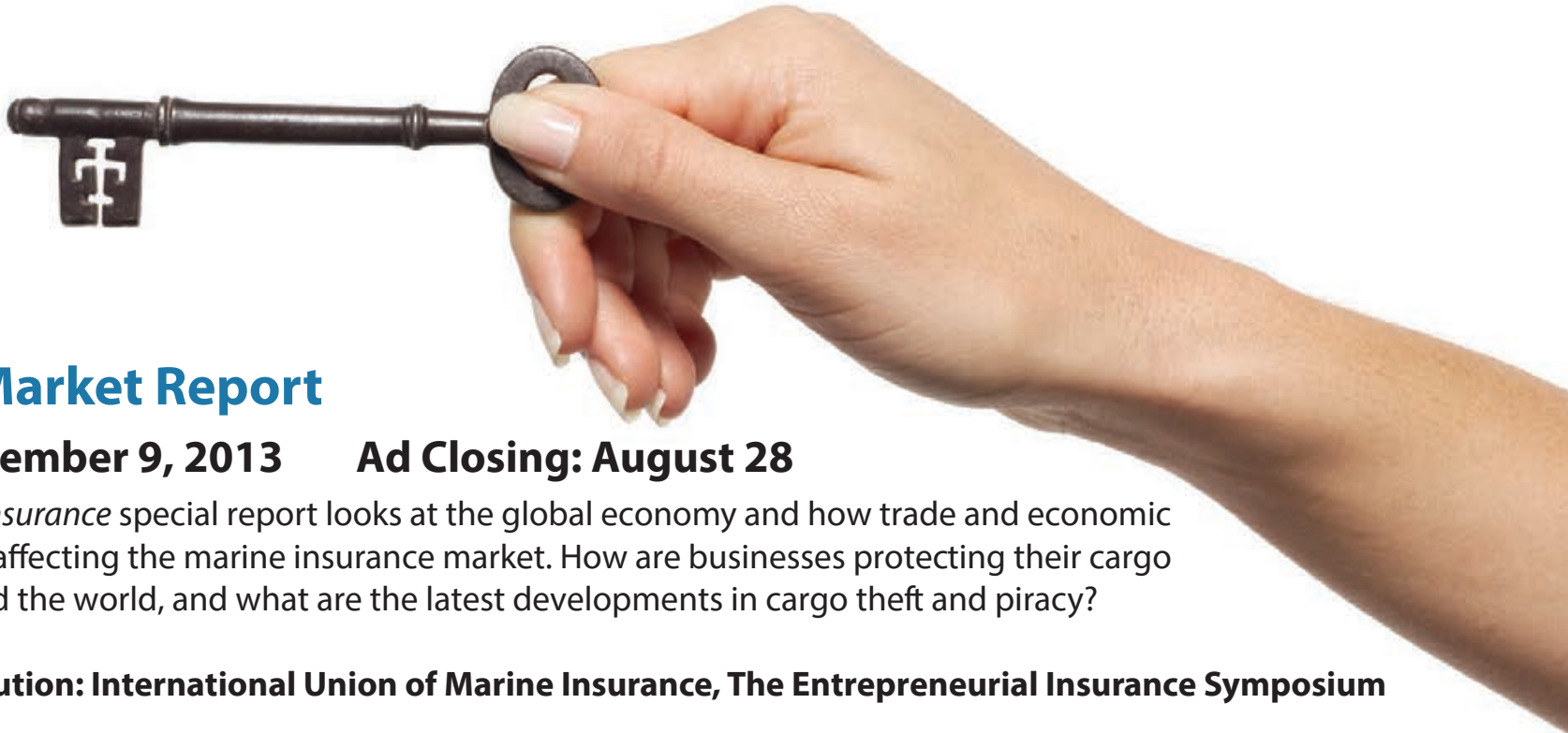
Number of defined benefit plans sponsored by midsize employers\*

Year	Number
2002	4,461
2003	4,238
2004	4,083
2005	3,935
2006	3,850
2007	3,768
2008	3,700
2009	3,534
2010	3,313
2011	3,189

\*For plans with between 250 and 999 participants  
Source: Pension Benefit Guaranty Corp.

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## Marine Market Report

**Issue: September 9, 2013      Ad Closing: August 28**

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**Bonus distribution: International Union of Marine Insurance, The Entrepreneurial Insurance Symposium**

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**September 23, 2013      Ad Closing: September 11**

## Excess & Surplus Lines Report

This *Business Insurance* annual special report looks at the excess and surplus lines market, along with the latest news, key developments and emerging trends for unusual or difficult-to-insure property/casualty risks. Included in this issue are rankings of managing general agents, wholesalers, surplus lines insurers and the state premium lists.

## Trends in Global Risk Management

A host of risks face businesses that open operations outside the United States or work with non-U.S. suppliers. This report will examine differences in the U.S. and European responses to supply chain issues, as well as how companies protect their reputations in a global market.

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## Kane lists \$9.5 million in notes for sale

■ Kane SAC Ltd., a subsidiary of Kane Holdings Ltd., has launched an independent, private catastrophe bond platform and issued \$9.5 million in notes on the Bermuda Stock Exchange. The Series 1-2013 notes represent the first time that a series of notes issued by a segregated accounts company has been listed on the exchange, Kane said in a statement. Kane, a Bermuda-based insurance manager, said in a statement that listing the notes on the Bermuda Stock Exchange in a tradable format would “significantly heighten their overall value to the investment community.”

## Gard CEO Isacson dies at age 57

■ Claes Isacson, CEO of Gard AS, has died at age 57, the company announced. Mr. Isacson was CEO of the Arendal, Norway-based marine insurer for the past 12 years. He died on Aug. 10 after an illness, the company said. “There is no doubt that Gard is the organization it is today because of his leadership and vision,” the company said in a statement. “He will be remembered for his energy, humor, hospitality and zest for life.” Memorial services will be held in Arendal and London in the fall.

## Catastrophes could hike P/C prices in Germany

■ A series of natural catastrophes may push the combined ratio of the German property/casualty insurance industry above 100% for 2013, possibly resulting in rate increases, according to a report by Standard & Poor’s Corp. Severe flooding in June and hailstorms in July are among the highest-ever insured losses of their kind seen in Germany, according to a report. S&P said the events could prompt rate increases to help bolster profitability in the sector in 2014-2015. The rating agency said it maintained a stable outlook on the German property/casualty industry, as most insurers would be able to absorb losses from the recent catastrophes, among other factors.

## SWERMA seeks clarity on Solvency II for captives

■ The Swedish Risk Management Association has written to Sweden’s financial regulator to ask that its application of Solvency II rules take into account the char-

## PROFILE: MALAYSIA

\$3.79  
BILLION

The Malaysian insurance market has experienced significant merger and acquisition activity since new risk-based capital requirements went into effect in 2009. There has been little change, however, in the way business is conducted. Restrictions imposed by fire and motor tariffs have limited innovation. The government is keen to develop Malaysia as a worldwide center for Islamic-compliant insurance and Malaysia has a well-established regulatory and legal environment for takaful.

◀ 2011 P/C premiums

### MARKET SHARE

Category	Share (%)
MOTOR	46.6%
PA & HEALTH CARE WRITTEN BY NON-LIFE COMPANIES	14.3%
PROPERTY	16.4%
MARINE, AVIATION, TRANSIT	10.0%
MISCELLANEOUS	4.5%
SURETY, BONDS & CREDIT	0.3%
LIABILITY	3.0%
WORKERS COMPENSATION & EMPLOYERS LIABILITY	1.3%
CONSTRUCTION & ENGINEERING	3.6%

Source: Axco Global Statistics/Industry Associations and Regulatory Bodies

### COMPULSORY INSURANCE

Several classes of insurance are compulsory, including:

- Motor third-party liability
- Workers compensation
- Professional liability for lawyers, brokers and financial advisers
- Travel insurance for certain bookings
- Foreign workers guarantee
- Oil pollution liability
- Foreign workers travel insurance

### NONADMITTED

Nonadmitted insurance is rarely permitted in Malaysia. Insurance must be purchased from locally authorized insurers except coverage for non-Malaysian-registered ships and aircraft, international marine hull and cargo for policyholders based in certain countries, and personal accident. If coverage is not available locally, the regulator may grant permission to purchase coverage overseas.

### INTERMEDIARIES

Intermediaries must be authorized to place insurance business. There are 34 registered brokers in Malaysia and more than 35,000 registered property/casualty agents. Brokers face stiff penalties for noncompliance with the nation’s rules and laws, including three years’ imprisonment, a nearly \$1 million fine or both. The penalty for any person or company insuring with an unlicensed insurer is about \$160,000.

### MARKET PRACTICE

Insurers and brokers are careful to comply with local rules and laws. Fronting is permitted, but a requirement that the local market be used when possible means there is limited potential for fronted coverage.

**MALAYSIA**

**POPULATION**  
29.6 million

**AREA**  
128,559 square miles

**NUMBER OF INSURERS**  
35

**NUMBER OF TAKAFUL OPERATORS**  
12

### MARKET DEVELOPMENTS

UPDATED JUNE 2013

- Acquisitions of local insurers by foreign insurers continued in 2011 and 2012 with Zurich acquiring Malaysian Assurance Alliance, Tokio Marine buying MUI Continental and South African insurer Sanlam announcing it would take a 49% stake in Pacific & Orient. More deals are expected as regulators encourage higher risk-based capital levels.
- The Financial Services Act 2012 and the Islamic Financial Services Act 2012 consolidated previous insurance legislation. New rules under the laws are expected to enhance supervision and increase penalties for noncompliance.
- The regulator, Bank Negara Malaysia, has announced a gradual revision of the motor tariff effective in 2016, which will be implemented over four years. An increase in rates is expected.
- The fire tariff also is expected to be phased out and a significant decline in property insurance rates is expected.

Information provided by Axco Insurance Information Services.  
[www.axcoinfo.com](http://www.axcoinfo.com)

acteristics of captive insurance companies. While Solvency II rules are designed to be applied using the “principle of proportionality,” SWERMA wrote the regulator calling for clarity about how captives will be treated in Sweden once the Solvency II rules go into effect and take into account the fact that captives typically only cover risks linked to their parent companies. Solvency II, a risk-based capital regime for insurance and reinsurance companies in Europe, likely will go into effect in 2016. There is considerable uncertainty over how captive companies’ need for special treatment will be incorporated into Swedish law, according to the letter written by Fredrik Finnman, chairman of SWERMA and CEO of Assa Abloy Insurance Ltd., and FERMA board members Annika Forsgren, CEO of Insurance AB Gota Lejon, and Ola Nilsson, CEO of SCA Insurance AB.

## JPMorgan China probe sends chill through banks

■ A U.S. banking regulator’s probe into JPMorgan Chase & Co.’s hiring practices in China will have rival banks scrambling to review their own records, lawyers say, in a market where ties to political and business leaders can be key to winning big deals. Banks around the world commonly hire people with government connections, but this is especially prevalent in China due to the role the ruling Communist Party plays in the country’s business. Offering a job to one of China’s so-called princelings — the offspring of China’s political elite — is now a potential liability, with the U.S. Securities and Exchange Commission investigating whether JPMorgan’s Hong Kong office hired the children of China’s state-owned company executives with the

express purpose of winning underwriting business and other contracts, said a person familiar with the matter. U.S. law does not stop companies from hiring politically connected executives. But hiring people in order to win business from relatives can be bribery, and the SEC is investigating JPMorgan’s actions under the U.S. Foreign Corrupt Practices Act, the source said.

Reuters

## Dane Douetil named group CEO of BMS

■ Dane Douetil has been appointed group CEO of BMS Associates, the company announced. BMS Associates is the parent company of brokerages BMS Group Ltd. and BMS Intermediaries Inc., and of Pioneer Underwriting Ltd. Mr. Douetil succeeds Carl Beardmore,

who left BMS in April. Mr. Douetil will begin his role at BMS in early September, the company said. He most recently was CEO of Amsterdam-based Brit Insurance Holdings N.V. He left that role in October 2011 when Brit, which previously had been listed on the London Stock Exchange and based in London, was bought by Achilles Netherlands Holdings B.V.

## Liberty Mutual names Singapore unit leader

Luiz Francisco Campos has been appointed president of Liberty Insurance Singapore, Liberty Mutual Insurance Co. said. Mr. Campos previously was the director of claims for Liberty Mutual’s operation in Brazil and has more than 30 years of insurance experience in the Brazilian market, Liberty Mutual said in a statement.

“Luiz Francisco brings to Singapore the experience and knowledge gained from a successful career in Brazil,” Luciano Suzuki, chief operating officer of Liberty International Asia, said in a statement. “Under his leadership, our Brazilian operations gained better control over claims costs and achieved 30% annual sales growth while opening multiple new branches.” Mr. Campos will be based in Singapore.

## Fonterra withdraws milk powder shipment

■ New Zealand’s Fonterra, the world’s biggest dairy exporter, caught up in a contamination scandal this month, said it was forced to withdraw 42 tonnes (46.3 tons) of milk powder bound for China because of high nitrite levels. Dairy products account for about one-quarter of New Zealand’s export earnings, and China is its biggest buyer of milk powder. The high nitrite levels were first brought up by the official *China Daily* in late July and have dealt another blow to the company after it announced this month that it had found bacteria that could cause food poisoning in some products. Fonterra had to apologize for a milk powder contamination scare in China after contaminated whey protein concentrate had been sold to China, Malaysia, Vietnam, Thailand and Saudi Arabia, and used in products including infant milk powder and sports drinks.

Reuters

## Canada Senate pushes insurance for railways

■ Canada should force railways to take out enough insurance to ensure they can cover damage caused by major incidents, the Senate said in a report issued after last month’s train disaster in Quebec, which killed 47 people. The recommendation was one of 13 in a Senate report on transporting oil and gas by pipelines and rail. The Senate is Canada’s unelected upper house of Parliament. A train operated by Montreal, Maine & Atlantic Railway Corp. derailed and blew up in the Quebec town of Lac-Mégantic on July 6, killing 47 and destroying the town’s downtown. Last week, Canada moved to shut down the railway, saying it did not have enough insurance to pay for the cleanup costs. Under federal regulations in Canada, there is no set minimum or maximum amount of insurance coverage required for rail operators. Coverage is based on a risk assessment carried out by the insurance company and the railway.

Reuters

## China to launch fresh bribery probe: Xinhua

■ China is intensifying its investigation into rampant bribery in the pharmaceutical and medical services sector with a fresh three-month probe, the official Xinhua news agency reported. The investigation by the State Administration for Industry and Commerce, a regulator in charge of market

supervision, is aimed at stamping out bribery, fraud and other anti-competitive practices in various sectors, Xinhua said. It comes as other Chinese regulators such as the National Development and Reform Commission as well as the police conduct multiple investigations into how foreign and domestic companies do business in the world’s second-biggest economy. Much of the focus has been on the pricing of items from medicine to milk powder and whether compa-

nies are violating a 2008 anti-monopoly law.

Reuters

## Runoff specialist Catalina to buy American Safety Re

■ Runoff specialist Catalina Holdings (Bermuda) Ltd. will acquire American Safety Reinsurance Ltd. from Tower Group International Ltd., Catalina announced. American

Safety Re is the Hamilton, Bermuda-based casualty reinsurance subsidiary of American Safety Insurance Holdings Ltd., which is in the process of being acquired by Toronto-based Fairfax Financial Holdings Ltd. In June, Fairfax announced it would buy American Safety and, on completion of that deal, sell American Safety Re to Tower for \$59 million. Catalina will assume Tower’s rights and obligations to American Safety Re under a definitive share purchase agreement.

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EDITORIAL

## BACKGROUND CHECKS NEED CLOSER LOOK

**T**he U.S. Equal Employment Opportunity Commission's policy on criminal background checks has put employers somewhere between the proverbial rock and a hard place. The EEOC is, not unreasonably, concerned about criminal background checks having a disparate effect on minorities.

However, the EEOC has failed to provide clear guidance as to how to proceed on this issue.

And following the EEOC's policy at this point is particularly difficult for large firms, which hire large numbers of workers and must find efficient, economic ways to eliminate potentially dangerous candidates from their pools of applicants.

The EEOC has only hurt its own cause in filing a lawsuit that, as a federal judge has pointed out, presents weak statistical evidence to support its case.

The advice of nine state attorneys general, who have urged the EEOC to reconsider two other lawsuits it has filed on this issue, also deserves to be taken seriously.

In addressing criminal background checks, the EEOC and employers should recognize that there is considerable common ground.

Businesses and the agency, for instance, would agree that a diverse workplace is desirable and that applicants should not have to suffer for what might have been minor youthful indiscretions.

Furthermore, based on the statistical data available, it can be argued convincingly that black youth are, unfairly, more readily arrested and convicted of crimes than their white counterparts and that this injustice should not be perpetuated.

Perhaps most important of all, both sides also would agree about the desirability of maintaining a safe, secure environment for workers and customers.

As experts have pointed out, it is going to take time to develop a policy that is feasible and addresses everyone's concerns.

In the meantime, perhaps the EEOC could tone down its aggressive approach on this issue, as well as clarify areas that remain vague.

It also would be wise for the agency and business interests to proceed by acknowledging that, when all is accounted for, everyone here should be on the same side.

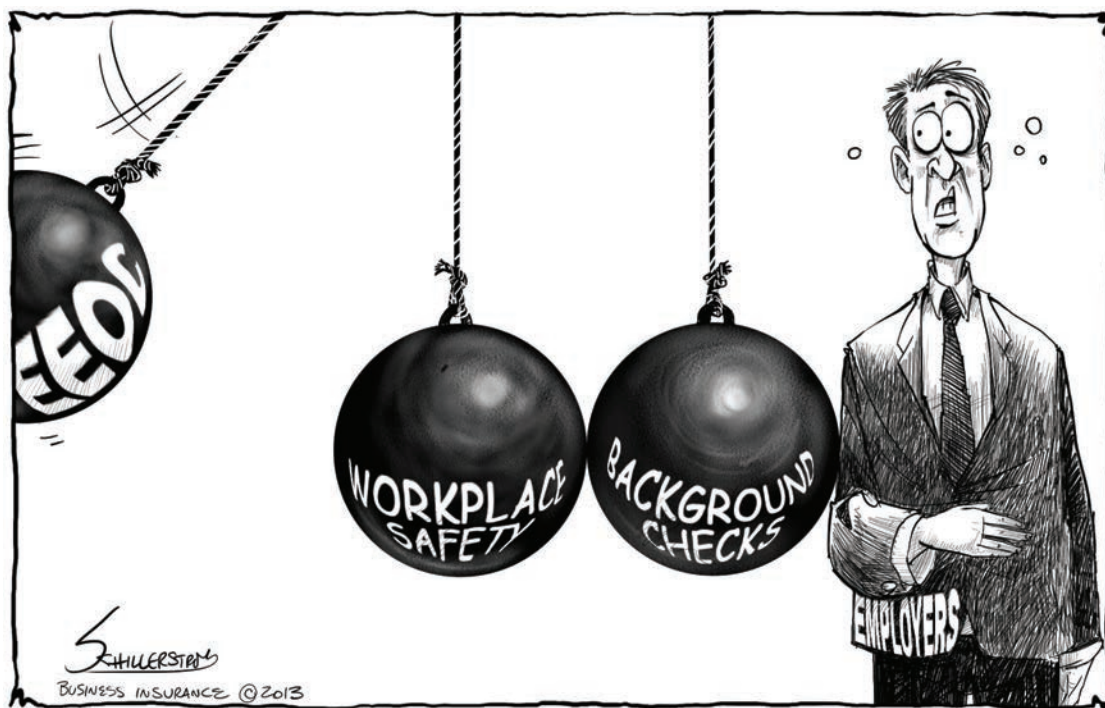
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SCHILLERSTROM



COMMENTARY

## INSURANCE LEGISLATION TOUGH SELL TO THIS CONGRESS

**A**ugust is nearly over, and Congress is gone. Not much in the way of risk management and insurance matters got resolved before lawmakers took their annual summer break — hardly surprising, given that congressional attention has been focused on Obamacare. There's also talk in some quarters of shutting down the government, a tactic that backfired in the 1990s.

When lawmakers get back, they're going to have an extremely tight window of opportunity to deal with issues of interest to risk managers, brokers and insurers.

If it seems like you've read this column before, you probably have, in part because issues go unresolved Congress after Congress. But with acrimony so bitter and off-year elections looming next November, lawmakers may simply decide to throw in the towel next year absent a major domestic or foreign crisis.

Probably the easiest insurance-related issue to get off the table is the National Association of Registered Agents and Brokers Reform Act of 2013, which would create a streamlined system for interstate agency and broker licenses. Nobody's going to say the bill's perfect, but it enjoys support across the insurance industry spectrum, including that of the National Association of Insurance Commissioners.

This should be a no-brainer, right? But odds are many industries have what they consider no-brainer bills before Congress. There's only so much legislative oxygen on Capitol Hill, and for it to become law, NARAB II's supporters will have to make sure it doesn't become lost in the shuffle.

Another measure that has drawn support across the



**MARK A. HOFMANN**

SENIOR EDITOR

industry that deserves not to get lost in the shuffle is legislation that would extend the federal government's terrorism insurance backstop program. The program, created in the wake of the Sept. 11, 2001, terrorist attacks on New York's World Trade Center and elsewhere, is slated to expire at the end of next year. It already has been extended twice.

Supporters of the program have launched a campaign to extend it in order to make sure that it's on the legislative radar long before it expires. But supporters admit extending it again will be no easy task. The Obama administration doesn't support the program. The Consumer Federation of America has been vocal in its opposition. And there's always a chance some lawmakers from the tea party wing of the Republican Party will weigh in against extending the program by arguing that it's an unnecessary federal intrusion into the private market.

Another issue that could come up is changing the taxation of certain offshore reinsurance transactions. This one has divided the insurance industry, and Congress traditionally has hesitated to wade into any issue that doesn't have widespread industry support regardless of what industry's involved.

Given the House majority's skepticism over new taxes of any kind, odds don't favor congressional action this time around.

SPECIAL  
REPORT

Insurer &amp; Reinsurer

Capital Management

Insurers adopt  
new tactics of  
capital management

PAGE 15

Array of alternative  
capital options for  
reinsurance buyers

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## NEW PLAYERS, NOVEL APPROACHES

Investor demand spurs alternative financing sources to compete against traditional reinsurers

BY BILL KENEALY AND CHRISTINE WILLIAMSON

**S**tronger demand for insurance-linked securities is putting pressure on traditional reinsurers, spurring innovation as reinsurers and brokers develop novel investment structures for institutional investors and the hedge fund managers who invest on their behalf.

This surge in insurance-linked securities is evident in the increased issuance of catastrophe bonds. According to a Swiss Re Ltd. report released in July, the total value of outstanding catastrophe bonds as of July 1 was \$17.1 billion, exceeding the previous full-year record of \$17 billion set in 2007 in the aftermath of Hurricane Katrina.

Unlike the upswing in the catastrophe bond market after Katrina, however, market dynamics now are being driven by investor demand from a variety of new sources, most notably insti-

tutional investors and traditional money managers.

"Everything is changing in the insurance-linked securities market, from the size of deals to the players involved," said Tim Faries, a partner in the insurance group at Appleby Global Group Services Ltd., a Hamilton, Bermuda-based financial services firm that advises on insurance-linked securities.

"Historically, our market was dominated by single-strategy hedge funds," said Judith Klugman, head of insurance-linked securities distribution and sales for Swiss Re. "They have been extremely successful and still make up a big percentage of our market, but that is beginning to shift as more generalist money managers take an interest."

The mix of institutional

See **SECURITIES** next page

"Everything is changing in the insurance-linked securities market, from the size of deals to the players involved."

Tim Faries,  
Appleby Global Group  
Services Ltd.



## SECURITIES

Continued from previous page

investors investing in catastrophe bonds and other securities linked to insurance now includes more pension funds, endowments and sovereign wealth funds.

“What we’ve seen is that pension funds have largely been behind the capital that has continued to flow into the market,” said Chicago-based Paul Schultz, CEO of Aon Benfield Securities.

Institutional investors increasingly have become enamored with insurance-linked investment strategies because catastrophe bond annual investment returns tend to fall in a range between 7% and 8%, topping ho-hum returns of traditional fixed-income securities in a low interest-rate environment — and they are uncorrelated with financial markets. The biggest investment area for institutions and hedge funds has been catastrophe bonds, by far the largest segment of insurance-linked securities, but there are other investments such as industry loss warrants and sidecars.

Increased transparency and education, as well as structural changes, have increased investor and issuer comfort with insurance-linked securities, sources said.

For example, a higher percentage of catastrophe bonds now use indemnity triggers, based on the losses suffered by the bond issuer and have gained popularity at the expense of both parametric triggers, which rely on measures such as wind speed to trigger the bond and indexed triggers, based on an industrywide index of losses, Ms. Klugman said.

“What we are finding is that as our investors have become more sophisticated, there is a greater acceptance of indemnity triggers,” she said.

Two of the most recent institutional investors to jump into insur-

ance-linked securities are:

- The \$13.2 billion West Virginia Investment Management Board, Charleston, which invested \$40 million in Chicago-based Elementum Advisors L.L.C.’s specialist catastrophe reinsurance hedge fund; and

- The 23 billion New Zealand dollar (\$18 billion) New Zealand Superannuation Fund, Auckland, which committed up to \$275 million in London-based Leadenhall Capital Partners L.L.P.’s property catastrophe hedge fund, having previously invested \$250 million in 2010 in Elementum’s hedge fund.

On a short-term basis, Aon Benfield’s Mr. Schultz said demand for catastrophe bonds has experienced ebbs and flows.

“In the early part of the year, there was significantly more capital looking to be deployed than transactions coming to market. Since then, we’ve seen a healthy stream of issuances, and supply and demand is now about the same,” Mr. Schultz said.

Aside from the New Zealand Superannuation Fund’s outsized \$500 million investment, most institutional reinsurance allocations are fairly small, in the \$30 million to \$50 million range, sources said.

Over the long haul, the aggregation of even such small investments has the potential to crowd out the traditional sources of reinsurance market capital, sources said.

Currently, only 15% of the total \$300 billion property catastrophe reinsurance market now is from nonreinsurance industry sources known in the industry as “alternative capital,” according to an estimate by Goldman Sachs Global Investment Research in its “The Search for Creative Destruction” report distributed Aug. 7. However, if pension funds with an estimated \$2 trillion of aggregate assets allocated just 50 basis points of their funds to property catastrophe investments, the resulting \$100

## TOP CONCERNS AMONG INSURERS

In a global survey, insurers were asked which of the following trends they think will have the most significant effect on their business in the next two years and in the next five years.

TREND	NEXT 2 YEARS	NEXT 5 YEARS
Capital management challenges from sustained low interest rates	66%	38%
Increased regulatory and legislative restraints	61%	47%
Volatile economic environment	50%	44%
Increased role of advanced technology such as big data	26%	35%
Increasing number of extreme weather events	23%	25%
Talent attraction and retention	21%	24%
Shifting demographics	19%	40%
Increasing power of consumers due to social media	15%	21%
Demand for insurance in emerging markets	11%	15%
Geopolitical instability around the world	9%	11%

Source: 2013 Insurance Megatrends Survey, Towers Watson & Co.

billion would be more than double the existing amount of alternative capital in the reinsurance industry, according to the report.

“The total amount of pension fund assets so dwarfs the size of the whole reinsurance industry. Even a small fraction of those trillions would completely swamp the reinsurance industry,” said Michael Luft, managing director and consultant for insurance-linked securities at investment consultant Rocaton Investment Advisors L.L.C., Norwalk, Conn.

The volume of new capital flowing into their reinsurance space already has altered the supply/demand dynamic and driven the cost of issuing bonds down relative to traditional reinsurance, said David Foley, global practice leader of actuarial and advanced analytics for Deloitte Consulting L.L.P.

“The frictional cost of catastrophe bonds is falling,” Mr. Foley said. “So even from a price standpoint, they are becoming competitive with traditional reinsurance.”

This diminishing price differen-

tial has prompted differing reactions from reinsurers.

“Some traditional reinsurance players are following the adage of ‘If you can’t beat ‘em, join ‘em’ and investing in building teams that are capital markets desks,” Appleby’s Mr. Faries said.

Conversely, during a July conference call with equity analysts, Evan Greenberg, CEO of Zurich-based insurer and reinsurer Ace Ltd., said his insurance company was being more selective about writing reinsurance as the influx of alternative capital has exerted downward pressure on rates, especially in catastrophe-exposed regions.

“You see alternate capital coming in, capital markets in addition to traditional players,” Mr. Greenberg said. “So you’ve got that pond, with more drinking out of it.”

*Bill Kenealy is an associate editor at Business Insurance; Christine Williamson is a senior reporter at sister publication Pensions & Investments.*

## Cat bonds expand into new perils

While the market for catastrophe bonds has long centered on risks from storms during the Atlantic hurricane season, it is increasingly embracing new perils.

Bill Dubinsky, New York-based head of insurance-linked securities at Willis Group Holdings P.L.C.’s capital markets and adviser group, said he sees opportunities for catastrophe bonds to play a bigger role in areas where insurance penetration is low or sufficient limits are unavailable, citing coverage for California earthquake risk as prime example.

“In California, you have a very limited pickup rate for large individual insureds, some of whom have multibillion-dollar exposures,” he said. “So there’s a lot of room for expansion just within natural catastrophe.”

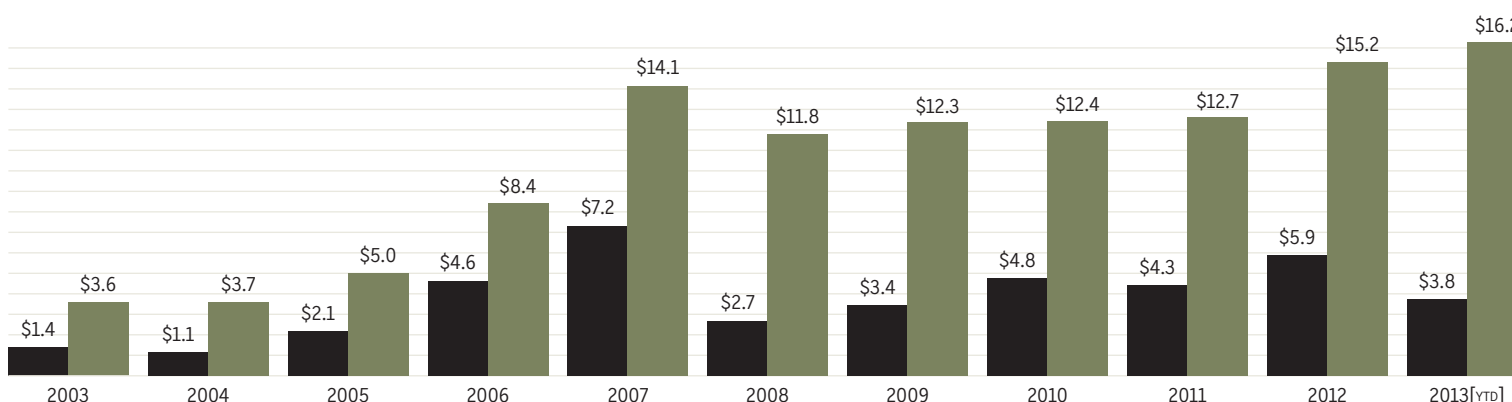
Moreover, Mr. Dubinsky said that some recent catastrophe bonds have contained coverage for disparate perils. The Queen Street VIII Re catastrophe bond completed by Munich Reinsurance Co. in July, for example, covers both U.S. hurricane risk and Australian cyclone risk.

“You are starting to see growth in new natural catastrophe perils and more multiperil transactions,” he said. “The economics of including things on a multiperil basis are much more appealing than on a standalone basis.”

By Bill Kenealy

## CATASTROPHE BOND VOLUMES BY YEAR

Issued capacity and capacity outstanding at year end, in billions of dollars



Source: Willis Capital Markets & Advisory

# REGULATORY MANDATES FORCE INSURERS TO ADOPT NEW CAPITAL MANAGEMENT STRATEGIES

European insurers led the way because of Solvency II; now others around the world follow

BY JUDY GREENWALD

Regulatory and rating agency pressures are causing many insurers to turn to capital management strategies, including enterprise risk management, to manage their capital. They are making good progress in this area and experts think these new approaches ultimately will benefit the insurers.

Two of the prods toward development of capital management strategies by insurers are Solvency II and the National Association of Insurance Commissioners' Risk Management and Own Risk and Solvency Assessment Model Act.

Rating agencies are encouraging its use as well, experts say.

"Every rating agency has a required capital model that's typically risk-based to some extent,"

said Don Mango, vice chairman and head of enterprise analytics for New York-based Guy Carpenter & Co. L.L.C.

Typically, insurers with good ratings from the rating agencies have "more than enough capital to satisfy the regulators," he said.

"Insurers' capital modeling has been around the market for probably 15 years, but over that time the use has been growing," partly because of regulatory pressure, said David Simmons, London-based managing director with Willis Group Holdings P.L.C.'s Willis Re unit and head of its strategic capital and results management operation.

A lot of capital management started in Europe, "primarily driven by Solvency II and the changing regulatory environment in Europe," said Stephen M. Sonlin,

head of risk and capital management solutions at Hartford, Conn.-based Conning & Co.

As a result, large European companies "have been at the forefront" in this development, "but it's being followed up pretty much across the globe," Mr. Sonlin said. While it has been adopted more by larger, more complex companies, it is "moving down pretty rapidly" in terms of company size as it becomes more of a widespread requirement, he said.

Louis DiFranco, head of the insurance business at Pasadena, Calif.-based Western Asset Management Co., said enterprise risk management "goes way beyond capital risk lots of times" and can include factors such as underwriting, the competitive landscape and product development.

Zurich North America's econom-

ic capital model encompasses multiple tools and techniques to quantify and aggregate risk from all sources, including premium, reserving, mortality and natural or man-made catastrophe data; market risk, including investment and asset/liability matching; credit risk, including investments and reinsurance; and operational and business risks, said Barry Franklin, Schaumburg, Ill.-based senior vice president and chief risk officer for the insurer.

"We have a very well-developed economic capital model that really encompasses a 360-degree view of risk," Mr. Franklin said. The insurer has "been able to weather the storm quite effectively when you look back to the most recent finan-

"Insurers' capital modeling has been around the market for probably 15 years, but over that time the use has been growing," partly because of regulatory pressure.

David Simmons,  
Willis Group Holdings  
P.L.C.

See **INSURERS** next page

## CAPTIVES IN THE GLOBAL ECONOMY

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# Comparing Solvency II and NAIC guidelines

## European and U.S. rules differ

While Solvency II and the National Association of Insurance Commissioners' Own Risk and Solvency Assessment requirement are encouraging insurers to address capital management issues, there are some significant differences between the two.

Solvency II has a slated start date of January 2014 but is expected to be delayed. The NAIC's Risk Management and Own Risk and Solvency Assessment Model Act, which was adopted in 2011, has an effective date of Jan. 1, 2015.

Don Mango, vice chairman and head of enterprise analytics for New York-based Guy Carpenter & Co. L.L.C., said Solvency II has a three-pillar framework: Insurers must have a strong enterprise risk management function; a capital model of their operations; and disclosure rules for key stakeholders, the public and the regulators.

ORSA "is more tailored to the U.S. marketplace," where there already was more disclosure of information through the yellow books — the annual reporting forms insurers submit to state regulators — and where there is "not such a big leap" as there is for European insurers in terms of disclosing information, he said.

"Solvency II does impose capital requirements that are new and imposed at a fairly high safety level" whereas in the United States, "they're not imposing any change in capital requirements. They're simply asking for companies to share what their own risk and solvency assessments are," said Maryellen J. Coggins, Boston-based managing director with PricewaterhouseCoopers L.L.P.'s insurance practice.

Solvency II is "very robust in terms of considering the main different risks inherent in insurance companies," said Louis DiFranco, head of the insurance business at Pasade-

na, Calif.-based Western Asset Management Co. ORSA is "more about documenting how a company thinks about its risk," more so than specifically promulgating what the risks are, he said.

ORSA basically has companies "do a self-assessment about various factors associated with the risk and report on them," Mr. DiFranco said. It is "very different than the idea of Solvency II, which is actually computing how much capital needs to be set aside."

Stephen M. Sonlin, head of risk and capital management solutions at Hartford, Conn.-based Conning & Co., said the ORSA requirements are "much less prescriptive, and give a much wider latitude to comply with the regulatory requirements (insurers) need to report against."

"I think the U.S. will eventually get Solvency II equivalency of some sort," said James Auden, managing director of insurance for Fitch Ratings Inc. in Chicago.

Meanwhile, Michael Murray, Jersey City, N.J.-based assistant vice president for financial analysis at Insurance Services Office Inc., said that beyond the U.S. and Europe, other jurisdictions that "perhaps lack the resources to develop their own regulations" may adopt the Basel, Switzerland-based International Association of Insurance Supervisors' Insurance Principals, Standards Guidance and Assessment Methodology, which was first released in October 2011 and amended in October 2012.

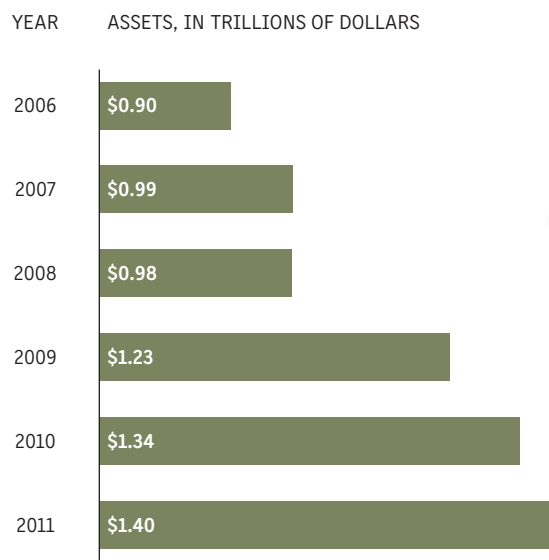
This document specifies the "best practices in insurance management" and what insurers should be doing to assure regulators they are practicing sound enterprise risk management, Mr. Murray said.

The Basel group represents more than 200 jurisdictions in close to 140 countries.

By Judy Greenwald

## INSURERS OUTSOURCING CAPITAL MANAGEMENT

Since 2006, insurers have been farming out more of the capital management of their assets to third parties.



Source: Insurance Asset Management Annual Survey, 2012, Patpatia & Associates Inc.

## INSURERS

Continued from previous page

cial crisis. While we experienced some losses, just as anybody would, we did construct our asset portfolio with an eye towards managing risk, so we were able to avoid the degree of investment losses that some others experienced."

"There's a lot more enterprise risk management and risk focus today" as insurers "look at their various businesses and what sort of capital they need to support that risk," said James Auden, managing director of insurance for Fitch Ratings Inc. in Chicago. "I think companies have gotten better at managing their concentrations of exposure over time."

"Most insurers at this point in time have adopted some element of enterprise risk management," although "some of it more formally than others," said Laurie Champion, Atlanta-based managing director of Aon Global Risk Consulting's enterprise risk management practice.

Insurers these days are "really looking at the breadth of their current risk management efforts" and "looking at all types of risk" on a broader ERM basis, she said.

Overall, the industry, which has been proactive in managing risk, "did pretty well during the financial crisis," said Cliff Gallant, San Francisco-based managing director and senior analyst with Nomura Holdings Inc.

However, John Wicher of San Francisco-based Wicher & Associates, said many insurers "still are struggling with trying to under-

stand where risks correlate." An example, he said, would be the Sept. 11, 2001, terrorist attacks, when "no one really thought about" the aggregation of exposures for companies, which included business interruption, workers compensation and disability.

Carmi Margalit, director at rating agency Standard & Poor's Corp. in New York, said, "We cover several hundred insurers, and I think within that universe there's a wide spectrum of companies in terms of how far along they are in implementation of various

*"There's a lot more enterprise risk management and risk focus today" as insurers "look at their various businesses and what sort of capital they need to support that risk."*

James Auden, Fitch Ratings Inc.

(capital management) frameworks."

Mr. Wicher said he thinks intuitively that "larger companies have been thinking about this issue and some in a very elegant way for a number of years, certainly since 9/11."

"Smaller companies have fewer resources" and "don't necessarily have the resources available internally" to develop these models, "particularly if you're looking at smaller, regional mutual companies," Mr. Wicher said.

But Mr. Mango said that special-

ty midsize regional companies with big enough staffs may be further along in the process of developing capital models.

However, many of the global insurers also "have done really well — surprisingly well, given their size — at getting a model and having input from all the necessary parties and sharing the output with their boards on a regular basis," Mr. Mango said.

He said one development he has seen are supporting models that are more flexible "in terms of being able to respond in short time frames for more strategic opportunities and decisions," such as an acquisition, "where the larger model can't just sort of turn on a dime and be adopted quickly."

"You sacrifice a little bit of accuracy," but these secondary models can "give directional guidance in a timely manner, and that's really valuable," Mr. Mango said.

Insurers will benefit from all of this, experts say. A lot of benefits have "come from the creation of processes to unify" all the disparate sources of risk information, Mr. Mango said.

"Capital management decision-making certainly will be enhanced because of these new sources of information," although it will take time "to absorb and understand, so there's still a maturing that needs to happen," said Maryellen J. Coggins, Boston-based managing director with PricewaterhouseCoopers L.L.P.'s insurance practice.

Mr. Sonlin agreed.

The move toward capital modeling "is going to create better profitability and greater opportunities for the companies" that have these processes in place, he said.



# EXPANDING ALTERNATIVE CAPITAL SOURCES GIVE REINSURANCE BUYERS MANY OPTIONS

Nontraditional, insurance-linked securities markets trigger inventive securitization choices

BY SARAH VEYSEY

An influx of third-party capital and improved comfort with nontraditional forms of reinsurance coverage mean that reinsurance buyers have greater flexibility and choice when putting together their programs.

Reinsurance buyers increasingly are seeking to access alternative forms of capital and using instruments such as catastrophe bonds and industry loss warranties as part of their overall reinsurance programs.

And the availability of third-party capital also is prompting competition in traditional reinsurance markets, enabling buyers to better tailor their coverage, experts say.

Insurance-linked securities markets are now more competitive, particularly for aggregate facilities using products such as cat bonds and structured industry loss warranties, said Des Potter, Europe, Middle East and Africa head at GC Securities, a unit of Guy Carpenter & Co. L.L.C., in London.

For large buyers of reinsurance, alternative forms of reinsurance coverage are attractive because they like “a diversity of risk-transfer tools,” Martyn Street, a director at Fitch Ratings Ltd. in London, said.

In addition, he said, risk-based capital regulation such as the upcoming Solvency II rules for insurers and reinsurers in Europe likely will mean that buyers of reinsurance will show increased interest in different forms of reinsurance, as a means to receive capital relief under their models.

And corporate insurance buyers are monitoring the reinsurance security of their insurance carriers, experts say.

The increased supply of reinsurance vehicles backed by private equity, hedge fund or pension fund capital has meant the pricing for the instruments offered by these vehicles has fallen during the past couple of years, said Simon Buxton, global head of reinsurance for Allianz Global Corporate & Specialty in London.

“Industry loss warranties, cat bonds and insurance-linked securities are becoming more popular,” he said. “This is because this is where prices have fallen the most.”

Allianz Global Corporate & Specialty buys its catastrophe program from Allianz Re, the dedicated reinsurer of Allianz S.E., which uses instruments such as loss warranties, cat bonds and other insurance-linked securities, he said.

There has been an increase this year in reinsurance buyers seeking to use capital markets instruments, particularly catastrophe bonds, as part of their program, said Dennis Sugrue, a director at Standard & Poor’s Corp. in London.

Cat bond issuance is expected to reach about \$5 billion to \$6 billion this year, he said, which would be the highest level of issuance since Hurricane Katrina struck the U.S. in 2005.

“In 2013, we have undoubtedly witnessed

a step change in buyer habits when it comes to making greater use of third-party capital instruments,” said Matt Fitzgerald, managing director of reinsurance at Arthur J. Gallagher & Co. in London.

For example, he said, the \$200 million MetroCat Re Ltd. catastrophe bond purchased in July by the New York Metropolitan Transport Authority to cover storm surge risk demonstrates the greater flexibility, availability and affordability of such instruments compared with a few years ago.



## TYPES OF INSURANCE-LINKED SECURITIES

### Catastrophe bonds

Used by reinsurers to transfer a specified set of risks to the capital markets. Reinsurers issue bonds via an investment bank that are sold to investors, typically via a special-purpose vehicle. Investors collect on the bond, if it is not triggered by a specified event, for example a hurricane or earthquake. If the bond is triggered, then the principal is paid to the sponsor, the insurer or reinsurer.

### Industry-loss warranties

The buyer purchases protection based upon the total industry loss from an event rather than from just its own losses. Buyers pay premium to an underwriter, usually a reinsurer or hedge fund, and receive protection up to an agreed limit if an industrywide loss exceeds the trigger. These warranties also can be bought for events that already have occurred but for which industrywide losses are not yet known.

### Proportional reinsurance

One or more reinsurers take a percentage share of each policy underwritten by the buyer.

### Excess of loss

The buyer pays a claim up to an agreed limit, after which the reinsurer pays the claim above that and up to a specified limit.

### Facultative reinsurance

Covers an individual risk within a cedent’s portfolio and typically is negotiated separately from the rest of the treaty.

“This is the first time the MTA has used the insurance-linked securities markets, which goes to illustrate how the more freely available and considerably cheaper alternative of third-party capital is not only influencing reinsurance but also insurance buying habits,” Mr. Fitzgerald said.

Many reinsurance buyers are tapping alternative sources of capital for their reinsurance coverage, sources said.

For U.S. catastrophe risk, about 40% of buyers “are now buying their reinsurance from nontraditional markets,” Mr. Fitzgerald said.

Capital markets are becoming more inventive in how they create products, Mr. Fitzgerald said, making them more attractive to buyers.

For example, he said, “moves to cover all named storms rather than just hurricanes or the inclusion of variable resets for key factors like attachment points” are making the coverage offered by third-party capital products more flexible and attractive to buyers.

The risk appetite of buyers and the “strategic purchase of reinsurance is becoming more sophisticated,” said James Vickers, chairman of Willis Re International, a unit of London-based Willis Group Holdings P.L.C.

Once cedents have decided how much capacity they need to buy, the abundance of third-party capital is “giving them more flexibility on how they manage that,” he said.

Specialty underwriters typically are able to be opportunistic about their reinsurance purchases, while larger companies that are concerned about the long-term sustainability of their reinsurance programs generally take longer to alter the makeup of their reinsurance program, he said.

However, such buyers have been able to use the presence of third-party capital as a bargaining tool with traditional reinsurers to achieve more favorable rates or terms and conditions, he said.

This is particularly pronounced for natural catastrophe-based coverages — the area where alternative capital instruments are the most well-established, Gallagher’s Mr. Fitzgerald said.

For example, Mr. Vickers said, rates for many buyers fell significantly at the June 1 Florida renewals, in part because of increased competition for traditional reinsurers from nontraditional capacity.

Mark Bernacki, London-based leader of the property team at Dublin-based Beazley P.L.C., said that during recent negotiations for his company’s catastrophe reinsurance coverage, it benefitted from increased competition from third-party capital by being able to combine two catastrophe reinsurance towers — one written at Lloyd’s of London and one written in the United States — into one.

This resulted in “significant cost savings and provided additional flexibility,” he said.

## Insurance buyers assess reinsurance

The extent to which their insurers use nontraditional reinsurance instruments as part of their overall program is something that corporate buyers of insurance are beginning to monitor more closely, experts say.

Corporate clients need to be assured that their insurers are not overly reliant on nontraditional forms of coverage, said Dennis Sugrue, a director with Standard & Poor’s Corp. in London. Dependency on nontraditional capacity may mean that insurers are not able to obtain all the coverage they require, and any additional costs associated with this may be passed on to the insurance buyers, he said.

“Corporate clients do not necessarily need to know very much about the reinsurance protection that their insurer buys,” said Simon Buxton, global head of reinsurance for Allianz Global Corporate & Specialty in London. “However, they do need to know about the financial strength and security of their insurer in order to feel comfortable buying their insurance products.”

This is more usually signaled by rating agencies, Mr. Buxton said. “Reinsurance effectively is just another form of capital that an insurer uses to help maintain a strong financial rating,” he said.

Typically, if insurance buyers use rating agency data to assess their insurance providers, they should be comfortable about the quality of nontraditional forms of reinsurance coverage being used by those insurers because rating agencies assess counterparty risk, among other things, said James Vickers, chairman of Willis Re International, a unit of London-based Willis Group Holdings P.L.C. “The question for really large corporate insurance buyers is, ‘Can some of their peak risks be transferred to the capital markets?’”

By Sarah Veysey

### WORLD'S LARGEST REINSURERS

Ranking based on 2012 net premiums written

Rank	Company	Headquarters	Phone/website	% change	2012 net P/C reinsurance written premiums	% change	2012 combined ratio	2012 employees	Principal officers
1	Munich Reinsurance Co. <sup>1</sup>	Munich	49-89-3891-0 www.munichre.com	11.7%	\$21,954,488,000	8.0%	91.0%	45,437	Nikolaus von Bomhard, chairman and CEO
2	Swiss Re Ltd. <sup>1</sup>	Zurich	41-43-285-2121 www.swissre.com	10.8%	\$15,028,992,000	10.3%	83.1%	11,193	Walter B. Kielholz, chairman; Michel M. Liès, CEO
3	Hannover Re Group <sup>1</sup>	Hanover	49-511-5604-0 www.hannoverre.com	14.0%	\$10,015,350,000	29.7%	95.8%	2,300	Ulrich Wallin, chairman and CEO
4	Lloyd's of London <sup>2</sup>	London	44-207-327-1000 www.lloyds.com	4.1%	\$11,088,154,000	4.0%	91.0%	752	John Nelson, chairman; Richard Ward, CEO
5	Berkshire Hathaway Reinsurance Group	Stamford, Conn.	203-363-5200 www.berkshire-hathaway.com	6.6%	\$10,162,000,000	6.6%	96.8%	N/A	Ajit Jain, president
6	Scor S.E. <sup>3</sup>	Paris	33-1-58-44-7000 www.scor.com	1.1%	\$5,078,000,000	9.2%	93.9%	1,416	Denis Kessler, chairman and CEO
7	PartnerRe Ltd.	Pembroke	441-292-0888 www.partnerre.com	1.9%	\$3,795,473,800	3.2%	87.8%	1,217	Costas Miranthis, president and CEO
8	Everest Re Group Ltd.	Hamilton	441-295-0006 www.everestre.com	(0.7%)	\$4,081,071,000	(0.7%)	93.8%	1,000	Joseph V. Taranto, chairman and CEO
9	Transatlantic Holdings Inc. <sup>3</sup>	New York	212-365-2200 www.transre.com	3.3%	\$3,986,101,000	3.3%	93.5%	620	Robert F. Orlich, chairman, president and CEO
10	Korean Reinsurance Co. <sup>4</sup>	Seoul	82-2-3702-6000 www.koreanre.co.kr	7.7%	\$2,726,858,400	7.6%	98.4%	N/A	Hyuk-Hee Won, chairman; Jong-Gyu Won, CEO

<sup>1</sup> Euro = \$1.3175. <sup>2</sup> British pound = \$1.6181. <sup>3</sup> BI estimate based on information from Global Reinsurance Highlights 2012, Standard & Poor's Corp.; and Global Reinsurance: Market Review, 2012, A.M. Best Co. Inc. <sup>4</sup> Fiscal year ending March 31. N/A Not available

Source: BI survey, except where noted

### PREMIUM GROWTH

Net reinsurance premiums written by the top 10 reinsurers, in billions of dollars

Year	Premiums
2002	\$88.60
2003	\$99.80
2004	\$98.10
2005	\$97.80
2006	\$97.40
2007	\$101.70
2008	\$108.90
2009	\$112.20
2010 <sup>1</sup>	\$114.60
2011 <sup>1</sup>	\$117.80
2012	\$123.90

<sup>1</sup> Global Reinsurance Highlights 2012, Standard & Poor's Corp.; Global Reinsurance: Market Review, 2012, A.M. Best Co. Inc.

Source: BI survey except 2010 and 2011

### GLOBAL REINSURANCE SIDECAR FORMATIONS, 2011-2013

In millions of dollars

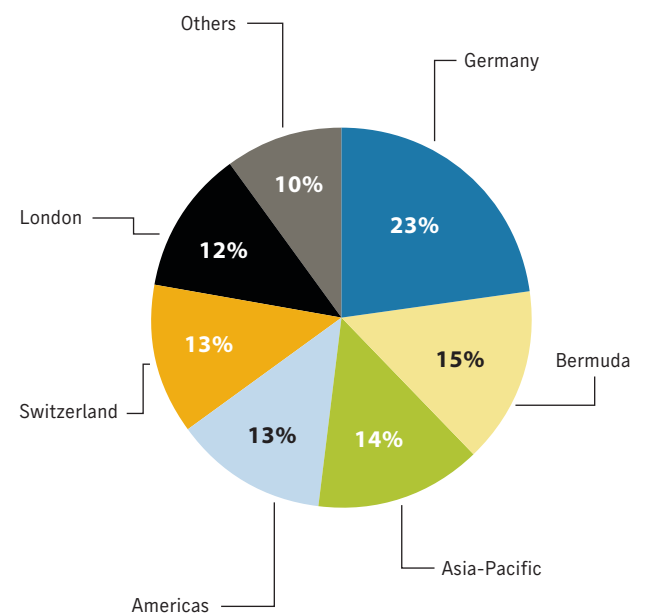
Sidecar	Estimated capital raised	Reinsurer sponsor	Sidecar	Estimated capital raised	Reinsurer sponsor
<b>2012</b>					
			Upsilon Re	\$100.00	RenaissanceRe Holdings Ltd.
			Timicuan III	\$55.00	RenaissanceRe Holdings Ltd.
			AlphaCat Re	\$70.00	Validus Holdings Ltd./outside investors
			New Point V	\$210.00	Alterra Capital Holdings Ltd./outside investors
			Accordion Re	\$250.00	Lancashire Holdings Ltd./outside investors
			Blue Water	\$200.00	Montpelier Re Holdings Ltd.
			PaCR <sup>1</sup>	\$500.00	Validus Holdings Ltd./outside investors
<b>2013 YTD</b>					
			Altair Re	\$95.00	Ace Ltd.
			Mt. Logan Re	\$250.00	Everest Re Group Ltd.
			Lorenz Re	\$75.00	PartnerRe Ltd.
			AlphaCat 2013	\$230.00	Validus Holdings Ltd.
			Upsilon Re II	\$185.00	Harambee Re/RenaissanceRe Holdings Ltd.

<sup>1</sup> A class 4 reinsurer

Source: Company press releases, A.M. Best Co. Inc., Fitch Ratings Inc., Bermuda Insurance Market

### GLOBAL REINSURANCE

Property/casualty gross written premium by reinsurance market



Source: Global Reinsurance Market Review 2012, A.M. Best Co. Inc.

SPECIAL  
REPORT

## Industry Financials

## Mid-year Results

Brokers see strong first-half growth, favorable rates

PAGE 20

Medical costs control helps health insurers increase profits

PAGE 22



## FAST OFF THE BLOCKS

Insurers see strong first half, remainder of year uncertain

BY MARK A. HOFMANN

**C**ommercial property/casualty insurers enjoyed generally favorable first-half results, although how long that benign environment will last is far from certain, according to market observers.

Insurers' performance benefited from low catastrophe losses, particularly in the first quarter, and continued modest rate increases. Yet catastrophe losses picked up in the second

quarter even as rate increases appeared to be decelerating. And there remains the wild card of increasing interest rates (see story, page 20).

For a group of 10 major commercial property/casualty insurers, net income rose dramatically in the first half of 2013 compared with the same period a year earlier, increasing an average of 23.3%. The group's combined ratio also improved to 95%

See **INSURERS** next page

**PROPERTY/CASUALTY INSURERS' FIRST-HALF 2013 RESULTS**

Largest U.S.-based and -listed commercial property/casualty insurers that report quarterly results. Ranked by net premiums written, in millions of dollars.

Insurer	Net premiums written 2013	% increase (decrease)	Net income 2013	% increase (decrease)	Combined ratio 2013*
American International Group Inc.	\$17,700	(1.2)	\$494	(10.9%)	100
Liberty Mutual Insurance Co.	\$17,486	6.5%	\$766	28.1%	99.9
The Travelers Cos. Inc.	\$11,421	0.5%	\$1,821	39.5%	91.4
Ace Ltd.	\$8,189	6.3%	\$1,844	41.7%	88.1
Chubb Corp.	\$6,157	1.8%	\$1,235	35.7%	86.7
The Hartford Financial Services Group Inc.	\$5,024	0.1%	(\$431)	N/M	96.2
XL Group P.L.C.	\$3,642	4.8%	\$662	51.3%	90.8
CNA Financial Corp.	\$3,564	7.4%	\$444	6.7%	101.5
W.R. Berkley Corp.	\$2,719	13.5%	\$233	(4.7%)	95.6
The Hanover Insurance Group Inc.	\$2,319	4.7%	\$120	69.6%	97.3
Cumulative	\$78,220	3.1%	\$7,187	23.3%	95.0

\*Includes dividends  
Source: Company reports

**INSURERS**

Continued from previous page

from 98% during the same period a year earlier.

“On balance, it was strong performance by the commercial sector,” said John Ward, CEO of Cincinnati Partners L.L.C., a Loveland, Ohio-based private equity firm focused on the insurance industry. “Underwriting results continue to improve for the industry. Investment results continue to be soft. On balance, it was a very strong six-month period.”

In an analysis released earlier this month, Barclay’s Capital Inc. said it remains “constructive” on the property/casualty industry. “There is evidence of firm P&C insurance prices translating into improved underwriting results,” Barclay’s Capital said. “As the economy recovers, improving insured exposure growth is a modest tail wind that should also drive top-line growth for top-tier insurers.”

While reserve releases continue and could last through 2014, “this tail wind will ease at some point,” Barclay’s Capital said.

“Operating results have generally been stronger than expected with last year’s rate increases driving generally better-than-expected accident-year margin improvement,” said Mark Dwelle, an insurance analyst at RBC Capital Markets, a unit of RBC Securities Inc. in Richmond, Va. He added that lower catastrophe losses also have helped results.



While insurers did fairly well in the first quarter, “they slowed” in the second quarter, said Meyer Shields, Baltimore-based managing director of equity research,

property/casualty insurance at Keefe, Bruyette & Woods Inc.

Mr. Dwelle said second-quarter results showed some signs of rate increases beginning to plateau,

**Interest rates a wild card**

One of the unknowns facing the property/casualty insurance industry is the effect of potentially higher interest rates.

Rates have been at historic lows for years, cutting into insurers’ investment income while maintaining the value of the underlying investments. But rates are slowly rising and could jump more dramatically depending on decisions made by the Federal Reserve Board.

“Higher interest rates didn’t seem to play much of factor in the first half but could be a bigger factor in the second half,” said Mark Dwelle, an insurance analyst at RBC Capital Markets, a unit of RBC Securities Inc. in Richmond, Va.

Increased interest rates could have a trio of effects on insurers, said Meyer Shields, Baltimore-based managing director of equity research, property/casualty insurance for Keefe, Bruyette & Woods Inc.

The first effect is that rising interest rates could hurt insurer book value, he said.

The second effect would be that increased rates would make potential investment income a little greater than it had been.

But the third effect would be to the extent that higher interest rates correspond to higher inflation, which could hurt overall returns, said Mr. Shields.

By Mark A. Hofmann

although different companies reported different effects. “One company would say property is soft, others would say that’s not so bad,” he said, adding that casualty was generally better.

“There was a sense on the casualty side that rate increases were stable but no accelerating,” Mr. Shields said.

Mr. Ward said there were “interesting dynamics” going on concerning rates. “We’re now seeing evidence that rates are flattening in some ways and I would expect that 2013 will play out in that rates will be virtually flat and on the decline by the end of the year.”

Rate increases showed signs of slowing in Dallas-based electronic insurance exchange MarketScout’s July commercial insurance rate report. Year-over-year, rates in July increased an average of 4% following several months where increases averaged 5%.

“There seems to be some downward pressure on reinsurance rates, so primary carriers can be more aggressive on their pricing,” said Mr. Ward. “And so much of the pricing cycle is impacted by capital, and surplus is increasing.”

Mr. Ward added there seems to be a “turning tide” regarding commercial insurance rates.

That could change, though, warned Mr. Shields.

“On the horizon, it depends on claims cost inflation, which has been remarkably benign for a long time. And when that changes, I think you’ll see worse underwriting results but bigger rate increases,” he said.

**Higher rates, better economy boost brokers**

**Cost management pays off for large firms**

BY BILL KENEALY

Powered by solid results in their core insurance brokerage business, as well as increasingly profitable offerings in reinsurance and consulting, the publicly traded insurance brokers posted strong first-half results in 2013.

Marsh & McLennan Cos. Inc., Aon P.L.C., Willis Group Holdings P.L.C., Arthur J. Gallagher & Co. and Brown & Brown Inc. all reported first-half gains in revenue compared with the prior year, while all except Willis reported gains in net income.

“Overall, it’s been a somewhat positive trend in terms of traction in the first half of 2013,” said Julie Herman, New York-based associate director for Standard & Poor’s Corp. “They are continuing to build off the momentum of 2012, and the headwinds they were facing from the soft economy and rates are turning.”

Indications of an improving business environment were evident in organic growth tallied by the brokers.

London-based Aon said organic revenue increased 4% in the six-month period in its retail brokerage business, reflecting gains in the Americas and internationally.

“International organic revenue increased 3% driven by strong growth in New Zealand, France and emerging markets, partially offset by a modest decline in Germany,” Aon President and CEO Greg Case said in a statement accompanying the earnings report.

Yet, Paul Newsome, managing director and senior insurance analyst at investment banking firm Sandler O’Neill & Partners L.P. in Chicago, said the most impressive metric for the brokers was not so much organic growth as it was margin improvements.

“The management at the big brokers have really buckled down and tried to manage their costs as best they can,” Mr. Newsome said.

Daniel Glaser, Marsh & McLennan’s president and CEO, touted the New York-based company’s expanding margins.

“Adjusted operating income grew 13%, reflecting excellent margin expansion in both the risk and insurance services and consulting segments,” he said in a statement. Additionally, Marsh & McLennan’s reinsurance intermediary, Guy

Carpenter & Co. L.L.C., “generated impressive underlying revenue growth, driven by its U.S. and international operations.

Likewise, while all three of the major business segments at Willis experienced first-half revenue growth, Willis Re, the brokerage’s reinsurance arm, posted the strongest growth, a 10.3% gain in commissions and fees compared with the same-period totals in 2012,

while the North America and international units’ brokerage revenue grew by 6.1% and 2.5%, respectively.

While Aon, Marsh and Willis all posted respectable revenue gains, the Itasca, Ill.-based Gallagher and Daytona Beach, Fla.-based Brown & Brown posted the greatest percentage gains.

While opportunities to win business from each other in the large-

account space dominated by Marsh, Aon and Willis exist, middle-market brokers have a relatively easier time taking business away from the smaller regional brokers they compete against, Ms. Herman said.

“When you hear a middle-market broker showing a lot of new business, it’s generally business won from smaller brokers that can’t compete as well in an

## ACQUISITIONS STILL GOING STRONG

While the largest insurance brokers demonstrated strong organic growth in the first half of 2013, acquisitive growth remains a priority as Brown & Brown Inc. and Arthur J. Gallagher & Co. announced record deals in the period.

In June, Brown & Brown said it was acquiring rival Beecher Carlson Holdings Inc. for \$336.5 million from private-equity firm Austin Ventures.

The move helps Brown & Brown, the seventh-largest broker of U.S. business according to *Business Insurance’s* 2013 ranking, grow its top-line revenue and enter the large-account business, analysts say.

In August, Gallagher, the third-largest broker of U.S. business according to *Business Insurance’s* 2013 ranking, acquired Short Hills, N.J.-based insurance broker Bollinger Inc. for about \$276.5

million.

The deal gives Gallagher a larger presence in the Northeast as well as boosting its employee benefits and program business.

Both deals were the largest in the brokers’ respective histories.

Julie Herman, New York-based associate director for Standard & Poor’s Corp., said she expects the brokers to continue to focus on growing through acquisitions.

“It’s still very fragmented in the middle market,” Ms. Herman said. “Even though there has been such a large amount of acquisition activity in the past year, there are still plentiful acquisition opportunities.”

By Bill Kenealy

## FIRST-HALF 2013 BROKER RESULTS

Results for the largest publicly traded insurance brokers, ranked by total revenue. Figures in millions of dollars.

Broker	2013 revenue	% increase*	2013 net income <sup>1</sup>	% increase (decrease)*
Marsh & McLennan Cos. Inc.	\$6,214	2.3%	\$801	18.5%
Aon P.L.C.	\$5,812	2.6%	\$502	3.7%
Willis Group Holdings P.L.C.	\$1,941	4.6%	\$324	(2.7%)
Arthur J. Gallagher & Co.	\$1,454	21.5%	\$134	34.3%
Brown & Brown Inc.	\$661	11.5%	\$112	21.7%

\*Percentage change reflects unrounded figures. 1 Includes the impact of acquisitions or discontinued operations.

Source: Company reports.

increasingly complex insurance environment,” she said. “There’s now a necessity to add real value.”

Another noteworthy occurrence so far this year has been the ascension of new leadership at Marsh and Willis, with Mr. Glaser succeeding Brian Duperreault at Marsh on Jan. 1. and Dominic Casserley taking over the reins at Willis from Joe Plumeri on Jan. 7. “The CEO change is more important and more profound at Willis than at Marsh,” Mr. Newsome said. “At Marsh, it was more of an internal change. At Willis, it’s an

external change.”

In a research note, Adam Klauber, Chicago-based analyst at investment banking and asset management firm William Blair & Co. L.L.C., said the leadership change at Willis will bring an outsider’s perspective.

“We continue to believe that 2013 will be a year of transition for Willis, as new CEO Dominic Casserley completes his strategic review and invests in new talent and capabilities in key growth areas,” Mr. Klauber said in the research note.

# YOUR OPINION COUNTS

Email invitations for the third annual *Business Insurance Drivers and Buyers Choice Survey* were sent out.

Your participation is important to determine the most important insurance decision of commercial insurance buyers like you.

*Business Insurance’s* mission is to provide insights and analysis to help our readers. The results of this annual survey helps buyers compare their opinions with those of their peers.

Furthermore, the results provide insurers, brokers and third-party administrators with valuable feedback and better information on insurance buyers’ needs and enable the industry to provide better products and services.

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AND TAKE A MOMENT TO  
COMPLETE THE SURVEY**



**BUSINESS INSURANCE  
BUYERS 2013  
CHOICE SURVEY**

# IMPROVED MEDICAL COST CONTROL EFFORTS HELP DRIVE PROFITS HIGHER FOR HEALTH INSURERS

Enrollment rises with increases in Medicare Advantage, Medicaid membership

BY MATT DUNNING

The nation's biggest health insurers continued to build financial momentum through the first half of 2013, as strategies for contending with the implementation of key health care reform provisions next year became clearer.

The five largest publicly traded U.S. health insurers increased their combined total revenue through June 30 by 12.4% year over year, to \$154.2 billion, according to *Business Insurance's* analysis of company reports.

First-half net profit among the market's leading insurers — Aetna Inc., Cigna Corp, Humana Inc., UnitedHealth Group Inc. and WellPoint Inc. — grew 9.9% over same-period results reported in 2012, to \$6.6 billion, aided in large part by lower-than-expected utilization and a heightened focus on controlling medical cost trends, analysts said.

"I would say performance for these companies was very impressive, particularly in the second quarter," said Tom Mason, a Charlottesville, Va.-based senior financial analyst at SNL Financial L.C., noting that all five top-tier insur-

ers outperformed his firm's estimates in the most recent quarter.

"In general, we saw a lot of positive reserve development, and keeping medical costs under control was a major theme," Mr. Mason said.

Overall, the market's largest insurers reported a 14% increase in their combined total medical enrollments through the first six months of the year. However, analysts said the year-over-year growth in total revenue was mainly driven by increased membership in market leaders' Medicare Advantage and Medicaid segments, which collectively grew by 32% over totals reported in 2012, compared with 8.5% growth in total commercial medical enrollments.

Having completed its acquisition of Coventry Health Care Inc. on May 3, Hartford, Conn.-based Aetna nearly doubled its footprint in government-funded plans.

"The Coventry deal provides Aetna with critical mass in Medicare Part D as well as material Medicaid exposure, shifting the book more heavily toward government programs," Jennifer Lynch, a research analyst at New York-

## MAJOR U.S. HEALTH INSURERS' FIRST-HALF 2013 RESULTS

Largest publicly traded U.S. health insurers ranked by reported revenue. Dollar figures and enrollment in millions.

Insurer	2013 revenue	% increase*	2013 enrollment	% increase*	2013 net income	% increase (decrease)*
UnitedHealth Group Inc.	\$60,748	11.4%	45.0	25.4%	\$2,628	(3.6)
WellPoint Inc.	\$35,423	14.9%	35.7	6.3%	\$1,685	12.3%
Aetna Inc.	\$21,066	19.1%	22.0	21.8%	\$1,026	5.9%
Humana Inc.	\$20,807	4.5%	12.4	3.6%	\$893	47.8%
Cigna Corp.	\$16,163	14.0%	14.3	3.2%	\$562	(25.2)

\*Percentage change reflects unrounded figures  
Source: Company reports

based BMO Capital Markets, said in a note to investors. "While we view government program revenue as more risky than commercial premium, it would be naïve to ignore the growth opportunity presented by entitlement program participation."

Although they comprise less than 15% of the five leading insurers' combined total medical membership, government-based medical enrollments accounted for

48.1% of the revenue collected through the first half of 2013, up from 43.1% a year ago.

"That's been the trend over the last couple of years," said Vishnu Lekraj, a Chicago-based senior research analyst at Morningstar Inc. "Excluding the individual mandate and the uninsured coming to the market as a result of that, the biggest growth opportunities for health insurers are going to be the Medicaid market and, just as a matter of demographics, the Medicare Advantage market."

Beyond much slower growth in enrollments, analysts said another factor driving down insurers' commercial group revenue is the rising number of employers electing to self-fund health benefit plans for active employees and pre-Medicare retirees. Through the first six months of 2013, administrative service-only enrollments among the largest health insurers increased by a combined 10.4%, to 67.1 million lives.

Minnetonka, Minn.-based UnitedHealth Group alone added 4.9 million lives to its ASO enrollments in the first half of the year, about a quarter of which had previously been enrolled in fully insured plans.

"ASO products carry greater profitability on a percentage basis, but it's also going to bring in fewer gross premium dollars," Mr. Lekraj said. "With the growth in employment and the broader pickup in the economy, you will see more and more membership growth in the ASO products."

Although health insurers reported a strong first half, analysts said the industry's true test still lies ahead in the form of new regulations under the Patient Protection and Affordable Care Act set to take effect in 2014 and, more immediately, the public health insurance exchanges due to open in the fall.

"The big thing these companies are going to be looking at in the second half of the year is how the individual insurance exchange market works out, and how they each fit into that market in terms of their execution, pricing, membership growth opportunities and their participation levels," Mr. Lekraj said.

So far, some top-tier insurers have signaled more confidence in the short-term viability of the public exchanges than others. UnitedHealth, WellPoint and Humana have each stated they intend to participate in as many as 14 state-based insurance exchanges.

In recent weeks, Aetna has withdrawn several rate proposals it had submitted to state and federal insurance regulators, citing prohibitive limitations placed on premiums. Similarly, Cigna has signaled its desire to let the public exchanges mature a bit before entering the marketplace.

"While Cigna is taking a wait-and-see approach to public exchanges, that distribution channel is appealing to the company," Ms. Lynch said. "Cigna plans to dabble in private exchanges and intends to create a proprietary marketplace as well."

## Large health insurers plan to make cuts to Medicare Advantage programs

Facing anticipated reductions in funding and regulatory changes under the health care reform law, several of the nation's largest health insurers have indicated plans to scale back their Medicare Advantage programs.

Beginning in 2014, insurers' Medicare Advantage plans will be held to a minimum medical-loss ratio of 85% under the Patient Protection and Affordable Care Act. The reform law also calls for a \$156 billion reduction in Medicare Advantage payments by 2022.

Those cuts, coupled with the 2% overall reduction in Medicare spending under the Budget Control Act of 2011 and potential further cuts resulting from ongoing budget negotiations in Congress, prompted senior executives at several leading health insurers to outline planned withdrawals from certain Medicare Advantage markets and narrowed Medicare benefit plan offerings during recent calls with securities analysts.

UnitedHealth Group Inc. and Humana Inc., which together account for about 37.5% of all Medicare Advantage enrollments, said that anticipated 2014 market withdrawals will affect roughly 5.1% and 3.2% of their total Medicare Advantage members, respectively. However, insurers indicated that most of the members affected by market withdrawals would be offered coverage under a different Medicare Advantage plan.

"The depth of the underfunding of these benefits to seniors is causing us to exit certain market areas, reduce the number of plan offerings and reduce benefits in the majority of the local markets we serve commensurate with our review of the competitive position and long-term sustainability of our services for each individual market," UnitedHealth Group CEO Stephen Hemsley said during the company's July 18 conference call with analysts.

By Matt Dunning

## NEW WILLIS CHIEF ASSESSES INDUSTRY CHANGES

**Q** What have you personally found to be the most surprising or challenging facet of the insurance industry's inner workings?

**A** I think the most interesting challenge we've faced is prioritizing opportunities. We see significant interesting opportunities to serve our clients and thereby grow around the world. But the reality is that we can't do all of them. The second aspect of working in the brokerage space has been the large amount of mergers and acquisitions activity, at dizzying price numbers in some cases, which are sometimes a bit difficult to figure out how they work. You end up having to include a huge amount of leverage in order to make some of them work, particularly in North America.

**Q** In what ways do you think the company's relationship with its producers, analysts and other personnel is changing?

**A** Clients are demanding more data and more analytics, and also demanding teams of people from Willis, and that has some

### Q&A

important indications for our staff. They've got to be more comfortable working in teams, they've got to be focused on building up their skills in new areas, and specialization around a particular industry or product area is becoming more and more the norm.

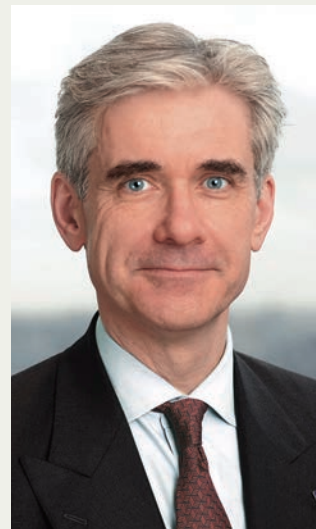
**Q** Can the rate of growth Willis has seen in its human capital practice be sustained on a consistent basis once the health care reform law has been fully implemented?

**A** An element of the growth in our human capital practice is the

ongoing inflation and innovation in the health care space, independent of the health care reform act. We don't see any signs of that changing, and that creates ongoing health care cost management issues for employers. Secondly, if you look at the history of other major regulatory changes, there's a bit of a spike when they happen, but the change doesn't stop thereafter. The idea that the Patient Protection and Affordable Care Act is the last piece of legislation we're going to see in the U.S. is slightly unlikely. I think we're going to be fine tuning it and changing it for some time, and who knows how politics might factor into how all of that plays out.

**Q** How would you characterize Willis' appetite for acquisitive growth in the next one to two years, both domestically and internationally?

**A** We look at opportunities globally. We're looking at companies that help us grow, where we see synergies with our company, and critically, where we see positive cash flow coming out of the deal. If



DOMINIC CASSERLEY

WILLIS GROUP HOLDINGS P.L.C.

Dominic Casserley took over as CEO of Willis Group Holdings P.L.C. in January, after a 29-year career in management consulting at McKinsey & Co. In an interview with *Business Insurance* Associate Editor Matt Dunning, he discussed his acclimation to the insurance industry and the company's growth strategy. Edited excerpts follow.

we're going to pay some amount of money, we want to make sure we get more cash back out, and we'll be very disciplined about that. We're going to be targeting acquisitions that meet those criteria, but we don't necessarily have a domestic/international split. We're looking at how they'll fit globally within our company.

**Q** What is the status of Willis' search for a carrier partner for its Global360 sidecar facility? What are some of the criteria you've set forth for evaluating potential partners?

**A** The criteria are easy. It's imperative that whatever agreements we put forward are in our clients' best interest. We're looking at arrangements that can ultimately help our clients and that are sustainable. We're in advanced stages of discussions with multiple carriers from a range of different markets and geographies who've expressed strong interest in participating in this Global360 facility. Obviously, we're not in a position to comment on any specific arrangements or deals, but we are in advanced negotiations.

### COMINGS & GOINGS

## UP CLOSE: ANDREW A.J. COHEN

SAN FRANCISCO-BASED SENIOR VICE PRESIDENT,  
EMPLOYEE BENEFITS PRACTICE LEADER  
Hub International L.L.C.

**PREVIOUS POSITION:** San Francisco-based area vice president for Gallagher Benefits Services Inc.

**CHALLENGES FACING INDUSTRY:** Specific to the health insurance industry, insurance carriers are faced with the daunting task of understanding, implementing and pricing for the Affordable Care Act, (which) is in the constant state of flux due to its political nature.

**INDUSTRY OUTLOOK:** I definitely see the landscape changing, for us to figure out how (employers) are going to create a total rewards package for their employees. Employees need to understand health care better and take responsibility for their own health.

**WHAT I WOULD CHANGE:** I would like to lower the cost of providing health care.

**FIRST INDUSTRY JOB:** I was a group underwriter for Blue Shield of California.

**WHAT SURPRISED ME:** I've been doing this for 31



years, and I have seen a lot of legislation come and go. What surprises me is we continue to absorb rate increases year after year without being more proactive in controlling costs.

**IF I KNEW THEN WHAT I KNOW NOW:** I would want to have more employers be self-insured to allow them to guide their own destiny.

**ADVICE:** Start by learning. Education is the key to understanding this industry.

**OUTSIDE THE INDUSTRY, A DREAM JOB:** I would like to be a sailor on Oracle, the America's Cup boat.

**HOBBIES:** Golf, gardening, hiking and playing with my family.

**THING MOST PEOPLE DON'T KNOW ABOUT ME:** That I was born in Bangkok, Thailand.

**FAVORITE BOOK:** "Robinson Crusoe" by Daniel Defoe.

**FAVORITE MEAL:** Any type of Mexican food.

### Professional Moves & Promotions

Visit [www.businessinsurance.com/ComingsandGoings](http://www.businessinsurance.com/ComingsandGoings) for a full list of this week's personnel moves and promotions. Check our website daily for additional postings and sign up for the weekly email.

#### BROKERS

Cooper Gay Swett & Crawford Ltd.	Dan Lazarz
Marsh Inc.	Steve Kempsey
Hub International Ltd.	Andrew Cohen
Swett Atlanta	Matt Brott

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Endurance Speciality Holdings Ltd.	Fred Cooper
Aspen International Insurance	Richard Smart
Citizens Property Insurance Corp.	Chris Gardner
Preferred Mutual Insurance Co.	Fred Schneider

#### REINSURERS

Munich Re	Patrick J. Shannon
Munich Re	Bradley Anderson

#### OTHER

New Benefits Ltd.	Marti Powles
New Benefits Ltd.	Dulce Bozeman
The Workers Compensation Research Institute	Alan McClain

*Business Insurance* would like to report on senior-level changes at commercial insurance companies and service providers. Please send news and photos of recently promoted, hired or appointed senior-level executives to: Kate Shepherd, *Business Insurance*, 150 N. Michigan Ave., Chicago, Ill. 60601-7524. [kshepherd@businessinsurance.com](mailto:kshepherd@businessinsurance.com).

## IRS website explains health care reform

The Internal Revenue Service has launched a website for employers to obtain information about the responsibilities they face under the nation's health care reform law.

The website, [www.irs.gov/uac/Affordable-Care-Act-Tax-Provisions-for-Employers](http://www.irs.gov/uac/Affordable-Care-Act-Tax-Provisions-for-Employers), launched last week, offers numerous links to IRS bulletins and rules that detail the many requirements that the Patient Protection and Affordable Care Act imposes on employers.

The website also includes the IRS notice that explains why government regulators in July delayed by one year until 2015 a key health care reform law provision that requires employers with at least 50 full-time employees to either offer qualified coverage or pay a fine.

## Ironshore unit launches claims-made policy form

Ironshore Inc.'s specialty casualty unit has launched a claims-made policy form to accompany its suite of products and services available to the commercial general liability market.

The general liability claims-made advanced form of Crisis ThreeSixty introduces a suite of endorsements that include recall reimbursement expenses, the insurer said in a statement.

The Crisis ThreeSixty policy enhancement covers up to \$150,000 in expenses related to a commercial general liability claim in addition to the policy limit, and it combines crisis management and recall reimbursement expenses.

Industry sectors that the claims-made form policy targets include manufacturers of consumer products, construction equipment, mining machinery, and railroad parts and equipment, the insurer said.

"The current pricing environment and recent product liability cases led to the development of a claims-made option including recall reimbursement expense cover to benefit insureds and our broker partners in meeting the liability coverage needs in diverse industry segments," Tim McAuliffe, president of Ironshore Specialty Casualty, said in the statement.

## AIG expands to \$100 million global Side A D&O limits

American International Group Inc. now offers up to \$100 million globally in limits for Side A directors and officers liability insurance.

The added capacity is aimed at facilitating resolution of severe and complex litigation by helping companies reduce the number of policy layers needed for adequate coverage, the insurer said in a statement.

Side A insurance responds when indemnification is not available for individual directors and officers to pay the cost of defending themselves in legal sit-



## Hartford liability suite expanded for tech firms

The Hartford Financial Services Group Inc. has expanded its Fail Safe professional liability insurance suite to address the needs of technology companies of all sizes.

Its features address the evolving needs of technology companies with expanded coverage for data, systems and network breaches, the insurer said in a statement. They include broader coverage for data loss, security breaches and damage caused by rogue employees, extended liability coverage for a technology company's activities on its own computer system and networks, and claims-made policy forms that ease reporting requirements.

The cost of professional liability claims — such as breach of contract, failure to perform and negligence — against technology companies average more than \$200,000, Hartford said.

"Professional liability is one of the most significant risks for technology companies today," Joe Coray, vice president of Hartford's technology and life science practice, said in the statement.

"An alleged failure of a product or service that causes economic loss to a client's business can result in a costly lawsuit and reputational damage," Mr. Coray said in the statement.

The insurer also launched HFP Pronto for Fail Safe, which is an agent portal offering a streamlined submission process, online collaboration capabilities for agents, customers and underwriters, and risk management and insurance shopping resources, according to the statement.

uations and can fill in coverage gaps that can occur in a large directors and officers programs, AIG said in the statement.

## Aon bolsters excess liability follow-form policy

Aon Risk Solutions, a subsidiary of Aon P.L.C., has enhanced its "Bermuda shorts" excess liability follow-form policy, answering demand for greater contract certainty and consistency of coverage.

The new form incorporates several

important coverage enhancements, the insurer said in a statement.

The enhancements include: duty-to-defend coverage, which provides insured clients with a defense to claims made under a policy; shaving or erosion of underlying limits; and business continuity, which provides for an automatic 30-day policy extension in the event of a natural disaster, according to the statement.

"The enhanced form will improve coverage for our insureds, remove cumbersome steps from the process of securing coverage and deliver the contract certainty needed during the claims process," Anthony DeFelice, managing director of Aon Risk Solutions' U.S. casualty major accounts practice, said in the statement.

Aon also plans to launch a "London shorts" form that will incorporate many of the benefits included in the enhanced "Bermuda shorts" form, the insurer said in the statement.

## Zurich updates policy for environmental liability

Zurich North America has revised its fixed-facility environmental liability Z Choice product to eliminate coverage sublimits and include built-in coverage features such as emergency expenses and crisis management.

The sublimits within the emergency expense coverage have been eliminated in the updated policy, the unit of Zurich Insurance Group Ltd. said in a statement.

"Eliminating emergency expenses sublimits is one of the key coverage enhancements in today's marketplace," Bob Newmarker, head of Zurich North America's environmental site practice, said in the statement. "Z Choice gives policyholders the ability to know that emergency expenses may not be restricted by a specific sublimit"

A crisis management expense coverage supplement was added to the policy to help minimize possible issues such as negative publicity, according to the statement.

## CFC Underwriting upgrades management liability policy

CFC Underwriting Ltd. has made several upgrades to its ExecSurance management liability policy for small and midsize businesses.

The policy has been expanded to include standard coverage for third-party discrimination claims and violations of the Immigration Reform Control Act, according to a statement by the London-based specialty lines insurer.

Additional enhancements include defense and indemnity coverage up to \$250,000 for wage-and-hour claims, as well as full-entity directors and officers liability coverage.

ExecSurance incorporates a range of insurance products, including D&O, employment practices liability, fiduciary liability, cyber and privacy risk, crime, kidnap and ransom, and reputation and brand protection.

## DEALS & MOVES

### Atlanta's Digital Insurance buys employee benefits firm in S.C.

Atlanta-based Digital Insurance Inc. has acquired Turnkey Benefits Inc., an employee benefits advisory firm based in Fort Mill, S.C.

As a result of the acquisition, Digital Benefit Advisors, a division of Digital Insurance, will open the company's first office in Charlotte, N.C.

Turnkey co-principals Shelley Stromple and Mark McLean and their team will join Digital Benefits to provide clients expanded offerings and greater support, the companies said in a statement.

"Bringing Shelley and Mark into the DBA fold strengthens our presence across the Carolinas and the Southeast," Mike Sullivan, executive vice president and chief marketing officer of Digital Insurance, said in the statement. "Turnkey Benefits is highly regarded for its strategic approach to managing health care-related expenditures by compiling and interpreting data to develop cost-saving solutions for their clients. Digital's emerging private exchange solution will also strengthen their competitive position in the marketplace."

Terms of the deal were not disclosed.

Digital Benefit's exchange marketplace, to be introduced in the coming months in many states, will offer health, life, disability, accident, critical illness, long-term care, dental and vision insurance, along with other products and services, the company announced in June.

The first exchange will open in Vermont, where Digital Benefit Advisors of Vermont, a Colchester, Vt.-based division of Digital Insurance, has reached an agreement with Blue Cross Blue Shield of Vermont to offer a range of health benefit plans through the exchange for plan years beginning Sept. 1.

### Ameritox of Baltimore acquires medical manager Prium

Ameritox Ltd., a Baltimore-based pain medication monitoring company, has acquired Prium, which provides medical cost management services serving the workers compensation market.

Terms of the deal were not disclosed.

Both firms will continue to function as separate entities, Ameritox said in a statement. "We are extremely excited about the opportunity to bring the unique capabilities of these two great companies together," Ameritox CEO Scott Walton said in the statement.

"Employers are increasingly aware and concerned about the quality-of-life issues and financial ramifications that the epidemic of prescription drug abuse and misuse are having on their employees, particularly the injured worker. Just as Ameritox pioneered the market for prescription-drug monitoring, Prium has pioneered a unique set of services on the medical management side of the equation," Mr. Walton said.

### Allied World unit buys 21.1% of Gravity Underwriting

Allied World Assurance Co. Holdings A.G. said its Dublin-based unit, Allied World Assurance Holdings (Ireland), bought a 21.1% share in London-based managing general agent Gravity Underwriting Ltd., which provides property/casualty coverage for insurance brokers in U.K. small- and medium-size markets. Under terms of the deal, Gravity will help facilitate business for Allied World Europe's property book.

# Help your workers save for retirement



Ms. Reynolds



Mr. McClain

Employers who develop a retirement income strategy will generate a competitive advantage in terms of employee retention, engagement and productivity, according to Mercer L.L.C. retirement savings plan experts Amy Reynolds and Bill McClain.

BY AMY REYNOLDS AND BILL MCCLAIN

Nearly a generation ago, organizations began the transformation from defined benefit pension plans to the prevailing defined contribution model for employee retirement. For most of today's workforce, the defined contribution plan represents the primary employer-sponsored retirement benefit. Despite concerns about retirement adequacy in a world of 401(k)s and other defined contribution plans, few employers are considering a return to the defined benefit model.

While the emphasis on individual participation and savings has been a powerful and challenging legacy of the past two decades, employers now have a critical — and rewarding — role to play in preparing their workforces for retirement. In our view, employers who proactively develop a retirement income strategy will generate a competitive advantage in terms of employee retention, engagement and productivity.

Indeed, the facts call for intervention. More than 75% of workers near retirement who responded to Mercer's 2012 Making Smart Benefit Choices survey say they are either "very" or "fairly concerned" about their retirement readiness. Workers are increasingly aware of the shortfall they face, and of their need for support and advice in making the critical decisions about how they utilize their retirement resources.

Employers can and should intervene, for a number of reasons. Basically, it's the right thing to do from a social responsibility standpoint, thus enhancing any organization's brand. In addition, the employment relationship forms a natural basis for acting collectively, since it improves buying power and leverage in managing vendors on behalf of employees, reducing costs and improving the level of services. The latter is especially important in helping employees make optimal decisions regarding complex financial products and investments. Improved employee decision-making can greatly improve retirement outcomes in the face of limited employee and employer resources.

Intervening also plays a practical role in workforce management. The 2012 Mercer Workplace Survey of more than 1,600 active 401(k) participants at companies of every size revealed that nearly half (44%) of employees are thinking of delaying their retirement since they can't afford to stop working. That poses a challenge for many employers in managing their retirement-age employees and controlling health care and severance costs. Delayed retirement due to

financial necessity can also lead to disengagement and lower productivity. A retirement-ready workforce can increase management flexibility and reduce the potential negative effects of employee financial distress.

Less obvious, though, is that efforts to secure retirement outcomes for employees can often better leverage investments already made to plan infrastructure. For example, many employers have devoted resources to the design of target date mutual funds that anticipate a certain pattern to drawing down retirement assets. However, when retirees draw down their defined contribution plan balances too quickly, the intended investment strategy no longer matches cash flow. Making sure that plan structures align with the employee behavior in generating retirement income is reason enough to play an active role in employees' retirement income strategies.

We've developed a number of retirement income principles to guide employers in determining the preferred approach for their employees. When structuring your thinking around target levels of retirement income, it's useful to consider the following two tiers:

**Tier 1: The minimum requirements**—the level of income required for basic day-to-day living expenses.

**Tier 2: Replacement**—the level of income required to broadly preserve current living standards, taking into account that expenditures tend to vary during retirement.

Given the history of low levels of retirement savings, many employers know that meeting Tier 1 requirements may be all that's attainable for some employee groups. That said, a solid income floor should include an insured element to protect against longevity risks, perhaps through an existing benefit from a defined benefit plan, by purchasing an annuity with a portion of the retirement pot, or through basic longevity insurance for retirees who live beyond a certain age, say 85. But it's not wise to weight things too heavily toward traditional insurance, which could result in more coverage than what's needed, thereby eroding retirement savings.

When planning for longevity, it's important to take into account the uneven spending pattern that typifies retirement. Retirees tend to con-

sume more in their early, active retirement years. Income needs level off as they enter a more passive phase, only to increase again toward the end of life with additional medical and care expenses. Post-retirement income structures should accommodate this U-shaped spending pattern while maintaining the best possible income floor.

How can employers get started on developing a retirement income strategy for their employees? Segmenting the workforce is the best way to understand employee levels of preparedness. Initially, the workforce can be segmented into the underfunded, those on track, and the overfunded. Further segmentation by demographic characteristics such as age, service, salary and job allows employers to see trends and workforce implications.

From there, the workforce can be further analyzed based on how individuals want to manage their retirement planning: some want their employer to do it for them; others want some help; and the rest choose to do it for themselves. This segmentation process allows employers to develop retirement income menus and tools that allow employees to customize their retirement income approach to their needs and preferences.

In summary, here are some guiding principles to help in developing a retirement income strategy:

**Provide assistance:** This makes a material difference, and demand is usually highest among workers nearly ready to retire and recent retirees. Assistance can include retirement readiness seminars and planning tools, access to individual advisors and guidance from financial institutions.

**Put all wealth to work:** Rather than focusing narrowly on the employer's own retirement plan, consider external assets and alternative income sources in the planning process such as home equity, for example, as well as the ability to continue working in retirement.

**Manage market risk:** Implement approaches that manage market and, indirectly, inflation risks by gradually reducing elements of the retirement portfolio that are not required to build the retirement income floor.

**Manage longevity risk:** Some plans, out of convenience, default to a draw down of retirement funds based on

required minimum distribution rules. Since these rules were developed for taxation purposes, and don't take into account market events and longevity risk, more sophisticated planning and annuitization need to play a role.

**Leverage buying power:** There's a significant difference between retail products and those available to employers through group purchase. It's more than a question of price; employers with a clear picture of their workers' needs can better align the solutions.

**Integrate workforce planning into retirement income strategy:** Retirement income strategy should reflect the organization's view on the duration of the employment relationship. Some employers eager to engage with older customers or retain key technical expertise have policies that accommodate part-time schedules or flexible work arrangements to manage the transition to retirement more gradually.

**Avoid too-rapid income drawdown:** The strategy must address this employee tendency through education and appropriate draw down strategies and default approaches.

**Manage through life cycles:** Since there's no clear point when employees can be classified as "near retirement," retirement readiness must be managed as a long-term challenge and savings as a lifetime habit. It calls for a pragmatic approach to structuring the accumulation phase.

**Know your fiduciary position:** Retirement income strategy is not isolated from the broader governance and fiduciary structures under which a defined contribution plan operates. Engaging with the appropriate internal committees and external advice can ensure consistency and alignment.

Utilizing scarce resources to help generate sustainable income for retirees has never been more challenging. These strategic guidelines can lead employers to an approach that provides customized choices for participants, better retirement outcomes, tighter alignment between retirement and workforce management, and a major dividend in the form of enhanced employee engagement.

*Bill McClain is U.S. defined contribution intellectual capital leader and a principal based in the Seattle office of Mercer L.L.C. He can be reached at bill.mcclain@mercer.com or 206-214-3627. Amy Reynolds is the U.S. defined contribution consulting leader and a partner in Mercer's retirement business based in Richmond, Va. She can be reached at amy.reynolds@mercer.com or 804-344-2639.*



Improved employee decision-making can greatly improve retirement outcomes in the face of limited employee and employer resources.

evolves into a long-term disability claim, said Christopher Anderson, president of Medaca Health Group in Toronto. In addition to lowering the incidence of long-term disability claims, they can lower the duration of short-term disability claims, he said.

Mr. Anderson spoke during the Disability Management Employer Coalition's 18th annual conference, held Aug. 18-21 in Atlanta.

Although such measures require resources, they also reduce costs, experts at the conference said.

"If you get people better, you will actually reduce costs and not increase them," Mr. Anderson said.

Unfortunately, while employers could improve worker productivity and reduce disability claims durations and costs by boosting mental health programs, stigma associated with obtaining help for mental illness remains an obstacle to receiving treatment.

To help counter that stigma, employers can structure their health and welfare programs to recognize and address mental illness in the same way they treat physical ailments such as heart or liver disease, the speakers said.

Also, employers can train supervisors to help lead employees to their company's mental health benefits offerings.

"Employers need to play a more active role in this, not only by providing services to help

individuals in the workplace who are suffering from mental illness, but by training supervisors who deal one on one with employees on a regular basis to better serve them and get them to the help they need," said Dr. Barton Margoshes, medical consultant for Chicago-based Pacific Resources Benefits Advisors L.L.C.

Substantial progress in understanding the brain and helping even those with serious mental illness contribute to society has occurred during the past two decades, said Rosalynn Carter, the former first lady and keynote speaker for the event.

Yet stigma remains the biggest obstacle for helping people with mental illness, and it causes discrimination in areas such as health care, housing and insurance, Ms. Carter said.

The stigma will always exist, but more employers are learning that providing employees help for mental health issues reduces days away from work due to disabilities, Mr. Anderson said.

"For the first time, we are seeing recognition that mental health in the workplace is not simply a human resource practice," Mr. Anderson said. "Today, mental health is a business imperative."

Early intervention to get employees mental health assistance is increasingly important in today's work environment, where 85% of jobs demand mental attention rather than physical labor, he said.

"Mental mistakes, or mistakes by overworked and stressed employees, increasingly drive business failure," Mr. Anderson said. "Healthy, mentally fit employees are required to meet business goals, especially in a world that is more stress-filled than ever."



**"Mental mistakes, or mistakes by overworked and stressed employees, increasingly drive business failure."**

Christopher Anderson, Medaca Health Group

the importance of appropriately addressing mental illness.

"Those of you in the audience need to educate your workforce, your managers, your employees, your unions," Ms. Carruthers said. "You could make a difference."

About 600 people attended the DMEC conference. Next year's event will be held in Las Vegas in August.

Reducing the stigma associated with mental health issues won't occur soon, said Marcia Carruthers, board chairman for San Diego-based DMEC. But Ms. Carruthers urged DMEC members to talk about mental health and educate their colleagues about

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### LEGAL NOTICE

UNITED STATES BANKRUPTCY COURT • SOUTHERN DISTRICT OF NEW YORK

In re Petition of Dan Yoram Schwarzmann, as Administrator of FOLKSAM INTERNATIONAL INSURANCE COMPANY (UK), LIMITED, Debtor in a Foreign Proceeding.

In a Proceeding Under Section 304 of the Bankruptcy Code  
Case No. 02-B-14070 (SCC)

**NOTICE OF ORDER PURSUANT TO SECTION 304 GRANTING RECOGNITION AND GIVING EFFECT TO SCHEME OF ARRANGEMENT IN THE UNITED STATES AND A PERMANENT INJUNCTION**

NOTICE IS HEREBY GIVEN THAT, in connection with the motion (the "Motion") of Dan Yoram Schwarzmann (the "Administrator"), as the administrator of Folksam International Insurance Company (UK), Limited (the "Company"), for the entry of a permanent injunction and order pursuant to section 304 of title 11 of the United States Code (the "Bankruptcy Code") giving effect in the United States to the scheme of arrangement between the Company and its Scheme Creditors pursuant to sections 895 to 901 of the United Kingdom Companies Act 2006 (the "Scheme") dated July 9, 2013, the United States Bankruptcy Court for the Southern District of New York (the "Court") has entered an order dated August 6, 2013 (the "Order"), among other things:

- Providing that the Scheme shall be given full force and effect in the United States, and shall be binding on and enforceable against all Scheme Creditors (as defined in the Order), including, without limitation, against such person or entity in its capacity as a debtor of the Company, in the United States;
- Permanently enjoining all persons and from taking any action in contravention of, or inconsistent with, the Scheme;
- Permanently enjoining all persons and entities from: (a) repossessing, transferring, relinquishing or disposing of any property of the Company in the United States, or the proceeds thereof, to any person or entity other than the Scheme Administrators (as defined in the Order); (b) commencing or continuing any action or legal proceeding in connection with any claim arising out of a contract of insurance, reinsurance or retrocession entered into with the Company (including, without limitation, arbitration or any judicial, quasi-judicial, administrative or regulatory action, proceeding or process whatsoever), including by way of counterclaim, against the Company or any property in the United States that is involved in the foreign proceeding, or any proceeds thereof, and seeking discovery of any nature against the Company; (c) enforcing any judicial, quasi-judicial, administrative or regulatory judgment, assessment or order, or arbitration award against the Company, and commencing or continuing any act or action or legal proceeding in connection with any claim (including, without limitation, arbitration, or any judicial, quasi-judicial, administrative or regulatory action, proceeding or process whatsoever) or any counterclaim to create, perfect or enforce any lien, attachment, garnishment, setoff or other claim over any of its property in the United States, or any proceeds thereof, including, without limitation, rights under reinsurance or retrocession contracts; (d) drawing down any letter of credit established by, on behalf of or at the request of, the Company, in excess of amounts expressly authorized by the terms of the contract or other agreement pursuant to which such letter of credit has been established; and (e) withdrawing from, setting off against, or otherwise applying property that is the subject of any trust or escrow agreement or similar arrangement in which the Company has an interest in excess of amounts expressly authorized by the terms of the contract and any related trust or other agreement pursuant to which such trust, escrow, or similar arrangement has been established;
- Requiring that all persons and entities in possession, custody or control of property of the Company in the United States, or the proceeds thereof, shall turn over and account for such property or its proceeds to the Scheme Administrators; and
- Requiring that all persons or entities that are beneficiaries of letters of credit established by, on behalf of or at the request of, the Company or parties to any trust, escrow or similar arrangement in which the Company has an interest, to: (a) provide notice to the Scheme Administrators' United States counsel of any drawdown on any letter of credit established by, on behalf of or at the request of, the Company, or any withdrawal from, setoff against, or other application of property that is the subject of any trust or escrow agreement or similar arrangement in which the Company has an interest, together with information sufficient to permit the Scheme Administrators to assess the propriety of such drawdown, withdrawal, setoff or other application; and (b) turn over and account to the Scheme Administrators for all funds resulting from such drawdown, withdrawal, setoff, or other application in excess of amounts expressly authorized by the terms of the contract, any related trust or other agreement pursuant to which such letter of credit, trust, escrow or similar arrangement has been established.

Copies of the Order, the Scheme and the Motion are available upon request at the office of the Petitioner's United States Counsel at the address below:

CHADBOURNE & PARKE LLP • Attorneys for the Petitioner • 30 Rockefeller Plaza  
New York, New York 10112 • (212) 408-5100 • Attn: Howard Seife, Esq. and Francisco Vazquez, Esq.

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### LEGAL NOTICE

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS  
COUNTY DEPARTMENT, CHANCERY DIVISION

IN THE MATTER OF THE LIQUIDATION OF LUMBERMENS MUTUAL CASUALTY COMPANY, ) NO. AMERICAN MANUFACTURERS MUTUAL ) 12 CH INSURANCE COMPANY AND AMERICAN ) 24227 MOTORIST INSURANCE COMPANY )

**NOTICE OF CLAIM FILING DEADLINE OF NOVEMBER 10, 2014 at 4:30 p.m. C.S.T.**

**PLEASE TAKE NOTICE**, that pursuant to orders entered on May 8, 2013, by the Circuit Court of Cook County, Illinois, effective May 10, 2013, Lumbermens Mutual Casualty Company, American Manufacturers Mutual Insurance Company, and American Motorists Insurance Company (collectively referred to herein as the "Lumbermens Companies") were placed into liquidation. The Orders of Liquidation With a Finding of Insolvency (the "Liquidation Orders") were entered pursuant to Article XIII of the Illinois Insurance Code (215 ILCS 5/187, et seq.). Andrew Boron, Director of Insurance of the State of Illinois, was affirmed as the statutory Liquidator (the "Liquidator") of the Lumbermens Companies.

**TAKE FURTHER NOTICE**, that pursuant to the Liquidation Orders, all rights and liabilities of the Lumbermens Companies and their policyholders, creditors and all other persons interested in their property or assets are fixed as of May 10, 2013.

**TAKE FURTHER NOTICE**, that on August 1, 2013, the Circuit Court of Cook County, Illinois, entered an Order providing for the filing of claims and the setting of a claim filing deadline ("Claim Filing Order"). Pursuant to the Claim Filing Order, all persons, companies, or entities who have, or may have claims against the Lumbermens Companies, their property or assets, or against a Lumbermens Companies' insured or policyholder, shall have the right to present and file with the Liquidator a proof of claim form on or before the claim filing deadline of **November 10, 2014 at 4:30 p.m. C.S.T.**

**TAKE FURTHER NOTICE**, that any insured under an insurance policy issued by the Lumbermens Companies shall have the right to present and file with the Liquidator a proof of claim setting forth a contingent claim on or before November 10, 2014 at 4:30 p.m. C.S.T. No such contingent claim shall be allowed for purposes of participating in any distribution(s) of estate assets that may be made at the fourth priority level, 215 ILCS 5/205(1)(d), unless such claim has been liquidated and the insured claimant has presented to and filed with the Liquidator evidence of payment of such claim on or before the contingent claim date of November 10, 2014 at 4:30 p.m. C.S.T. Any insured's contingent claim for which a proof of claim was received by the claim filing deadline of November 10, 2014, at 4:30 p.m. C.S.T., but which is not liquidated by November 10, 2014 at 4:30 p.m. C.S.T. may be estimated pursuant to Section 209(4)(b) of the Code, 215 ILCS 5/209(4)(b) for purposes of participating in any distribution(s) of estate assets that may be made at the fifth priority level, 215 ILCS 5/205(1)(e), unless otherwise directed by the court.

**TAKE FURTHER NOTICE**, that the form and required contents of all proofs of claim are described in 215 ILCS 5/209. Proofs of claim, along with supporting documents, are to be filed with, and may be obtained from the Liquidator of the Lumbermens Companies, c/o the Office of the Special Deputy Receiver, located at 222 Merchandise Mart Plaza, Suite 960, Chicago, Illinois 60654, OSD website: [www.osdchi.com](http://www.osdchi.com), or by calling OSD at (312) 836-9500. In order for a proof of claim to be timely filed, the liquidator must have physical possession of the proof of claim form on or before the claim filing deadline, or the proof of claim form must have been delivered to the United States Postal service for delivery to the Liquidator and postmarked on or before the claim filing deadline with full postage pre-paid, or the proof of claim form must have been delivered to a private mail courier for delivery to the Liquidator on or before the claim filing deadline with delivery charges fully paid.  
Paul Miller, Special Deputy Receiver

### LEGAL NOTICE

IN THE MATTER OF THE LIQUIDATION OF CONSOLIDATED MUTUAL INSURANCE COMPANY  
Supreme Court County of Kings, Index No.: 10402/79  
NOTICE

Pursuant to an order of the Supreme Court of the State of New York, County of Kings ("Court"), entered May 31, 1979 ("Liquidation Order"), the Superintendent of Insurance of the State of New York and his successors in office were appointed as liquidator ("Liquidator") of Consolidated Mutual Insurance Company ("Consolidated Mutual") and, as such, has been directed to take possession of Consolidated Mutual's property, liquidate its business and affairs, and dissolve its corporate charter pursuant to Article 74 of the New York Insurance Law ("Insurance Law"). The Superintendent of Financial Services of the State of New York has now succeeded the Superintendent of Insurance as Liquidator of Consolidated Mutual. The Liquidator has, pursuant to Insurance Law Article 74, appointed Michael J. Casey, Acting Special Deputy Superintendent ("Acting Special Deputy"), as his agent to liquidate the business of Consolidated Mutual. The Acting Special Deputy carries out his duties through the New York Liquidation Bureau, 110 William Street, New York, New York 10038. The Liquidator has submitted to the Court a verified petition ("Verified Petition") seeking an order: (i) approving the Liquidator's report ("Closing Report") on the status of and request to close Consolidated Mutual's liquidation proceeding ("Liquidation Proceeding") and the financial transactions delineated therein; (ii) authorizing the continued payment of administrative expenses, including such expenses pertaining to the closing of the Liquidation Proceeding; (iii) terminating and closing the Liquidation Proceeding; (iv) authorizing the Liquidator, without further application to the Court, to continue to receive and disburse assets, pursuant to Insurance Law Article 74, to those creditors of Consolidated Mutual with allowed claims who are eligible to share in a pro-rata distribution, after the termination of the Liquidation Proceeding (including any portion of the Post-Closing Amount (as defined in the Closing Report) remaining after payment of administrative expenses (including administrative expenses incurred in connection with the collection of such assets); (v) releasing and discharging the Liquidator, his predecessors and successors in office, and their agents, attorneys and employees, from any and all liability arising from their acts or omissions in connection with the Liquidation Proceeding; (vi) authorizing and directing the Liquidator, in his discretion, to destroy or otherwise dispose of any and all of the books, files, records and other property of Consolidated Mutual without further order of the Court; and (vii) providing for such other and further relief as the Court deems appropriate and just.

A hearing is scheduled on the Verified Petition on the 20th day of September, 2013, at 9:30 a.m., before the Court at the Courthouse, IAS Part 18, 360 Adams Street, Room 775, Brooklyn, New York. If you wish to object to the Verified Petition, you must serve a written statement setting forth your objections and all supporting documentation upon the Liquidator and Clerk of the Court, at least seven (7) business days prior to the hearing. Service on the Liquidator shall be made by first class mail at the following address: Superintendent of Financial Services of the State of New York as Liquidator of Consolidated Mutual Insurance Company, 110 William Street, New York, New York 10038, Attention: John Pearson Kelly, Esq., General Counsel.

The Verified Petition and Closing Report are available for inspection at the above address. In the event of any discrepancy between this notice and the documents submitted to Court, the documents control. Requests for further information should be directed to the New York Liquidation Bureau, Creditor Claims Department at (212) 341-6809.

Dated: July 17, 2013, Benjamin M. Lawsky, Superintendent of Financial Services of the State of New York as Liquidator of Consolidated Mutual Insurance Company.

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Vermont and other U.S. domiciles can attract captives that want to be taxed as a U.S. company from offshore domiciles.

## VCIA

Continued from page 4

adding that he doesn't think it's a good thing when captive regulation is only a part-time responsibility for a domicile's insurance regulators.

Mr. Mullen offered his thoughts in an interview during the Vermont Captive Insurance Association's annual conference in Burlington, Vt.

"It really is amazing in terms of the number of domiciles," said James A. Swanke Jr., a director at Towers Watson & Co. in Minneapolis.

Mr. Swanke said he sees clients considering some of the newly formed captive domiciles. "I think some of the new domiciles are getting a look," he said. "I think people are kicking the tires on them."

But there's always a tendency to include one of the traditional domiciles in any assessment of forming a captive, Mr. Swanke said. An established captive infrastructure is an important consideration, he said, adding, "What we tell our clients is get on an airplane, visit two or three domiciles, meet the regulators and figure out which is best for your situation."

In choosing a domicile, it's important that the captive regulation be separate from the politics in a domicile, Mr. Swanke said. "Being

comfortable with the regulators and the regulation is very important."

And from a business reputation perspective, it's important that captive parents make the right domicile choice, Mr. Swanke said, and not find their captive located in a place where changing political winds affect the commitment to captives or political considerations drive captive regulation.

"You just don't want surprises when you're working with a captive," he said.

Speaking on a panel examining companies' expanding utilization of their captives, Tim East, director of risk management for The Walt Disney Co. in Burbank, Calif., said the regulatory environment was a strong consideration when Disney chose the domicile for its first captive. Disney ultimately chose Vermont for its Buena Vista Insurance Co. property insurance captive in 2002, and chose the domicile again for its Alameda Insurance Co. casualty captive in 2003.

In selecting a domicile, the company wanted a flexible captive environment but also wanted strong regulatory oversight, Mr. East said, because Disney's No. 1 asset is its reputation.

Speaking on the same panel, Anthony A. Benish, general counsel for Cook-Illinois Corp. in Oak Forest, Ill., said his company initially chose Bermuda for its Five Fam-

ilies Insurance Ltd. captive when it formed in 2006 because it was looking for possible tax benefits and easy access to the reinsurance market.

But, he said, "We had some bumps in the road in Bermuda and decided in 2010 to relocate to Vermont." In fact the company hadn't used the captive to gain access to the reinsurance market and was electing to be taxed as a U.S. company, so the onshore domicile made sense, Mr. Benish said.

One factor that's been driving fewer domicile decisions than some had anticipated is the Nonadmitted and Reinsurance Reform Act of the Dodd-Frank Wall Street Reform and Consumer Protection Act, said Daniel D. Towle, director of financial services in the Vermont Department of Economic Development.

At issue is whether the NRRA subjects insurance business placed in captives operating outside their parent's home states to home state self-procurement taxes, with some in the captive industry saying some states have used the law to drive captives to form or redomicile in their states.

However, said Mr. Towle and David F. Provost, deputy commissioner in the Captive Insurance Division of the Vermont Department of Financial Regulation, there's little current evidence of states using confusion over the law's intent to force captive domicile decisions.

Mr. Towle said he's talked to captive consultants about the issue, "and they've said for the most part it's quieting down." It remains an important issue, he said, but isn't "on the front burner."

Many captive experts are seeing considerable interest in captive formations among Latin American companies.

"We've got a strong pipeline of feasibility studies coming out of Latin America," said Aon's Mr. Mullen. Factors driving the growing captive interest in Latin America include the region's economic growth and the increasing risk management maturity of companies there. "It's also broker-driven," Mr. Mullen said.

Bermuda has been the biggest recipient of Latin American captives thus far, but Mr. Mullen said he's seeing them look to Luxembourg and Switzerland as well.

Many Latin American captive parents are looking not only for strong captive infrastructures but domiciles where they can have easy access to top-name banking, legal, accounting and other services, Mr. Mullen said.

"One of the things I find about Latin American companies is they want top-quality everything," Mr. Mullen said.

This year's Vermont Captive Insurance Association conference, held Aug. 13-15 in Burlington, Vt., drew more than 1,100 attendees.

Next year's conference is scheduled for Aug. 12-14, 2014. For additional information about next year's conference, go to [www.vcia.com](http://www.vcia.com).

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# BACKGROUND

Continued from page 1

evaluating criminal backgrounds, the time that has passed since the offense, and the nature of the potential job.

At the heart of the EEOC's policy is data showing that while blacks accounted for just 13.1% of the U.S. population as of 2012, they represented 38% of the sentenced prisoners under state and federal jurisdictions at the end of 2011.

Despite recent pleas by nine state attorneys general that the EEOC reconsider its policy as well as a federal judge's sharp criticism of its implementation, the EEOC is expected to stand firm on the issue (see related story).

"We're not preventing employers from doing due diligence in this respect," said Tanisha Wilburn, a Washington-based senior attorney adviser in the EEOC's office of legal counsel. But "employers can't use this information as a screening tool," and there must be a "careful and thoughtful process," she said.

Not only is conducting a complicated process of checking criminal backgrounds onerous, "it raises the issue of hiring people who may cause liability, perhaps because of their criminal background," said Richard B. Cohen, a partner at law firm Fox Rothschild L.L.P. in New York.

The agency in effect "is injecting a lot of subjective analysis into a process where human resources' inclination is to try to keep everything fairly objective in this approach," said Peter J. Gillespie, of counsel at Fisher & Phillips L.L.P. in Chicago.

Furthermore, it is impractical particularly for large employers "to do a full-scale analysis into every applicant and the circumstances of every single conviction," said Michael A. Warner Jr., a partner at Franczek Radelet P.C. in Chicago.

Another concern is whether the EEOC's policy conflicts with state laws, said Mark B. Wiletsky, of counsel at Holland & Hart L.L.P. in Boulder, Colo.

Depending on the industry or type of organization or business, "some organizations are required by state laws to conduct background checks," Mr. Wiletsky said.

Despite the April guidance, legal experts say the policy remains vague.

"The EEOC's concerns about background checks really have not yet crystallized into enforceable standards or practices that can be followed," Mr. Gillespie said.

"They've left employers in a bit of a limbo situation in that they haven't really been able to provide employers with concrete examples of what aspects of a policy can create issues."

"I don't think we have enough yet where anyone can do X, Y and Z and you're bullet-proof unless you just go all out and say, 'Consider each one individually,'" said Michael W. Fox, a shareholder with Ogletree, Deakins, Nash, Smoak & Stewart P.C. in Austin, Texas.

Now is that "period of time where the litigation system begins to take an issue and evolve with it, and I think that's always a risky time for employers and those who are trying to provide counsel," Mr. Fox said.

"You may win in the end" should the EEOC file suit on the issue, "but you've spent a lot of money getting to that point," Mr. Warner said.

However, Sheila B. Gladstone, who heads the labor and employment practice at law firm Lloyd, Gosselink, Rochelle & Townsend P.C. in Austin, Texas, said "there is some reasonableness" to what the EEOC has said so far. "You

# Background check policy under fire from AGs

The Equal Employment Opportunity Commission's policy on criminal background checks is under fire.

In July, nine Republican state attorneys general asked the federal agency to reconsider its policy on criminal background checks and dismiss two lawsuits the EEOC filed against Spartanburg, S.C.-based BMW Manufacturing Co. L.L.C. and Goodlettsville, Tenn.-based Dolgencorp L.L.C., a Dollar General Corp. subsidiary.

The suits, which allege the companies violated Title VII of the Civil Rights Act of 1964, are pending in federal court.

The lawsuits and the EEOC's application of the law "are misguided and a quintessential example of federal overreach," the attorneys general said in the letter.

This month, in sometimes scathing language, a federal judge in Maryland dismissed an EEOC lawsuit that had accused Freeman Decorating Services Inc. of using criminal background check information in such a way that it had a disparate effect on minorities. In particular, U.S. District Court Judge Roger W. Titus criticized data used to support the EEOC's case.

There is "such a plethora of errors and analytical fallacies" underlying one statistics expert's

conclusions that it renders them "completely unreliable and insufficient to support a finding of disparate impact," Judge Titus ruled.

Tanisha Wilburn, a Washington-based senior attorney adviser in the EEOC's office of legal counsel, said the agency is considering the letter from the attorneys general and its options with respect to the ruling in *Equal Employment Opportunity Commission v. Freeman (Freeman Decorating Services Inc.)*.

Observers, however, expect the EEOC to appeal Judge Titus' Aug. 9 ruling.

In the meantime, observers do not expect a significant change in the EEOC's policy.

If anything, the letter from the attorneys general and the Maryland judge's ruling "will cause (the EEOC) to become more focused on this issue," said Pamela Q. Devata, a partner with Seyfarth Shaw L.L.P. in Chicago.

Instead, the EEOC may calibrate its focus in future litigation and "look to see if they can't find a case where they've got a stronger set of facts and a concrete example of how an employer's policies have affected a specific individual," said Peter J. Gillespie, of counsel at Fisher & Phillips L.L.C. in Chicago.

By Judy Greenwald

The letter from the attorneys general and the Maryland judge's ruling "will cause (the EEOC) to become more focused on this issue."

Pamela Q. Devata,  
Seyfarth Shaw L.L.P.

need to balance your employee and customer safety with the fact there may be some criminal backgrounds that are completely irrelevant to the job."

She also said the EEOC has had a general policy on the issue since the 1970s. "This isn't new, but the enforcement of it is new," she said.

There are steps employers can take to avoid running afoul of the EEOC (see box, page 1).

The EEOC's policy "might even have the effect of absolving employers from the beginning, if they end up hiring someone with a criminal background and they're not allowed to ask about it" and

problems develop subsequently, Mr. Cohen said.

The issue "is probably going to be with us for the next few years, and one that will result in a change of behaviors by employers over a period of time," Mr. Fox said. "The threat of big litigation tends to focus one's mind."

# GALLAGHER

Continued from page 1

employee benefits business.

"They have a program business and many other aspects of the business that will allow Gallagher to diversify," Mr. Ward said.

For Gallagher, the Bollinger deal also provides a big footprint in the key Northeast market. With commercial and personal lines business, Bollinger operates eight offices in New Jersey, New York, Pennsylvania and Connecticut and is ranked No. 21 in U.S. business, according to the 2013 *Business Insurance* ranking. Gallagher is the third-largest broker of U.S. business.

J. Patrick Gallagher Jr., chairman and CEO, said in a statement announcing the Bollinger acquisition that the deal "gives us a unique opportunity to significantly expand our Northeastern operating platform."

A spokeswoman for the brokerage said that although the acquisition of Bollinger is Gallagher's largest buyout according to purchase price, the company's 2011 acquisition of London-based HLG Holdings Ltd. is the largest based on total annual revenue.

Meanwhile, Mr. Ward said brokers are looking to vary revenue streams by offering clients expertise in areas such as handling claims to augment their organic growth.

## Seeking diversification

Diversification also was a primary impetus behind Brown & Brown Inc.'s \$336.5 million June acquisition of Atlanta-based rival Beecher Carlson Holdings Inc. That was the biggest brokerage deal this year and the Gallagher purchase of Bollinger was the second-largest acquisition.

Giving Brown & Brown a foothold in the large-account arena, that deal was a departure

from the Daytona Beach, Fla.-based broker's previous acquisition strategy, said Timothy J. Cunningham, managing director of Chicago-based investment banking and consulting firm Optis Partners L.L.C.

"It breaks the mold for Brown & Brown and puts them in a different segment of the business," Mr. Cunningham said.

"The industry leaders all have expertise in searching for and zeroing in on acquisitions that fit their ambitions," said Bruce Ballentine, New York-based vice president and senior credit officer at Moody's Investors Service Inc.

The Beecher Carlson purchase came little more than a year after Brown & Brown spent \$400 million to diversify its offerings by acquiring managing general agency Arrowhead General Insurance Agency Inc.

Another example of the trend is the June purchase by Aon Global Risk Consulting, the risk consulting business of Aon P.L.C., of

Dempsey Partners L.L.C., a Wilton, Conn.-based provider of claims preparation and forensic accounting services for an undisclosed sum.

"There is an emerging claims presence in the top brokers, which could fuel more M&A activity in the short term," Mr. Ward said. "This is different from acquisitions that are done solely to build out the U.S. brokerage footprint."

Another reason for large brokerages to add new businesses rather than expand existing ones is that many of the large independent brokers that are the most likely acquisition targets by publicly-traded brokers recently have been recapitalized or changed private-equity backers.

"I see continued activity in the vertical acquisition front, but as big acquisitions become less available, there could be a shift to more horizontal acquisitions," Mr. Ward said. "When you look at their acquisition activity in the sector, it

has been very active the past few quarters."

However, such deals "may be slowing down a bit just due to the fragmented nature of the segment and lack of suitably large independent brokers that remain," he said.

Mr. Ballentine said acquisitions have been a way of life for brokers for years and there are plenty more acquisitions to come.

"The U.S. brokerage and agency sector is highly fragmented with hundreds of midsized firms and thousands of smaller firms that are targets for acquisition over time," Mr. Ballentine said.

Likewise, Julie Herman, New York-based associate director for Standard & Poor's Insurance Ratings, said she expects the deals to continue.

"Even though there has been plenty of acquisition activity in the past year, you don't hear the brokers saying that it is drying up," Ms. Herman said. "It's an incredibly robust pipeline."

# MERGERS

Continued from page 3

indemnity, you might ask for \$20 million while I could ask for just a \$2 million indemnity and purchase \$18 million in reps and warranties insurance, making my bid more attractive to the seller,” Mr. Schioppo said.

“Buyers also use it when there’s friction in the sales agreement. It’s a way to bridge the gap between buyers and sellers who can’t agree” on the amount of indemnity needed to close a transaction, he said.

Jeremy S. Liss, a partner at law firm Kirkland & Ellis L.L.P. in Chicago, began recommending representations and warranties insurance to clients involved in M&A activity about three years ago after discovering that terms and pricing for the coverage have improved significantly.

“We looked at this a long time ago, maybe 12 years ago. The carriers were too reluctant to underwrite it, and no one had any experience. Then about three years ago, we took another look. There was more of a marketplace,” he said.

Today, at least half a dozen insurers write representations and warranties insurance policies, providing up to \$300 million in capacity, Mr. Schioppo estimated.

Premiums for the coverage also have dropped precipitously from maybe 6 to 8 cents for each dollar of coverage 10 years ago to as little as 2 to 3½ cents per dollar today, sources said.

“Today, you would pay between \$200,000 and \$400,000 for \$10 million in coverage,” said Alex Jezerski, president of RT ProExec, a Bloomfield, Conn.-based insurance wholesaler, who said his firm has been receiving “between five and eight calls a week from brokers asking questions” about the coverage. He compared the nascent

interest in the product to “what employment practices liability insurance was like in the early ’90s.”

“If you think about how long you’d have to tie up that amount of money in escrow and the limited return on investment you’d get because you’d have to invest it conservatively,” representations and warranties insurance makes an attractive alternative, said Mr. Jezerski.

In some cases, “representations and warranties insurance can get a potentially stuck transaction unstuck,” he said. “We’re seeing the most interest in buyer-side policies, which protects the buyer from breaches made by the seller. Say the seller doesn’t want to agree to the amount of escrow requested by the buyer, or the length of the survival period. In a competitive bid situation, the seller could potentially walk away with more cash if the buyer gets a policy to reduce the amount of money placed in escrow.”

Peter Rosen, a partner at Latham & Watkins L.L.P. in Los Angeles, said “a fair amount” of his firm’s corporate and finance clients “have found that transactional risk policies can be very beneficial in minimizing their risk, whether as a seller or a buyer. Let’s say you’re a private equity firm and you’ve made some representations and warranties and want to backstop them with a policy so that if there is a claim, you don’t have to deal with it anymore from a financial standpoint. You’ve now passed the downside risk onto the carrier, and you can essentially close your books on that transaction.”

Alternatively, “say you’re a family-owned company that’s selling because the family owners are fighting with each other. They deposit funds into escrow, but they may not be enough to satisfy the various representations and warranties, and the buyer doesn’t want to chase the family members,” Mr. Rosen said.

# Streamlined underwriting simplifies transactional coverage

The underwriting process for transactional risk insurance is a lot smoother today than it was in the early days of the product, industry experts said.

In the past, deals were sometimes delayed while parties underwent the rigorous review and conscientious drafting of these mostly manuscript insurance policies.

“A decade ago, someone would think of the coverage as a bit of an afterthought. You’d come in like a SWAT team and try to write the coverage quickly,” said Carl Metzger, a partner in Goodwin Procter L.L.P.’s Boston office who focuses on risk management and insurance.

By contrast, “brokers today have gotten better at jumping on fast-paced situations, while the carriers have gotten better at promptly underwriting the coverage in an efficient, intelligent way so they don’t hold up the deal,” Mr. Metzger said.

That said, underwriting a representations and warranties insurance policy remains a two-step process, taking anywhere from a week to 10 days, sources said.

First, “the underwriter makes sure the proper due diligence has been done” by carefully reviewing all documents involved in the transaction, said Henry Jennings, a senior vice president at Lockton Cos. L.L.C. in New York.

This review is followed by a series of conference calls involving underwriters and all pertinent parties to the transaction.

For example, “if it’s a sell-side policy, underwriters will work primarily with the sellers. If it’s on the buy side, the underwriters deal with the buyer and the buyer’s advisers,” Mr. Jennings said.

Often, underwriters will ask “detailed questions about the types of risk inherent in the industry, such as patent infringement for a tech company,” said Craig Schioppo, transactional risk practice leader at Marsh Inc. in New

York. Or “they may talk to current management about the history of the company” being sold, he said.

All transactional risk insurance policy buyers are required to pay a nonrefundable underwriting fee ranging from \$10,000 to \$50,000, depending on the complexity of the transaction being covered, sources said.

“This separates the tire-kickers from the serious buyers,” said Alex Jezerski, president of RT ProExec in Bloomfield, Conn., a wholesaler that specializes in transactional risk insurance products.

“Once we finish the diligence review, the underwriters issue a base template policy tailored to respond to the purchase agreement,” said Mr. Jennings. “The policy is issued on the date of the closing and the premium is paid at closing. They sign a no-claim declaration saying they are unaware of any breaches at close.”

Buy-side policies typically are in place for six years, whereas sell-side policies mirror the survival period on the purchase agreement, Mr. Jennings said.

As underwriters gain greater experience with the types of claims that trigger representations and warranties insurance policies, they have become more flexible in negotiating coverage terms, said Peter Rosen, a partner at Latham & Watkins L.L.P. in Los Angeles.

“These policies are highly modifiable, manuscripted to match the deal structure,” Mr. Rosen said.

“People in the M&A business don’t want to wait a month to get a policy in place. As more people have used it and they’ve seen how it’s worked, we now have a history of getting these deals done very quickly. We can now do it in less than a week,” said Jay Rittberg, vice president for mergers and acquisitions insurance at American International Group Inc. in New York.

By Joanne Wojcik

# COSTS

Continued from page 3

Employer health plan design changes, such as significantly increasing employee cost-sharing by imposing higher deductibles, also have cooled demand for health care services as well as made employees more careful consumers of services.

“When employees have more skin in the game, they learn to be better consumers, and that has helped to dampen health care inflation,” said Michael Thompson, a principal with PricewaterhouseCoopers L.L.P. in New York.

Mercer L.L.C. statistics illustrate the growing prevalence of health plans that expose employees to more costs than traditional plans. For example, last year, 15% of employees working at large organizations — those with at least 500

## HEALTH PLAN COST COMPARISON

Group health insurance premiums for family health coverage vary by the design of a plan, including preferred provider organizations, health maintenance organizations, point-of-service plans as well as consumer-driven health plans.

Plan type	Average 2013 premium
PPO	\$16,671
HMO	\$16,543
POS	\$16,429
CDHP	\$15,227

Source: Kaiser Family Foundation

employees — were enrolled in high-deductible, consumer-driven health care plans. That is more than double the 7% of employees who were enrolled in such plans in 2008.

And the percentage of employees enrolled in these high-deductible plans is likely to go much higher,

especially as employers make them the only health plan design they offer.

“I think we will see a huge increase in CDHPs,” said Tracy Watts, senior partner in Mercer’s Washington office.

These plans not only expose employees to more costs, they also carry much lower premiums compared with more traditional plans, because of their high deductibles. For example, the average premium for family coverage through such a plan was nearly \$1,500 less this year than family coverage through a preferred provider organization (see chart).

At the same time, employers are exploring new approaches to help keep cost increases in check.

“Employers are getting more creative,” said Dave Ratcliffe, a principal in the Washington office of Buck Consultants L.L.C.

In recent years, one popular strategy employers have utilized

to try to hold down costs is to give employees a financial incentive to have various medical screenings to detect medical problems before they develop into expensive complications.

In a twist on that strategy, some employers now are making employees pay higher premiums if they don’t have certain screenings or take other steps to improve their health.

“It is a ‘stick’ approach. It is a form of cost-shifting to try to change behavior,” Mr. Ratcliffe said.

“You will pay more if you don’t play by the rules,” said Tim Nimmer, chief health actuary with Aon Hewitt in Denver.

Consultants say other cost-control strategies that are expected to grow over the next few years include providing greater coverage of services received by the most cost-efficient providers in a network and reference pricing, in

which an employer limits the coverage it will provide for a service to a fixed amount.

Still, there is one ultimate cost-control step that few employers appear willing to take: eliminate their health care plans, direct employees to public exchanges and bump up employees’ salaries to offset, at least partially, the premiums they will pay for coverage.

Last week, a Towers Watson & Co. survey of 420 large and midsize employers reported that 98% of respondents intend to continue to provide health coverage.

“Health care plans are a key part of employers’ rewards package. No one wants to be the first to do something so radical” as eliminating coverage, said Mark Olson, a senior Towers Watson consulting actuary in Boston.

“I do not have one client who plans to drop coverage and have not heard of one who will drop coverage,” Lockton’s Ms. Perez said.

# INTOXICATED

Continued from page 3

failing to prevent a patient from leaving the hospital in December 2006 while he was still intoxicated.

The patient, Kevin Kowalski, later wandered onto a nearby highway and was struck by a car, leaving him paralyzed below the neck. Throughout the case, Mr. Kowalski contended that even though he decided on his own to leave the hospital, the hospital should have prevented him from doing so based on his level of inebriation.

The appeals court ultimately rejected the lawsuit under the state's Mental Hygiene Law that, as do similar statutes in most states, neither permits nor requires health care providers to forcibly detain patients admitted voluntarily for treatment unless they pose a threat to themselves or others, or are unable to make informed decisions about their treatment. Still, legal experts say *Kowalski* highlights many of the legal risks inherent to treating and discharging intoxicated patients.

"The real value of this case for a hospital is that it gives them some guidance and some comfort in knowing what their obligations and duties are when presented with an intoxicated patient who says he wants to leave," said Jeffrey Araten, a New York-based partner at Wilson Elser Moskowitz Edelman & Dicker L.L.P., which represented St. Francis Hospital.

"Barring specific circumstances, hospitals can't lock someone up or restrain them just on the basis of that person being intoxicated," Mr. Araten said. "Intoxication is not in and of itself enough to warrant involuntarily confining a patient."

Perhaps the most salient lesson for risk managers and medical staff from *Kowalski* is the imperative nature of detailed, real-time record-keeping of all interactions with an intoxicated patient from the time they are admitted to the time they are discharged.

"First and foremost, documentation is the most important thing any doctor or hospital staff can do to protect themselves," said Marshal Endick, Wilson Elser's lead attorney in *Kowalski*. "Document what was done in terms of treatment, what was told to the patient, how the patient was evaluated and any advice not to leave that was

given to the patient."

"In this case, we relied very heavily on the documented physical observations of the patient, that he was able to walk and answer questions," said Judy Selmecci, a New York-based associate at Wilson Elser. "Those kinds of notes were immensely helpful to us."

Health care legal experts also said *Kowalski* underscores the value of reviewing records of any prior admissions. Although staff members at St. Francis admitted that they did not consult records of Mr. Kowalski's prior visit to the hospital — during which he had presented as a suicide risk and was placed under continuous watch — the appeals court noted

that nothing in that record would presumably have altered the treatment he received during the subsequent visit.

"If this had been an emergency room situation, the value of that omission of prior information becomes much more significant to a plaintiff," said Pamela Popp, executive vice president and chief risk officer at Western Litigation Inc. in Denver. "In a perfect world, we would check for prior records every time someone is admitted, whether it's voluntary or a medical emergency, but there's a lot of challenge in the volume and time it takes to determine what information is readily available."

Finally, experts said *Kowalski*



## HEAR INTERVIEW

Access the *Business Insurance* interactive digital edition to hear Pamela Popp of Western Litigation Inc. discuss best practices for treating/discharging intoxicated patients.

should be an impetus for hospital risk managers and medical staff to ensure that their organization has a formalized set of policies outlining procedures to manage the admission, treatment and discharge of intoxicated or otherwise

cognitively impaired patients in accordance with state and federal laws, as well as additional requirements set forth by their accrediting entity.

"There are certain agencies that mandate that you do review those policies every so often," said Cynthia Green, a Sarasota, Fla.-based clinical risk consultant at Hub International Inc. "For instance, if you're accredited by the Joint Commission, you're required to review your policies every two or three years. Other hospitals have decided on their own that it's important to review their policies on an annual basis. That's probably the most appropriate approach if it's a patient safety or clinical policy."

# BUSINESS INSURANCE

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# WORKERS

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health care industry are relatively new because limited risk management budgets have focused more on patient safety, said Lori Severson, health care loss control consultant for Lockton Cos. L.L.C. in Denver. Patient safety has received greater media, regulator and public survey scrutiny than workers comp losses, she said.

“So I see an imbalance between patient safety and employee safety in health care, but it’s tipping stronger (toward employee injury loss reduction as employers) see that the total cost of risk is very heavy for work comp and they need to change that,” Ms. Severson said.

Studies calling for systemwide improvements, meanwhile, continue reporting a substantial number of worker injuries.

Last month, for example, a non-profit consumer organization named Public Citizen issued a report questioning the U.S. Occupational Safety and Health Administration’s ability to protect health care workers.

“In 2010, for instance, health care employers reported 653,900 workplace injuries and illnesses ... 152,000 more than the next most afflicted industry sector, manufacturing,” according to the report, citing U.S. Department of Labor data.

Neither OSHA shortcomings in overseeing health care operations, nor the industry’s worker injury rates are surprising, experts say.

Barry Weiner, senior vice president and account executive for Aon Risk Solutions in Philadelphia, for example, said his advising career has spanned pulp and paper manufacturers and health care companies.

“You would think pulp and paper



ZDENKA DARULA/SHUTTERSTOCK.COM

manufacturing would be one of the most dangerous, hard-to-fix industries you could think of,” Mr. Weiner said. “But ironically, health care is 10 times the challenge and certainly has a higher incident rate than heavy manufacturing.”

The potential dangers health care workers face include blood-borne pathogens, drug and chemical exposures, needle sticks, radioactive materials, violence, slip-and-fall accidents, and back or musculoskeletal injuries from lifting or repositioning patients.

But “the two biggest risks for hospitals and nursing homes include combative behavior, and the biggest one (overall) is the lifting risk,” said Steve Cooper, pres-

ident of United Wisconsin Insurance Co., a Milwaukee-based workers compensation insurer that, as United Heartland, underwrites more than 400 hospitals and nursing homes.

Data shows that to be the case.

In 2010, nursing aides, orderlies and attendants suffered 249 incidences per 10,000 workers of musculoskeletal disorders, such as back injuries due to lifting, that required days away from work, according to U.S. Department of Labor data. In contrast, the average rate for all workers during the year was 34 per 10,000 workers, according to the Public Citizen research.

Violence, including assaults and threats of assault, also occur more

frequently in health care settings.

On average throughout the past decade, health care workers have accounted for two-thirds of all U.S. nonfatal workplace violence injuries involving days away from work, prompting the National Institute for Occupational Safety and Health to announce earlier this month a free online violence prevention training course for nurses.

The losses mean many insurers decline to write health care accounts.

A high rate of costly claims drove Employers Holdings Inc. to shy away from underwriting long-term care facilities beginning about four years ago, said Steve Festa, chief claims officer for the

# 249: 10,000

In 2010, nursing aides, orderlies and attendants suffered **249 incidences per 10,000 workers** of musculoskeletal disorders, such as back injuries due to lifting, that required days away from work, according to U.S. Department of Labor data. In contrast, the average rate for all workers during the year was 34 per 10,000 workers, according to Public Citizen research.

Reno, Nev.-based workers compensation insurer.

The insurer also found providing return-to-work opportunities was problematic at long-term facilities because the workers typically are older, requiring longer recovery times, and the facilities could not provide enough modified-duty positions, Mr. Festa said.

“We are not comfortable the (long-term care) industry is where it needs to be yet,” Mr. Festa said. “But some (long-term care facility operators) are recognizing that the injuries are expensive and they need to think differently from a loss control standpoint.”

United Heartland won’t bind a health care account unless their executive management team shows it is committed to safety and will work with the insurer’s loss control services to make improvements, Mr. Cooper said.

Loss control measures that hospitals and nursing homes have adopted include installing patient-lifting technology and training nurses to recognize dementia patients’ nonverbal cues, Ms. Severson said.

Even larger, self-insured hospitals, have faced economic challenges that have limited them to “taking infant steps” on employee safety improvements, she said.

Efforts to improve are being helped, however, by greater recognition of a link between patient safety and worker injuries, Mr. Weiner said. Fewer worker injuries mean there are more hospital employees on the job to provide care, he said.

The statistics do not yet reflect improvements, however, because the efforts are still maturing, Mr. Weiner said.

“These programs are just being understood and implemented,” he said. “We are not reaping the benefits of them yet.”

## Safety standard for patient lifting under consideration in Congress

Federal legislation introduced this summer seeks to reduce worker musculoskeletal injuries by creating a national standard for the safe lifting and moving of patients in health care facilities.

A lack of nationally recognized safety standards is among issues hampering U.S. Occupational Safety and Health Administration efforts to reduce a high rate of worker injuries in hospitals and nursing homes, experts say.

The Nurse and Health Care Worker Protection Act of 2013, sponsored by Rep. John Conyers Jr., D-Mich., was introduced and referred to committee on June 25.

It incorporates safe patient-handling practices developed by a working group organized by the Silver Spring, Md.-based American Nurses Association, said Lori Severson, health care loss control consultant for Lockton Cos. L.L.C. in Denver.

Ms. Severson participated in the working group, as did ergonomics experts, physical therapists, patient-handling equipment manufacturers and others, the nurses association said.

They created eight core components or best practices that can be implemented across all aspects of health care. About a dozen states have adopted their own standards, but overall there is a lack of consistency in implementing patient-handling practices that reduce worker injuries, she said.

“Here is one of the leaders causing huge dollars being spent on workplace injuries, and there are no occupational safety standards addressing it,” Ms. Severson said.

But incorporating such standards into law could give OSHA inspectors the ability to review health care companies’ implementation of the practices.

By Roberto Cenicerros

“Here is one of the leaders causing huge dollars being spent on workplace injuries, and there are no occupational safety standards addressing it.”

Lori Severson,  
Lockton Cos. L.L.C.

## Michael Van Gilder gets probation, \$5,000 fine

■ Michael Van Gilder, who resigned as CEO of Denver-based Van Gilder Insurance Corp. last October after being indicted on five counts of insider trading, was sentenced to five years of probation, six months of house arrest and a \$5,000 fine. Mr. Van Gilder pleaded not guilty to the counts of securities fraud last year but he changed his plea in May as part of a plea agreement, admitting to a single count in connection with illegally profiting from a December 2007 purchase of stock in Delta Petroleum Corp. just before a private investment firm acquired a 35% stake in the company.

## Legally wed same-sex couples eligible for FMLA leave

■ Legally wed same-sex couples are now eligible for family emergency leave benefits, according to an internal memo sent to staff members at the U.S. Department of Labor. The department has updated several of its guidance documents regarding the federal Family and Medical Leave Act to reflect the U.S. Supreme Court's June 26 ruling striking down Section 3 of the Defense of Marriage Act, which had prohibited federal agencies from recognizing legal same-sex marriages. In his memo to department staffers, Labor Secretary Thomas Perez said references to DOMA have been removed from FMLA guidance documents and affirmed the availability of spousal leave benefits for legally married same-sex couples.

## Vermont licenses 13 captives so far in 2013, expects more

■ Vermont has licensed 13 new captives so far this year, with signs of an active fourth quarter of formations ahead, said David F. Provost, deputy commissioner of the Captive Insurance Division in the Vermont Department of Financial Regulation. Mr. Provost said five health care captives writing medical malpractice coverage and four risk retention groups are among the Vermont captives licensed so far in 2013.

## Former Willis head Plumeri joins KKR as senior adviser

■ Joseph J. Plumeri has been appointed as senior adviser at New York-based investment firm Kohlberg Kravis Roberts & Co. L.P. and has joined the board of directors of First Data, a KKR company. Mr. Plumeri until July was chairman of Willis Group Holdings P.L.C.

## Workers comp benefit costs rise on improving economy: Report

■ Workers compensation benefit costs rose 3.5% nationwide in 2011 compared with 2010 as the economy improved, according to a report by the National Academy of Social Insurance. Injured workers received \$60.2 billion in workers comp benefits in 2011, the latest year for which statistics are available, according to NASI. That figure included a 4.5% increase in medical spending and a 2.6% increase in wage replacement benefits over 2010. Employer costs related to comp claims, including benefit payments and administration costs, increased 7.1% in 2011 over 2010 to \$77.1 billion, the NASI report

said. However, the organization noted that employer costs have been lower from 2009 to 2011 than at any other point in the past 30 years.

## 98% of employers to continue offering health care plans: Survey

■ Nearly all employers expect to continue offering health care plans to employees in 2014 and 2015, but many are considering discontinuing coverage provided to Medicare-eligible retirees, according to a survey. Ninety-eight percent of employers responding to a Towers Watson & Co. survey said they have no plans to stop offering coverage over the next two years and instead direct employees to public exchanges authorized by the health care reform law that will offer coverage effective Jan. 1

## Wells Fargo Insurance executive dies on business trip

■ Anne J. Doss, executive vice president and head of personal and small business insurance for Wells Fargo Insurance, died Aug. 14 while on a business trip, the company confirmed. Ms. Doss, 56, died unexpectedly in her hotel room in Bloomington, Minn. Based in Charlotte, N.C., Ms. Doss previously led the insurance national practices and special risk group at Wells Fargo and was serving as president of Wachovia Insurance Services when the company was acquired by Wells Fargo in 2008. She is survived by her husband, son and daughter.

## NCCI recommends 1% increase for Florida workers comp rates

■ Florida employers would see a 1% workers compensation rate increase beginning Jan. 1 under a new rate filing from the National Council on Compensation Insurance Inc. Florida's Office of Insurance Regulation announced the filing and said it will conduct a public hearing in early October to help evaluate the rate request's potential impact on employers and the state's workers comp insurance market. If adopted, Florida's workers comp rates would still be 55.9% below their level when the state passed reforms in 2003, the Office of Insurance Regulation said.

## Hawaii captive administrator George Sumner resigns

■ George Sumner has resigned as Hawaii's captive insurance administrator and deputy insurance commissioner, effective Aug. 29. Mr. Sumner had been captive insurance administrator for more than three years. Sanford Saito, captive insurance examiner, is expected to be named interim head of the state's captive insurance operation, according to a statement from the Hawaii Captive Insurance Council.

## Financial agencies urge firms to prepare for natural disasters

■ A staff advisory on business continuity and disaster recovery planning issued by three federal agencies, including the U.S. Securities and Exchange Commission, says firms should prepare for widespread disruption and consider alternative locations in light of the damage caused by Superstorm Sandy. The advisory issued by the SEC, the Commodity Futures Trading Commission's Division of Swap Deal-

er and Intermediary Oversight, and the Financial Industry Regulatory Authority comes after a joint review by regulators in the aftermath of Sandy, which caused widespread damage to Northeastern states and closed U.S. equity and options market for two days in October 2012.

## Women save less through defined contribution plans

■ Women on average save less through their employers' defined contribution plans than men and are more likely to default on plan loans, according to a new report. On average, women contribute 6.9% of pay to defined contribution plans, such as 401(k) plans, sharply lower compared with men, who contribute an average of 7.6% of pay, according to Aon Hewitt. In addition, 31% of women contribute less than the amount needed to be eligible to receive a matching contribution from their employers, compared with 25% of men.

## Berkshire Hathaway Specialty adds underwriting execs

■ Berkshire Hathaway Specialty Insurance Group, the new commercial insurance arm of Berkshire Hathaway Inc., announced the addition of two senior executives to lead its underwriting units for the health care and construction industries. Leo J. Carroll, formerly of Zurich North America, has been named senior vice president of the Boston-based specialty insurer's health care professional liability unit, while William B. Sullivan, from The Hartford Financial Services Group Inc. has been appointed vice president of the company's construction casualty unit.

## BP spill claims deadline may slip by year or more

■ The April 2014 deadline for compensation claims against BP P.L.C. over its U.S. oil spill is almost certain to be extended, say both sides of the legal settlement that governs payouts, possibly into 2015. The last date for claims, part of the oil company's settlement last year with individual and business claimants, was always potentially moveable, but the indefinite extendibility may not have been fully appreciated by long-suffering investors, analysts say. Extension might not make much difference to the total number and cost of relevant claims — \$9.6 billion at the end of June and rising — but it would drag on the company's hopes of leaving behind the wider Gulf of Mexico oil spill litigation saga.

Reuters

## OSHA proposes regulations for airborne silica dust

■ The Occupational Safety and Health Administration announced that it is proposing to create a rule for preventing silicosis by lowering workplace exposure to crystalline silica particles. Silicosis is an incurable and progressive disease. Exposure to airborne silica dust occurs in operations involving practices such as the cutting and crushing of concrete and stone products and in the use of sand such as for glass manufacturing. Exposure to silica is responsible for lung cancer, chronic obstructive pulmonary disease and kidney disease. OSHA's proposed rule would limit exposure to crystalline silica to 50 micrograms per cubic meter in the workplace.

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## Official mocks comp, then files for it

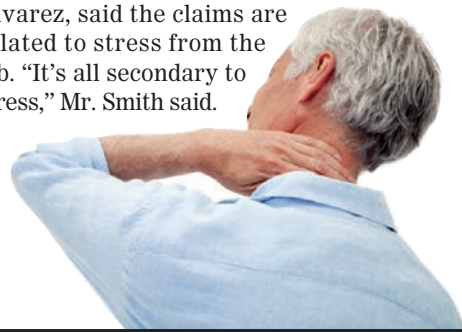
**A** former San Francisco city official famously skeptical of workers compensation claims is now asking the city to cover a claim contending that he was injured by stress on the job.

According to a report in *The SFGate*, Henry Alvarez, the former head of the San Francisco Housing Authority, filed the claim on April 26, two weeks after being fired from his post. Mr. Alvarez claims that he sustained injuries to his back and neck and seeks disability payments, health care and a voucher worth up to \$10,000 for job training, according to the report.

Ironically, while at his post, Mr. Alvarez clashed with several employees over their use of disability and paternity leave. Two former employees have filed suit against Mr. Alvarez and the Housing Authority for discrimination after being fired while on disability leave.

"We find it the height of hypocrisy that after an extensive record of saying that anyone who takes workers comp is a malingerer and a fraud, Mr. Alvarez then files for it," Heidi Machen, an attorney for one of the workers, told the newspaper.

Byron Smith, an attorney for Mr. Alvarez, said the claims are related to stress from the job. "It's all secondary to stress," Mr. Smith said.



## Fraudster moves to the big house

**A** San Diego woman caught carrying heavy boxes while claiming to be wheelchair-bound reportedly was sentenced this month to a year in jail and ordered to pay restitution for workers compensation fraud.

Yolandi Kohrumel broke her toe in 2002 while working for Staples Inc., according to *KSWB-TV* in San Diego. Unable to use crutches, she was provided first a manual wheelchair and later an electric wheelchair. She claimed to suffer numerous health conditions, including depression and hypersensitive feet, that kept her in the chair for nine years.

Her father, Anton Buitendag, also participated in the scheme, claiming to provide her around-the-clock health care, reports said. He sought payments of \$324,000 from third-party administrator Esis Inc. and insurer American International Group Inc. for his services.

The scheme was uncovered when movers saw Ms. Kohrumel get out of her chair and lift heavy boxes while moving to a bigger house that she had requested from AIG to accommodate her wheelchair, reports said. They were ordered to repay \$1.6 million to Esis at sentencing.

## POLICYHOLDER WOWS INSURER WITH GOLD CLAIM



AP PHOTO

Fans play "World of Warcraft: Mists of Pandaria." A player in Australia fought with her insurer after her winnings from the game were stolen.

**S**ometimes virtual gaming can have real-world consequences, as one Australian nurse discovered when her home was robbed and thieves absconded with \$75,000 in gold she "farmed" by playing "World of Warcraft." Gold farming is conducted by selling virtual game currency won while playing the online multiplayer "World of Warcraft" games for real-world money.

Katrina Fincham took her victory spoils and had them made into gold bars, which she locked in a safe in her home.

But even though Ms. Fincham had purchased insurance to cover the gold, her homeowners insurer, Melbourne, Australia-based AAMI, denied the claim, instead accusing Ms. Fincham of insurance fraud. After a police investigation later revealed that it was Ms. Fincham's boyfriend who tipped off the robbers that her home would be vacant, and that she had no part in the theft, AAMI has agreed to settle the insurance claim.

But Ms. Fincham's victory against her insurer came at a high price: Besides losing her boyfriend, Ms. Fincham was forced to sell her home to cover the cost of a bad-faith lawsuit she filed against her insurer.

Terms of the settlement are being kept confidential, but rumor has it that Ms. Fincham is asking that AAMI pay part of her claim in gold coins.

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## Facebook does investigator's job

**A** free Facebook account sometimes turns out to be pretty expensive, as one man has found out.

Michael Mallory was injured while working in Ohio and started collecting workers compensation benefits, according to the Ohio Workers Compensation Bureau's special investigations department. He moved to Arizona, where he took a construction job but illegally continued to collect Ohio workers compensation benefits, according to the bureau.

That might have been the end of it, but Mr. Mallory decided to let people know what he was up to. Based on a tip, investigators found photos on his Facebook page of him wearing rappelling gear and doing rappelling work while on the job. The construction company with whom he was employed also confirmed he worked there.

Recently, in the Franklin County, Ohio, Court of Common Pleas, Mr. Mallory pleaded guilty to workers compensation fraud and was ordered to pay the bureau \$7,600 in restitution and investigative costs.

## Giving new meaning to life in the slow lane

**G**as prices and eco-friendly inclinations are driving more cities nationwide to allow golf carts to putter down their public streets, raising safety and risk management concerns.

Cities from Kentucky to Minnesota are joining others that already have expanded the legal use of carts beyond the golf course and retirement community over the past decade, according to recent news reports. But some worry that mixing the lightweight carts — sans air bags — with faster-moving trucks and large sport utility vehicles could prove hazardous.

States allowing golf-cart type vehicles to roam streets are carving out exceptions to life-saving safety regulations and years of work by insurers, automakers and the federal government to make driving safer, states a 2010 report from the Insurance Institute For Highway Safety.

In response, cities are adopting regulations and giving out safety advice. Some are allowing operation only during daylight hours, limiting the number of passengers they carry and advising drivers to avoid sharp turns. Others are requiring the carts to display slow-moving emblems — as if other drivers might confuse them with a capable sports car.



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- **Charisse McCumber**, vice president at Holmes Murphy & Associates in Dallas.
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- **Jim Millaway**, a producer at The Holmes Organization in Tulsa, Okla.
- **Morgan H. Moore**, an account executive in the energy practice of Arthur J. Gallagher & Co.'s Houston Galleria office.
- **Mike Noyes**, a partner at The Noble Group in Sugar Land, Texas.
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