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September 3, 2012

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HURRICANE ISAAC CAUSES UP TO $2 BILLION IN LOSSES ON GULF COAST / PAGE 3

ACQUISITIVE VALIDUS SEEKS TO BUY FLAGSTONE FOR $600 MILLION / PAGE 3

INSURERS, EMPLOYERS WELCOME NEW MASS. LAW ON MEDICAL COSTS / PAGE 3

inBrief

N. American reinsurers post strong results

The North American reinsurance sector posted strong financial performance numbers in the first half of 2012, according to data released by the Reinsurance Association of America. The 19 U.S. property/casualty reinsurers in the RAA survey collectively wrote $14.6 billion of net premiums during the six months of 2012, a 5.8% increase from the amount written during the same period in 2011.

Construction industry faces rate hikes

Insurers are seeking rate hikes of 5% to 15% for primary casualty construction business, Marsh Inc. said in a special report. But, "risks with high loss

See **IN BRIEF** page 21

SPOTLIGHT

INSURER CAPITAL MANAGEMENT

Insurance-linked securities bolster traditional reinsurance; insurers look beyond bonds; ERM essential for P/C insurers. **PAGE 9**

HEALTH INSURERS

WellPoint seeks new direction

Braly blamed for weak earnings; successor sought

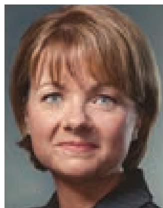
By **MATT DUNNING**

Correcting the management missteps and anemic earnings that led to last week's abrupt departure of Angela Braly as president and CEO of WellPoint Inc. must be a top priority for her successor, analysts said.

Ms. Braly, the Indianapolis-based managed care company's chief executive since 2007, stepped down last week amid growing pressure from investors dissatisfied with the company's financial performance.

In a statement, WellPoint said it is actively searching for a successor.

John Cannon, an executive vice president and WellPoint's general counsel, corporate secretary and chief public affairs officer, has been named interim president and CEO. Jackie Ward, the company's lead director, will replace Ms. Braly as a nonexecutive chair of WellPoint's board of directors.



Ms. Braly

JUNE 2007
- Named president and CEO

MARCH 2010
- Named board chair

AUGUST 2012
- Exits WellPoint

In the statement, Ms. Ward said the board stands behind strategic decisions made during Ms. Braly's five-year tenure, but felt that "now is the right time for a leadership change."

"Our board continues to believe that time will prove the wisdom of potentially transformative actions taken under Angela's leadership," Ms. Ward said. "We believe the remaining executive team is dynamic and strong, with great potential to drive WellPoint's future success."

A WellPoint spokeswoman said Ms. Braly did not plan to comment on her departure from the

See **WELLPOINT** page 7

LIABILITY & LITIGATION

REUTERS

Apple's patent infringement verdict over Samsung puts a spotlight on intellectual property risks that high-tech companies face.

Apple's patent victory puts focus on tech risks

By **RODD ZOLKOS**

The landmark $1.05 billion patent infringement verdict that Apple recently won against Samsung won't stop innovation, but it is likely to draw more attention to intellectual property risks.

The ruling also could cause companies to rethink whether they try to deal amicably with competitors during product development, instead of litigating once a product is put on the market, experts say.

In its verdict in late August, a federal court jury in San Jose, Calif., hit South Korea-based Samsung Electronics Co. Ltd. with a $1.05 billion judgment for violating Apple's patents by "willfully" copying the Apple iPhone and iPad in devising and marketing Samsung products.

Last week, Apple asked U.S. District Court Judge Lucy Koh to order Samsung to pull eight products from U.S. shelves. The judge will rule on Apple's request at a Dec. 6 hearing.

In a prepared statement, Samsung said it plans to appeal. "This is not the final word in this case or in battles being waged in

See **APPLE** page 2

INTERNATIONAL

Insurers eye refinery risks after Venezuela blast

By **STUART COLLINS**

The fire and explosion that killed 42 and injured more than 100 at a Venezuela oil refinery late last month added to a growing trend of onshore energy losses and may lead to greater scrutiny of all refinery risks by underwriters.

But the blast at the Petróleos de Venezuela S.A. refinery in Los Taques, Venezuela, likely won't lead to a major loss for the international insurance market and it is not expected to alter market conditions significantly, according to energy insurance experts.

AP PHOTO

An explosion and fire rocked Venezuela's largest refinery late last month.

The state-owned oil producer did not purchase business interruption coverage for the site, and much of the loss is expected to be retained within PDVSA's Bermuda-based captive, they say.

The Aug. 25 explosion ripped through the area surrounding the refinery, destroying homes and businesses. The accident is one of the worst for the energy sector over the past several years. Production at the plant was still suspended last week.

Caracas, Venezuela-based PDVSA owns a Hamilton, Bermuda-based captive, PDV Insurance Co. Ltd., which has a reinsurance program that is led in the London Market by QBE European Operations P.L.C., a unit of QBE Insurance Group Ltd. in Sydney. The coverage was placed by Cooper Gay & Co. Ltd. in London. QBE and Cooper Gay confirmed their

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NEWSPAPER

Business Insurance

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gallery

CROP DAMAGES: The drought devastating crops across the country also is affecting insurers and reinsurers. View this *Business Insurance* photo gallery to see how the Federal Crop Insurance Program can help. *www.BusinessInsurance.com/photos*

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2. Most employers to continue offering health plans in 2014
3. Claims with opioid prescriptions likely to become catastrophic
4. DSW wins dispute with Chartis unit over data theft coverage
5. GOP VP nominee Paul Ryan says PPACA has 'no place' in U.S.
6. Passage of Calif. comp reform bill could lead to reduced rates
7. Enstar to buy workers comp insurer SeaBright in $252M deal
8. No penalties for employers not offering dependent coverage
9. Lloyd's prepared for challenges to business model
10. Apple seeks quick bans on eight Samsung phones

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Apple: Focus on tech risks

CONTINUED FROM PAGE 1

courts and tribunals around the world, some of which have already rejected many of Apple's claims. Samsung will continue to innovate and offer choices for the consumer." Samsung declined to comment beyond its statement.

Indeed, a Tokyo court ruled Friday that Samsung's mobile devices did not violate an Apple patent used in synching mobile devices and computers.

While many experts expect "ripple effects" from the U.S. verdict, "the real unknown at this point is the scope of any injunction. If it is broad, it could force major product redesigns," said Mark A. Lemley, the William H. Neukom professor at Stanford Law School at Stanford University in California. "It certainly raises the legal risk, but I don't think it will stop innovation."

Edward J. Larson, professor and Hugh & Hazel Darling Chair in Law at the Pepperdine University School of Law in Malibu, Calif., said he thinks the breadth of the patent rights afforded Apple in the "powerful decision" may prompt more caution in research and development of new products.

He said he could see other companies try to take advantage of similarly broad patent protections. For example, "I can see people using it more broadly in patenting medical procedures," Mr. Larson said.

Richard S. Betterly, president of Betterly Risk Consultants Inc. in Sterling, Mass., said he thinks companies likely will pay more attention to intellectual property issues as a result of the landmark U.S. ruling against Samsung.

Patent attorneys' influence on research and development and design also might increase, although Mr. Betterly said he was uncertain about the role of risk managers.

"I don't know how many risk managers get involved in intellectual property activities," he said. "My experience is not so much."

But Roger L. Andrews, director of risk management at E.D. Bullard Co. in Provo, Utah, and a former president of the Risk & Insurance Management Society Inc., said he thinks the Apple-Samsung case could add patent infringement issues to risk management duties at many companies.

"These ancillary matters that traditionally wouldn't concern risk management, increasingly these things seem to become risk management issues," Mr. Andrews said. "If you're into enterprise risk management, your focus should be on managing the risks whatever they are.

"I work for a manufacturer and always had some interface with research and development, new product development, especially when it gets to the point of labeling, warnings that kind of thing," Mr. Andrews said.

"It would be a rare risk manager who might be able to see the distinctions between what you're developing and the patents already in place," he said. "But at least there should be a process by which they're reviewed by the appropriate people."

Andrea M. Matwyshyn, assistant professor of legal studies and business ethics at the Wharton School of the University of Pennsylvania in Philadelphia, said many industries face similar issues.

"There's a bit of an innovator's dilemma that happens in situations particularly in high R&D industries where it's expected, and almost inevitable, that there will be some design overlap, even among products that were independently designed," she said.

At many companies, the strategy is to "tell the R&D people, 'Don't do any patent research. Just invent … we'll clean up the legal later,'" Ms. Matwyshyn said. "That approach allows a more fertile space for development, but inevitably it leads to more inefficiencies down the road."

A "broader risk management dynamic" at many companies involves whether the company should try to work with competitors on licensing or other contractual arrangements before products come to market, she said. While there were such discussions between Apple and Samsung, the companies couldn't come to terms.

"Had they struck a deal in the licensing negotiations, it's entirely possible that much of this litigation could have been avoided," she said.

The decision whether to try to be conciliatory with a rival in the product development process and achieve predictability or to be more adversarial and "roll the dice" with litigation later is a "major risk management decision," she said.

That decision also depends on an organization's culture. "For some companies, unfortunately, they don't recognize that it is a business decision," ultimately taking the litigation route by default, Ms. Matwyshyn said.

"I think some participants, particularly in the technology ecosystem, will be more likely to consider all possible strategies for handling infringing (intellectual property)," she said. "Whether that will result in a change in strategy is unknown, of course, but at least for some companies it will open the conversation."

Commercial insurance availability limited

Commercial insurance available for patent infringement or intellectual property violations is limited, a risk management consultant said.

"There's not much out there for limits," said Richard S. Betterly, president of Betterly Risk Consultants Inc. in Sterling, Mass. "For a larger company, it's not an easy thing to insure. For a smaller company, it's insurable but cumbersome."

In an April review of the intellectual property insurance market in the Betterly Report, the company said coverage available "is the province of highly specialized sources such as Lloyd's, Liberty International and ProSight Specialty, with two exceptions." Those are patent infringement indemnity coverage available through Chartis Inc. and coverage offered by ThinkRisk Underwriting Agency, backed by Great American Insurance Co., for infringing the aesthetic design of products.

"It's still rather a challenging thing to buy" with "rather low limits," Mr. Betterly said. "That's not to say there isn't coverage at the captive level that's invisible or coverage that's buried in a general liability policy."

While intellectual property policy limits of $25 million used to be commonly available, today's "carriers, I think, are just scared to death of the risk," he said.

Betterly's April report said efforts to obtain coverage in intellectual property infringement cases through commercial general liability policies rarely succeed.

—By Rodd Zolkos

EMPLOYMENT PRACTICES

Ruling on confidentiality may hamper work probes

Onus on employers to argue business case for worker silence

By JUDY GREENWALD

A National Labor Relations Board ruling that forbids employers from issuing blanket rules ordering workers to keep investigations confidential could seriously hamper and even undermine such investigations, some experts say.

While the NLRB ruling permits employers to require worker confidentiality in an investigation if they can provide a valid business reason, it puts the onus on employers and adds an unnecessary step in such investigations, they say.

Observers describe the rule in *Banner Health System, DBA Banner Estrella Medical Center and James A. Navarro* as part of the NLRB's strategy to remain relevant in today's prevailing nonunion environment (see related story).

But experts differ in their advice about how employers should respond to the ruling (see story, page 17).

"To justify a prohibition on employee discussion of ongoing investigations, an employer must show that it has a legitimate business justification that outweighs employees' Section 7 rights," an NLRB panel ruled 2-1 in the July 30 *Banner* decision.

Section 7 of the National Labor Relations Act gives union and nonunion workers the right to engage in "concerted activities for the purpose of collective bargaining or other mutual aid or protection."

The case involved a human resources consultant who routinely asked employees at the Phoenix medical center who made a complaint not to discuss the matter with co-workers while the investigation was ongoing. Such a request "had a reasonable tendency to

See **CONFIDENTIAL** page 17

Labor relations board churning out regulations

Observers say the National Labor Relations Board's July 30 ruling on confidentiality comes after board rulings on the use of social media in the workplace and positions it has taken against handbook language that suggests employees' at-will status cannot be changed.

On May 30, the NLRB issued its third report on social media policies, in which it cited six cases where it contended that employers' policies and rules were overbroad and unlawful. The NLRB had issued previous reports on social media in August 2011 and January of this year.

And in a February ruling involving the Arizona Blood Services Region of the American Red Cross in Tucson, an administrative law judge held an agreement in its handbook that employees were required to sign stating that an "at-will relationship cannot be amended, modified or altered in any way" was "overly-broad and discriminatory."

Many observers describe these rulings as being part of a strategy to remain relevant in today's workforce, where just 7% of workers in the private sector are unionized.

Jonathan T. Hyman, a partner with Kohrman Jackson & Krantz P.L.L. in Cleveland, said the board "is really sticking its nose into issues it really doesn't understand, and I think the NLRB should not meddle into these types of common" human resources practices.

However, Susan Davis, a partner with Cohen Weiss & Simon L.L.P. in New York, which represents the interests of labor and individuals said it is "one of the best-kept secrets in the world that the NLRB applies equally strongly in a nonunion setting, and a fair amount of what the Obama board has done is reiterate employees in a nonunion setting have rights." This is true regardless of what percentage of the workforce is unionized, she added.

An NLRB spokeswoman had no comment.

—By Judy Greenwald

CATASTROPHES

AP PHOTO

Interstate 10 was partially submerged by floodwaters from Hurricane Isaac in LaPlace, La. New Orleans itself was spared, thanks in large part to a new levee system built after 2005's Hurricane Katrina.

Isaac drenches Gulf Coast, leaves New Orleans intact

By BILL KENEALY

Hurricane Isaac, packing high winds and heavy rain, left insured damage as high as $2 billion along the Gulf Coast last week, but spared New Orleans a repeat of the devastation Hurricane Katrina inflicted seven years ago.

As a Category 1 hurricane, Isaac made landfall in southeastern Louisiana, but its maximum sustained winds of 80 mph bypassed downtown New Orleans.

GALLERY: View *BI*'s Protecting New Orleans photo gallery at *www.BusinessInsurance.com/photos.*

Nonetheless, almost eight inches of rain fell at the city's airport, and nearby Plaquemines Parish, La., suffered extensive flooding when storm surge and heavy rainfall pushed water over levees.

Although Isaac quickly weakened to a tropical storm after landfall, it caused five deaths in Louisiana and Mississippi, and knocked out power for an estimated 900,000 customers across five states, including portions of New Orleans. The city's levee system, rebuilt after Katrina, remained intact last week.

The death toll on the Gulf Coast was less than the 29 people killed from the tropical storm that first hit the Dominican Republic and Haiti, as the storm made its way through the Caribbean.

Oakland, Calif.-based catastrophe risk modeling firm Eqecat Inc. estimated U.S. onshore insured losses as high as $1.5 billion while Boston-based AIR Worldwide Corp. estimated them as high as $2 billion.

Tim Doggett, principal scientist at AIR, said the slow-moving storm dumped up to 25 inches of rain over a 36-hour period in certain areas of the Gulf Coast.

"This is definitely not your standard Category 1 hurricane," Mr. Doggett said. "The longevity has been pretty noteworthy."

See **ISAAC** page 19

REINSURANCE

Validus seeks more growth with bid for rival Flagstone Re

By MARK A. HOFMANN

Validus Holdings Ltd.'s proposed more than $600 million acquisition of rival reinsurer Flagstone Reinsurance Holdings S.A. should bolster Validus' capital position and increase its share of the property catastrophe reinsurance market.

The deal will further expand the operations of Pembroke, Bermuda-based Validus, which has been a significant player in the mergers and acquisition market since its formation in the wake of Hurricane Katrina in 2005.

While Validus has been on both the winning and losing sides of takeover battles in the past, the Flagstone deal is less likely to draw rival bids than other recent M&A transactions, according to one analyst.

Under the terms of the agreement announced last week, Validus will acquire all issued and outstanding shares of Luxembourg-based Flagstone. Flagstone shareholders will receive 0.1935 Validus voting common shares and $2.00 in cash for each Flagstone share. The transaction provides Flagstone shareholders with a 19.4% premium and $8.43 of value per share based on the closing share price of Validus and Flagstone as of Aug. 29, when Validus closed at $33.21 and Flagstone closed at $7.05, and represents an aggregate equity value of $623.2 million, said Validus in a statement.

Mr. Noonan

The transaction should be completed during the fourth quarter of this year, subject to customary regulatory and shareholder approval, Validus said in the statement announcing the deal.

Flagstone also was formed in Bermuda in 2005 but it later merged its Bermuda and Swiss operations and then redomiciled to Luxembourg in 2008. It completed the sale of its Lloyd's operations to Amsterdam-based ANV Holdings B.V. last month. It retains operations in Bermuda, Canada, Switzerland and the United States.

"This is a compelling transaction for us that allows Validus to further build upon our market-leading position in catastrophe risk," said Validus Chairman and CEO Ed Noonan in the statement. "Flagstone brings a strong client base that will add scale to our business. Validus has an established track record of integrating acquisitions quickly and effectively with a focus on the needs of our clients and intermediaries. We are confident that this transaction will generate excellent value going forward for Validus and Flagstone shareholders."

This was not the first major acquisition by Validus. In 2007, Validus acquired Talbot Holdings Ltd., which operates in the Lloyd's market through syndicate 1183. Two years later, Validus acquired Bermuda rival IPC Holdings Ltd., overturning an agreed friendly merger between Max Capital Ltd. and IPC, and outbidding both Berkshire Hathaway Inc. and its current takeover

See **VALIDUS** page 17

HEALTH CARE BENEFITS

Mass. medical cost limits broadly welcomed

Insurers, employers support provisions to curb inflation

By MATT DUNNING

Despite lingering questions about compliance obligations and potential market fallout, health insurers and employer advocacy groups in Massachusetts largely support a new state law designed to limit escalation in medical care costs.

Scheduled to take effect on Nov. 1, Massachusetts' health care payment reform law will hold health care providers and insurers jointly responsible for maintaining annual medical cost growth rates in proportion with the rate of growth in the state's overall economy.

The law also contains provisions aimed at driving a statewide reduction in fee-for-service contracts favorable to accountable care organizations and other outcomes-based health care delivery models, as well as tax incentives for employers that promote wellness and health management.

Since its Aug. 6 ratification by Massachusetts Gov. Deval Patrick, representatives of the state's largest private health insurers have said they support the new law, though they are still weighing the practical implications of its requirements.

"The legislation includes a number of important provisions that will complement and even accelerate affordability-related initiatives already under way in the market," Andrew Dreyfus, president and CEO of Boston-based Blue Cross Blue Shield of Massachusetts, said in a statement. "These include significant changes to the health care payment system that reward quality and efficiency, greater transparency for consumers, reforms to the existing medical malpractice system and, for the first time in the nation, a specific medical spending target to ensure that health care spending grows no faster than the rest of our economy."

Under the law, the annual growth rate of medical expenditures in the state will be capped according to the state's projected gross state product in a given year. Although the cap will be a measure of aggregate medical costs, state regulators will use the prescribed growth rate as a basis for expenditures reported annually by individual providers, provider organizations and health insurers.

If an entity's year-over-year medical cost growth exceeds the prescribed rate limit or is otherwise deemed "excessive," that company will be required to submit and implement a performance improvement plan to be approved, published and monitored by the state.

Failure to submit an improvement plan, or failure to implement the plan "in good faith," could result in fines of up to $500,000. Observers also noted the considerable reputational harm to the individual entities that might result from publishing the improvement plans on the state's website.

"Certainly, there are things that we need to do that are a little bit different than we've done them, but I don't think anything on that to-do list jumps out as being particularly troublesome or

See REFORM page 20

OBITUARY

Risk management veteran had lasting influence

By RODD ZOLKOS

Judy Lindenmayer, whose accomplishments in the risk management and insurance industry included being chosen *Business Insurance*'s 1997 Risk Manager of the Year®, died last month at age 71.

Ms. Lindenmayer, who died Aug. 4, lived in Waleska, Ga., and had retired several years ago after being a senior vice president at Hilb Rogal & Hobbs Co. in Atlanta. She'd earned her Risk Manager of the Year® honor while serving as vice president of Fidelity insurance and risk management at Boston-based FMR Corp., better known as Fidelity Investments.

She joined FMR in 1988 and was credited with turning a fledgling risk management department into a state-of-the-art operation. As FMR's risk manager, Ms. Lindenmayer was actively involved in captive insurance and arranging cutting-edge insurance programs for her company such as a program designed to address operational exposures, securing coverage for losses caused by rogue traders and multiyear integrated—or concentric—risk insurance programs.

Ms. Lindenmayer joined Hobbs Group L.L.C., then operating as a unit of Hilb, Rogal & Hamilton Co., in 2002, after retiring that year from FMR.

Ms. Lindenmayer began her risk management career in 1969 while serving as personnel manager of Sealy Inc. in Chicago, when she was asked to take on the additional responsibility of purchasing corporate property/casualty insurance. Accepting the new responsibilities but uncertain because of her lack of experience, Ms. Lindenmayer pressed her employer to send her to school. She enrolled in the associate in risk management program, and was the only woman in her class. She earned the associate in risk management designation.

In 1978, she moved on to become risk manager of Chicago-based Zenith Radio Corp., where among other things she established a corporate safety program and safety oversight committee to focus the safety efforts of individual profit centers.

Ms. Lindenmayer subsequently headed the risk management operations at Atlanta-based Rollins Inc. and Boston-based Data General Corp. before joining Fidelity.

In 2000, Ms. Lindenmayer was selected by *Business Insurance* as one of the 100 Leading Women in Insurance, recognized for her professional achievements, her influence on the marketplace and her contributions to the advancement of women in risk management and the insurance industry. She was active in the Risk & Insurance Management Society Inc. and was the first woman president of the Chicago RIMS chapter.

Judy Lindenmayer was chosen *Business Insurance*'s 1997 Risk Manager of the Year®.

As a risk manager, she was known for her creativity and tenacity with brokers, as well as for her commitment to help promote the career development of those on her staff.

Several of Ms. Lindenmayer's friends and former industry colleagues are establishing a memorial fund in her honor to benefit the Spencer Educational Foundation Inc.'s Risk Manager in Residence program. Ms. Lindenmayer was one of the first risk managers to participate in the program, lecturing at Georgia State University in 1997. Donors can make checks payable to the Spencer Educational Foundation and note "In Memory of Judy Lindenmayer."

Errors & Omissions

In the Aug. 20 issue, the chart, "Program Highlights, How the Patient Protection and Affordable Care Act's Transitional Reinsurance Program Will Work," was misplaced. The chart should have accompanied the article on page 21 regarding health care reform.

WORKERS COMPENSATION

Disease management requires new approach

DMEC gathering focuses on boosting worker engagement

By ROBERTO CENICEROS

DENVER — Employers failing to gain desired results from disease management and wellness programs might consider a broader-than-usual array of issues such as managers' treatment of workers.

Succeeding at absence management and boosting worker productivity also may require evaluating how problems societywide affect the workforce, a panel of experts told the Disability Management Employer Coalition's 17th annual International Conference, held Aug. 12-15 in Denver.

The panel's presentation came amid acknowledgment by conference attendees and speakers that wellness programs and employee assistance programs suffer from low employee engagement rates and can fail to tackle behavioral health and mental health issues such as employee depression.

"We are pouring lots of money into disease management ... and we are not seeing the returns," said Tracy Messineo, vice president of total health and productivity management for Sutter Health in Sacramento, Calif. "We are seeing low (employee) engagement rates."

Ms. Messineo said, however, that she is optimistic because Sutter, a hospital and medical group, is now analyzing employee health claims data to learn whether its workers' needs for targeted wellness programs might vary by geographical region

"In one region maybe it's obesity, in another (it may be) based on depression," she said.

Addressing such problems is key to keeping employees at work and focused on the job, the speakers said.

"If you want to solve wellness, solve mental health," said Carol A. Harnett, a health, disability and employee benefits consultant based in Simsbury, Conn. "You will get a whole lot more bang for your buck."

> 'If you want to solve wellness, solve mental health ... You will get a whole lot more bang for your buck.'
>
> Carol A. Harnett, Employee benefits consultant

Keeping employees healthy may also require "social mapping," or looking at issues that impact their lives such as a lack of grocery stores selling healthy foods in the neighborhoods where they tend to live, said Gary L. Earl, vice president of health transformation, national accounts at UnitedHealthcare in Fripp Island, S.C.

Mr. Earl told of one obese worker forced to purchase

See DMEC page 20

ACCESSIBLE RELIABLE ACCURATE HONEST AFFORDABLE

ACCURATE

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Relying again on pensions to fund stable retirements

Stock market volatility leads mid-market firms back to cash balance plans

By JOANNE WOJCIK

At a time when stock-market volatility is causing retirement anxiety among aging baby boomers, cash-balance pension plans are becoming increasingly popular among middle-market and smaller employers, industry experts say.

Because cash balance plans are a type of defined benefit plan, they provide a guaranteed benefit regardless of how the underlying investments perform, unlike 401(k) plans whose value can fluctuate based on how the funds are invested. Cash balance plans also are insured by the Pension Benefit Guaranty Corp, while 401(k) plans are not.

Cash balance plans are especially attractive to professional service firms with large numbers of high-paid executives, experts say, because the amount that can be invested in them is significantly higher than the Internal Revenue Service allows for defined contribution plans.

While employees can contribute up to $17,000 annually to a defined contribution plan—or $22,500 if they are over 50—and an employer can match those contributions up to a total of $50,000, employers can fund an annual benefit of up to $200,000 per employee in cash balance or other defined benefit pension plans.

Since the stock market crash of 2008 and continuing volatility of 401(k) investments, middle-market business owners are increasingly turning to cash balance plans as a "safe money" option, according to Dan Kravitz, president of Los Angeles-based retirement plan administrator Kravitz Inc. Of the more than 1,000 retirement plans that Kravitz administers, approximately 400 are cash balance plans.

"We're seeing a lot of growth in the small and middle market," Mr. Kravitz said.

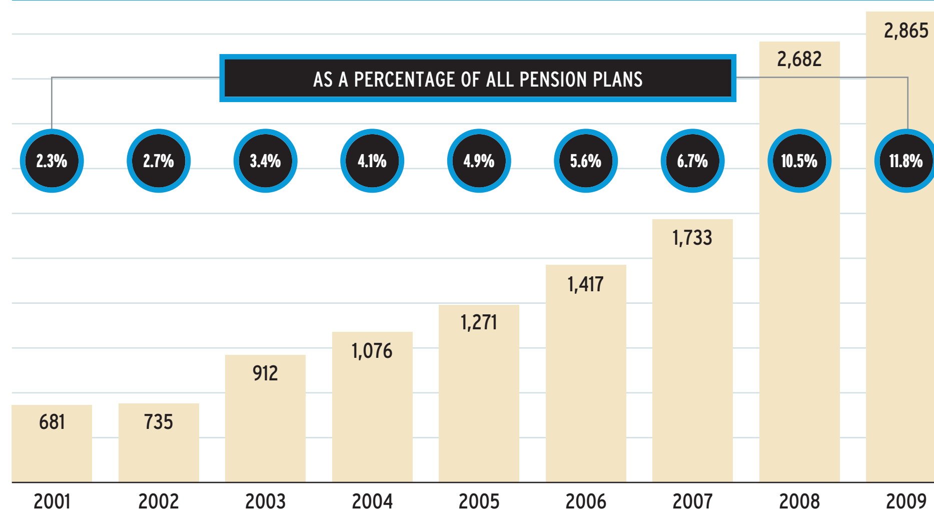
Figures published by the PBGC for "hybrid plans," which include cash balance plans, support this assertion. While just 681 of these plans were offered by employers with fewer than 1,000 participants in 2001, the number grew to 2,865 in 2009, according to PBGC data (see chart).

Overall, the number of cash balance plans grew 21% nationwide between 2009 and 2010, almost double the previous year's growth rate of 11%, according to Kravitz's 2012 National Cash Balance Research Report.

At the same time, the number of new 401(k) plans shrank slightly during the same period, down 1%, Kravitz reported.

HYBRID GROWTH CONTINUES

Number of hybrid plans with fewer than 1,000 participants, and the percentage of those plans among all pension plan types.*



The two most common hybrid plans are cash balance plans and pension equity plans.
Source: Pension Benefit Guaranty Corp.

Pension augments medical group's benefits

Atlanta-based Digestive Healthcare of Georgia P.C. introduced a cash balance pension plan in 2011, offering it to 16 physician partners and 35 employees, said Gaye Pennington, executive director.

Digestive Healthcare has a total of 135 employees, all of whom are eligible to participate in a defined contribution profit-sharing plan that has been in place since 1996, when the medical group was formed, Ms. Pennington said.

"The doctors wanted to be able to put away more for themselves, of course, and the nice thing about the cash balance plan is that it can be used for non-highly compensated employees as well," she said. "We have a lot of longevity among our employees, and the doctors wanted to be able to reward those who have been here the longest with another benefit. Tax savings also was a huge motivator."

When Tri-City Cardiology Consultants P.C. in Mesa, Ariz., added a cash balance plan in 2009, 17 partners and 33 of its 175 employees were selected to participate, CEO Ken Frandsen said.

"It provided an opportunity for our physician partners to save for retirement on a tax-deferred basis," he said. In addition, "because it is a qualified plan, it provides a greater level of asset protection from any potential lawsuits against the medical group," Mr. Frandsen said.

Like Digestive Healthcare, Tri-City Cardiology wanted to offer its longtime employees a supplement to its defined contribution plan.

"With the volatility of the stock market, a lot of our 401(k) balances haven't done as well," Mr. Frandsen said. "This provides for diversification of retirement investments. It's a guaranteed pension. There are not a lot of guarantees anymore."

—By Joanne Wojcik

Cash balance plans are especially popular among "law firms, multispecialty medical practices and accounting firms looking to increase the amount they can put into a retirement plan for themselves, their partners and employees," Mr. Kravitz said.

With cash balance plans, "they can save more than the IRS allows for 401(k) plans," he said.

For example, it is possible to put away up to $250,000 when a 401(k) and cash balance plan are offered together, Mr. Kravitz said.

In fact, the vast majority of employers introducing new cash balance plans already offer some type of defined contribution plan to employees, according to Sheldon Gamzon, a principal at Pricewaterhouse Coopers L.L.P. in New York.

"Nearly everyone has a 401(k) plan already," Mr. Gamzon said. "Cash balance plans are often being added as supplemental."

The business tax savings is also a significant motivating factor behind businesses introducing a cash balance plan, experts said.

"Most business owners like saving for retirement, but what trumps that is the tax savings," Mr. Kravitz said.

"Cash balance plans are a very effective vehicle to reduce tax liability for the business owners and shareholders, as in law firms," Mr. Gamzon said.

"When you have the right set of demographics, you want to add a defined benefit component if you want to maximize the tax benefits of retirement savings," said David Wray, president of the Chicago-based Plan Sponsor Council of America. "Having both plans, if they're structured to benefit everyone, is a great idea."

Nondiscrimination testing often is easier for employers to pass with cash balance plans than with defined contribution plans, which are barred from discriminating in favor of highly compensated individuals.

"The test is on the value of the benefit for the low-paid vs. the high-paid people," Mr. Gamzon said, whereas nondiscrimination tests for 401(k) plans focus on employee contribution rates.

For example, if an employer contributes an amount equal to 15% of a 50-year-old's pay to a cash balance plan vs. an amount equal to 5% of pay for a 25-year-old, it would appear that the 50-year-old is getting more based on his or her likely higher salary, Mr. Gamzon said.

But the IRS reasons that the 25-year-old will earn interest on that 5% contribution for 40 years, whereas the 50-year-old will earn interest only for 15 years, he said.

The Pension Protection Act of 2006, followed by cash balance regulations published by the IRS in 2010, also gave cash balance plans a boost, retirement plan experts said. The regulations provided greater clarity and expanded options for interest crediting rates, making these plans more appealing to employers, they said.

"The regulatory environment has made it harder for employers to comply with traditional defined benefit funding rules," said Dan Schwallie, a senior associate at Aon Hewitt in Cleveland and author of "Cash Balance Plan Answer Book."

"That also speaks to why cash balance plans are more attractive now. On the surface, they track more like savings plans. They're easier for people to understand," he said.

By contrast, "traditional defined benefit plans have been underappreciated by employees because they don't really understand them, plus retirement is a long way off for many. But what's happened in the 401(k) market has renewed interest in annuity-type products. This also is driving interest in cash balance plans," Mr. Schwallie said.

WellPoint: Angela Braly exits as CEO

CONTINUED FROM PAGE 1

company.

Analysts said overly aggressive pricing on WellPoint's commercial group lines, poor benefit plan designs in certain segments of its Medicare Advantage business and lingering integration issues from its 2004 merger with Anthem Inc. were among issues troubling investors the past two years.

"There had been pressure from investors for this to happen for some time," said David Windley, a Nashville, Tenn.-based managing director at Jefferies & Co. Inc.

"Under Ms. Braly's watch, there had been some underwriting mistakes and missteps in the operations," he said. "There was a belief that the company was underearning and needed fresh leadership."

Profits decline

Analysts said the final catalyst for the leadership change likely was WellPoint's most recent earnings report, which noted a 7.7% drop in first-half 2012 profits, to $1.5 billion. First-half revenue increased just 2.7% over prior-year results, as WellPoint's enrollments dropped 1.9% to 33.5 million from a year earlier, including 169,000 commercial segment members.

"We've actually been pretty vocal about leadership at WellPoint," said Alex Morozov, global health care equity research director at Chicago-based Morningstar Inc. "We've called them out for a number of execution mishaps, so we feel like this announcement supports our positive take on the company but negative take on the management team."

In a July conference call, Ms. Braly and other WellPoint executives attributed disappointing first-half results to unexpected membership losses and spikes in medical cost trends and utilization rates, notably in outpatient care, physician visits and specialty pharmaceuticals.

However, analysts were skeptical of the company's explanation, noting that costs and utilization rates didn't appear to affect most of WellPoint's competitors to the same extent.

"They sort of went overboard in saying that they were just the first ones to get hit with these trends and that they were trying to be as transparent as possible with the market," Mr. Windley said. "When you look at the things that they discussed, and then look at the things that some of the other insurers were saying, you see that they're really not first."

The day after announcing Ms. Braly's departure, WellPoint's stock price rose more than 8% over the previous day's close.

"We remain bullish on the stock, and we continue to recommend shares," Mr. Morozov said. "WellPoint has definitely had some issues in the past, but it's also one of the strongest operators in the space. It's an exciting business, but it's been severely mismanaged."

Analysts said questions surrounding WellPoint's strategy going forward likely would remain unanswered until a successor is named.

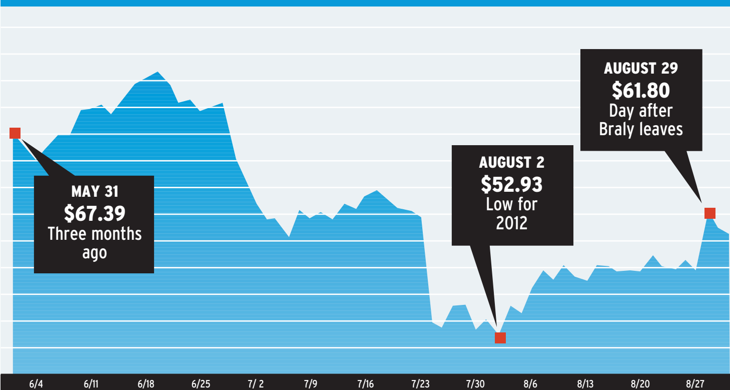
"A lot of investors wanted this leadership change, so they see this news as a step in the right direction, but it's only one step," Mr. Windley said. "In my mind, the next leadership announcement is really important."

In a note to investors, Steve Zaharuk, senior vice president at New York-based Moody's Investors Services Inc., called the leadership disruption "somewhat troublesome" at a time when WellPoint is attempting to close its acquisition of Amerigroup Corp., preparing for the full implementation of the health care reform law and addressing the rising medical cost trends it cited in its second-quarter earnings report.

"While the recent and very public reports of calls for Ms. Braly's resignation were a distraction for the company, the current leadership uncertainty is unsettling during this crucial period for WellPoint," Mr. Zaharuk said. "At best, it will likely be several months before a permanent CEO is named and begins to address WellPoint's strategic direction and operational issues."

WELLPOINT STOCK DROPS

WellPoint Inc.'s stock prices over the course of the year partly led to shareholder calls for a change in leadership at the health insurer.



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Opinions

EDITORIAL

NLRB undercuts employer probes

Employers' efforts to conduct fair and honest investigations of worker complaints may be undermined by the National Labor Relations Board.

That is because the NLRB in a recent ruling said employers cannot issue blanket rules ordering workers to keep misconduct investigations confidential. They can do so only if they provide a valid business reason.

Many, if not all, employers warn workers whom they question in response to a workplace complaint to keep the investigation confidential. The reasons are easy to understand: A witness who talks freely about an investigation may unintentionally, or even deliberately, color other workers' recollections as to what happened.

There is also a real risk workers could collaborate on a false story, and even the danger in some cases that harassers or other bad guys could get wind of an investigation and cause problems for the complainants.

Furthermore, when workers become aware investigations are not confidential, they may hesitate to even make their complaints. That could create a cascade of problems for employers and employees.

The NLRB does permit employers to remind workers to keep investigations confidential if they have a valid business reason for doing so. At its best, that gives employers that are seeking to embark on an efficient investigation one more step they must take.

And reasons for keeping an investigation confidential may not become apparent until after it is well under way, when it may be too late to tell witnesses who have already been interviewed to keep things quiet.

All of this creates a conundrum. Even the legal experts cannot agree precisely how employers should react. Do they embark on the onerous process of evaluating complaints case-by-case? Do they require confidentiality by category of complaint, such as in sexual harassment cases? Or do they generally ignore the NLRB ruling and risk repercussions?

Experts say, at some point, the ruling may be overturned. For now, all employers can do is to decide for themselves how they should approach the issue, and hope that common sense ultimately prevails.

SCHILLERSTROM

COMMENTARY

Age bias a growing problem

I often like to paraphrase Kathy Bates' iconic line in the film "Fried Green Tomatoes," when she tells two young women after ramming their car in retaliation for beating her out of a parking space, "I'm older and have more insurance," by saying, "I'm older and know more about insurance."

After more than 25 years of reporting for *Business Insurance*, I think I may have picked up a thing or two about the industry. And throughout my career, I have met some extremely knowledgeable people, some of whom have been kind enough to take the time to break it down into simpler terms so that I, a reporter, might better understand this extremely complicated discipline.

JOANNE **WOJCIK**
SENIOR EDITOR

That's why it worries me to see so many of these astute insurance industry veterans given their pink slips years before their scheduled retirement dates. It seems too great of a risk for an industry that remains under siege by lawmakers, government regulators and consumer groups to trade its institutional brain trust for younger, cheaper labor.

While a few of those who were "let go" in recent years have continued to share their industry acumen by serving as consultants to their former firms or to other organizations, far more of them have resorted to finessing their resumes to hide work experience prior to a certain date so they will appear younger.

Even as the population ages and people continue to work later in life, age discrimination is rampant in our society. According to the U.S. Equal Employment Opportunity Commission, 23,465 violations of the Age Discrimination in Employment Act were filed in 2011, up from 23,264 in 2010 and 22,778 in 2009. The age discrimination allegations reached a record 24,582 cases in 2008 during the height of the recession.

Rather than putting older workers out to pasture, as it appears so many employers are doing, they should think of age as yet another element of diversity, just as they do race, gender and sexual orientation. They should welcome the contributions made by older workers. A wise man once said, "Those who cannot remember the past are condemned to repeat it."

Experience is the best teacher, especially in business.

Ageism also can make employees of every age feel less interested and complacent in their jobs, according to new research by Sloan Center on Aging and Work at Boston College. The researchers found when younger workers perceive their older colleagues are less likely to be promoted or given tough assignments because of their age, they themselves become less engaged in their own work.

Contact: *jwojcik@businessinsurance.com*

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PAYING COMPLEMENTS

Insurance-linked securities, traditional reinsurance combine to increase available capacity

By BILL KENEALY

The use of the insurance-linked securities by primary insurers has surged in 2012.

According to a report released in July by Swiss Re Ltd., the first half of the year was the most active first half for the issuance of these securities since 2007, with about $3.6 billion of catastrophe bonds, issued in 16 transactions and 28 tranches, entering the market.

"The penetration of capital markets-based capacity, whether it be in catastrophe bond form or collateralized reinsurance form, has grown dramatically," said Cory Anger, New York-based managing director at GC Securities, a unit of Guy Carpenter & Co. "We see a much larger swath of insurers and reinsurers using the products."

While the insurance-linked securities market remains relatively small compared with traditional reinsurance capacity, it serves a valuable function for insurers, said Judith Klugman, New York-based managing director and head of distributing these securities at Swiss Re Capital Markets Corp.

See SECURITIES next page

Insurer Capital Management

SPOTLIGHT

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P/C INSURERS EMBRACE ERM AS A NECESSITY
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NEXT SPOTLIGHT Sept. 17: Global Programs Reinsurance: Rendez-Vous Report

Securities: ILS vehicles complement reinsurance

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"You've always had a core of issuers that felt it made sense to complement their overall risk-transfer program by adding catastrophe bonds into the mix, but as the cost of getting that protection through the capital markets has continued to decrease the last six months, we have seen more and more issuers flock to the market," Ms. Klugman said. "It's not meant to cannibalize reinsurance, but it is made to work on a complementary basis."

For Tallahassee, Fla.-based Citizens Property Insurance Corp., diversifying its reinsurance programs was a top operational priority, said Sharon Binnun, chief financial officer of the state-run property insurer of last resort.

"In 2011, Citizens' board decided we needed to transfer risk, and risk transfer to the private sector was the way to do it," she said. "We also wanted to diversify our reinsurance program, so we budgeted for both traditional reinsurance and catastrophe bonds in 2012."

Accordingly, Citizens on May 1 announced the signing of a two-year, $750 million cat bond deal issued through its Bermuda-incorporated special purpose insurer, Everglades Re Ltd. The deal, the largest single-tranche cat bond ever, provides several benefits for Citizens, Ms. Binnun said. "One benefit to a cat bond compared to traditional reinsurance is that it is going to be a multiyear transaction, so you are locking in rates," she said. "Another is that it is fully collateralized so that you don't have credit risk."

Moreover, the competitive nature of the offering helped save Citizens money, Ms. Binnun said, reckoning the competition among investors to invest in the bond saved the insurer $15 million. Moreover, the knowledge that the state-run insurer now had more options when it came to risk transfer, gave it more leverage when negotiating for reinsurance, saving it an additional $20 million. "We saved some money by bringing competition," she said.

Ms. Anger said the size of deal augured well for the insurance-linked securities market. "Transactions above $500 million are still rare," she said. "However, given how heavy the usage of catastrophe bonds was in the first half of the year, the fact that Citizens was able to secure $750 million in cat bond form shows the depth of capacity in this market."

Ms. Klugman said that increased demand from investors for these securities is one of the primary dynamics propelling the market forward. In turn, increased investor demand means a better deal for issuers.

"Because we are seeing greater demand from investors, we are seeing tighter spreads," she said. "So, for issuers this is now becoming a much more attractive economic alternative and a great complement to what they do on the reinsurance side."

In addition to better prices, another trend making catastrophe bonds more appealing to sponsors is the manner in which the triggers used to activate the bond are constructed. While bonds triggered by parametric measures and modeled loss are still prominent, bonds that use indemnity triggers are increasingly common, Ms. Anger said.

Indemnity triggers, which are based on the losses suffered by the bond issuer, 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, which are based on an industry-wide index of losses.

"Many sponsors prefer indemnity-based coverages, and seeing the receptivity will be helpful in getting them to access this form of capacity," she said.

Ms. Klugman agreed that wider use of indemnity triggers is a turning point for the market.

"One of the trends that made things more attractive for issuers is the fact that we are seeing an uptick in the number of bonds using an indemnity trigger," she said. "Institutional investors are now more eager to take an indemnity trigger."

Ongoing advances in catastrophe modeling also have helped assuage investor concerns, Ms. Klugman said.

"Investors wouldn't be buying the bonds if they were not comfortable with the risk assessment being provided by the modeling firms," she said.

Peter Nakada, New York-based managing director of risk markets at Newark, Calif.-based Risk Management Solutions Inc., one of the primary cat modeling firms used to model catastrophe bonds, said the market has finally reached critical mass nearly two decades after the first catastrophe bond was issued. Previously, a lack of catastrophe bonds failed to attract investors, while at the same time a lack of investors made the bond prices uncompetitive with traditional reinsurance, he said.

"In the old days, every cat bond was a snowflake," he said. "That's not the way a market develops. Repeat issuers and standardized structures and documentation are what make a robust market."

While the spike in catastrophe bond usage in 2012 is in some ways a reaction to the multiple catastrophes that occurred in 2011, it is also a validation of the inherent value of insurance-linked securities for insurance companies and investors, Ms. Klugman said.

"Sponsors truly value the collateralized and multiyear nature of the product, while for investors ILS products really make sense to add as an uncorrelated asset to their portfolio," she said.

TYPES OF REINSURANCE ALTERNATIVES

- **CATASTROPHE BONDS:** Corporate bonds issued by a special-purpose vehicle that help an issuer transfer weather-related risk to the capital markets.
- **INDUSTRY LOSS WARRANTIES:** Issuers buy protection based on the total catastrophe-related losses for the entire insurance industry rather than their own losses.
- **SIDECARS:** Special limited-purpose reinsurance vehicles designed to absorb a portion of a ceding insurer's or reinsurer's risk in exchange for a percentage of the premium.
- **LONGEVITY SWAPS:** Sponsors, usually pension funds, agree to transfer cash to a counterparty to hedge against longevity risk.

More investors attracted to ILS market

One of the factors shaping the market for insurance-linked securities in 2012 has been an upswing in investor demand for the product.

While a mixture of hedge funds, money managers and banks have traditionally made up a large part of the investor base, recently dedicated investment funds such as Westport, Conn.-based Fermat Capital Management L.L.C. are playing a larger role in the market for insurance-linked securities. Solely dedicated to investing in these products, these funds raise money from a variety of sources including sovereign wealth funds, endowments, pension funds and wealthy investors.

Cory Anger, New York-based managing director at GC Securities, a unit of Guy Carpenter & Co., said the influx of stable money, such as pensions funds, into the insurance-linked securities market is noteworthy.

"The mix of capital market investors continues to change," she said. "It ebbs and flows with the market environment."

Judith Klugman New York-based managing director and head of insurance-linked securities distribution at Swiss Re Capital Markets Corp., said the surge in demand for the products makes sense in light of the dearth of investment opportunities elsewhere. "The financial crisis has really driven home the point that having an asset that's diversifying is not a bad thing to add to the mix," she said.

Ms. Anger said that the fact that products such as catastrophe bonds are not correlated to wider political events is a draw for investors.

"Investors are always looking for investment diversification, and catastrophe bonds bring that," she said. "Whether the wind is blowing or the ground is shaking has nothing to do with the financial markets."

When Tallahassee, Fla.-based Citizens Property Insurance Corp. issued its first-ever catastrophe bond in May, the investor base varied widely by investor type and geography, said Sharon Binnun, chief financial officer of the state-run property insurer of last resort.

"We looked at the investors in the cat bond, and of the 32, 30 of them do not participate in the traditional cat bond space," she said. "We added 30 new players from all over the world."

—By Bill Kenealy

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Insurers weigh their options as investment yields swoon

Some look beyond bonds in search of better returns

By RUSS BANHAM

Property/casualty insurance companies are confronted with a conundrum: continuing to confine investments to high-quality, extremely liquid instruments such as bonds, while earning enough income to stave off the effects of inflation.

Solving this daunting problem has been confounding. But the industry is not sitting still. Many insurers are tinkering with their investment portfolios, slightly altering bond classes and durations, dabbling a bit in equities, and making tentative forays into more esoteric gambles such as real estate and private equity.

Who can blame them?

"Never before has any insurer management team faced the interest rate environment of the moment," said Robert Hartwig, president of the New York-based Insurance Information Institute Inc. "The problems are not just U.S. but global in nature, affecting insurers and reinsurers the world over."

With interest rates running in the very low single digits, safer bets like bonds—the industry's traditional investment vehicle—are akin to stuffing cash under the mattress. According to the III, about 70% of insurers' invested assets are held in bonds, which are interest-rate sensitive, of course. To inch up returns, insurers are readjusting their bond portfolios, carefully and slightly shifting from municipal bonds to higher-yield corporate bonds, among other offerings.

"There is only so much insurers can do because of regulatory restraints to keep investments liquid and of high quality," Mr. Hartwig said. "But, there is definitely some action out there, with many insurers chasing (better) yields, where they can find them."

Right now, they're less apt to find these yields in municipal bonds. While munis accounted for 52% of U.S. property/casualty insurers' aggregate bond portfolio at year-end 2007, they accounted for 44% at year-end 2011, according to the III. Higher-yield corporate bonds picked up the slack, increasing from 30% to 37% over the duration.

The migration to corporates is driven by factors besides improved yields. "There are a lot of conservative views (of municipal bonds) now that two or three municipalities have gone under and several more are threatened," said Herbert E. Goodfriend, senior vice president at New York-based insurance broker and financial advisory firm Gill & Roeser Inc.

Additionally, the superior tax treatment of municipal bonds vs. corporate bonds (municipal bonds are exempt from federal taxation of interest income) loses its luster when the yields are so low, Mr. Hartwig said. As he put it, "There's just not much of a tax benefit left."

Despite the migration from munis to corporates, the industry still confronts meager portfolio returns. As Karen Wells, co-head of the insurance investment advisory group at Towers Watson Investment Services in New York, said, "Regulations are written requiring insurers to hold a preponderance of fixed income bonds, which are really one of the riskiest classes out there, given that yields are effectively lower than the rate of inflation," she said.

"We're asking clients to take off the traditional insurance investment blinders and explore the wider universe," Ms. Wells said.

This wider universe comprises other asset classes such as equities and real estate, and different approaches to fixed income maturity. "Durations are shortening across the board, and are now at about 6.5 years," said Stephan Christiansen, managing director of insurance research at Hartford, Conn.-based research firm Conning & Co.

'The problems are not just U.S. but global in nature, affecting insurers and reinsurers the world over.'

Robert Hartwig,
Insurance Information Institute Inc.

Mr. Hartwig provided III statistics on maturities indicating that at year-end 2007, 8% of insurers' bond portfolios had a maturity of 20 years or longer. At year-end 2011, this percentage fell to 6%. Thirteen percent of insurers' bond portfolios at year-end 2007 contained bonds maturing in a 10- to 20-year timeframe, whereas only 10% at year-end 2011 held bonds of this duration. Similarly, five- to 10-year duration bonds also fell to 27% of holdings from 34% over the period. Meanwhile, bonds with a one- to five-year duration saw increases to 41% of portfolio holdings from 30%.

The upshot?

"Obviously, fewer companies are locking into longer-term bonds due to the low yields and the effects of inflation," Mr. Hartwig said. "When you invest at 1.5% for 10 or more years, you are locking into something that will likely be below the rate of inflation, guaranteeing a loss."

Another shift in investing philosophy appears to be toward more sector-diverse corporate bonds. "We're seeing a move away from purely A-rated or better corporate (bond) exposures to more diverse issuer exposure in the BBB marketplace," Ms. Wells said. "We believe insurers with stronger exposure to BBB corporates will have better diversification than those that stick with an A or better mentality. As long as they do proper credit research, there remains a very low probability that these (bonds) will default—they're still investment-graded fixed income assets."

Mr. Christiansen agreed that there is more interest in BBB and BB bonds, and in equities to boot. "Some companies are looking to increase yield by allocating more of their investments into lower-quality bonds," he said. "Others are shifting a bit into equities, particularly those sectors that produce decent dividends and are priced relatively low. It's not impossible to see a 3% yield on equities with dividends, which is double the return on a one-year Treasury (bond) these days."

James Amen, partner and insurance company specialist at Philo Smith & Co., a Stamford, Conn.-based independent investment banking firm, estimates that 1% of insurer portfolios are invested in preferred stocks and 15% in common stocks, much of it dividend-bearing. "If a company is underleveraged and able to generate close to an underwriting profit, they are more likely to be more heavily exposed in equities as well as alternative investments such as private equity, real estate and sector-specific funds," he said. "Still, these are slight movements—nothing dramatic."

Mr. Hartwig added another relatively nontraditional investment to the list—privately placed bonds, which represented around 3.5% of insurer bond investments at year-end 2007 and 8% at the conclusion of last year, he said.

Ms. Wells echoed these and other diversifications, including bank loans (a loan made to a corporation, with the investor taking on the issuer risk); master limited partnerships, typically energy-related; and real estate. The latter comprises traditional real estate investment trusts spinning off cash flow and moves by some insurers to buy company buildings, as opposed to leasing these facilities. "There are lots of options out there," she said.

While there may be options to lift investment income, the outlook nonetheless remains grim.

"The impact of poor investment earnings has clear ramifications," said Howard Mills, chief adviser to the insurance industry group at New York-based Deloitte. "The focus must be on underwriting and expenses. Insurers are making greater use of data to increase underwriting gains, while cutting costs wherever they can. The days of relying on investment income to smooth over underwriting losses are over, at least for the foreseeable future."

Mr. Hartwig said: "Insurers can tweak their portfolios, but where the rubber meets the road is pricing."

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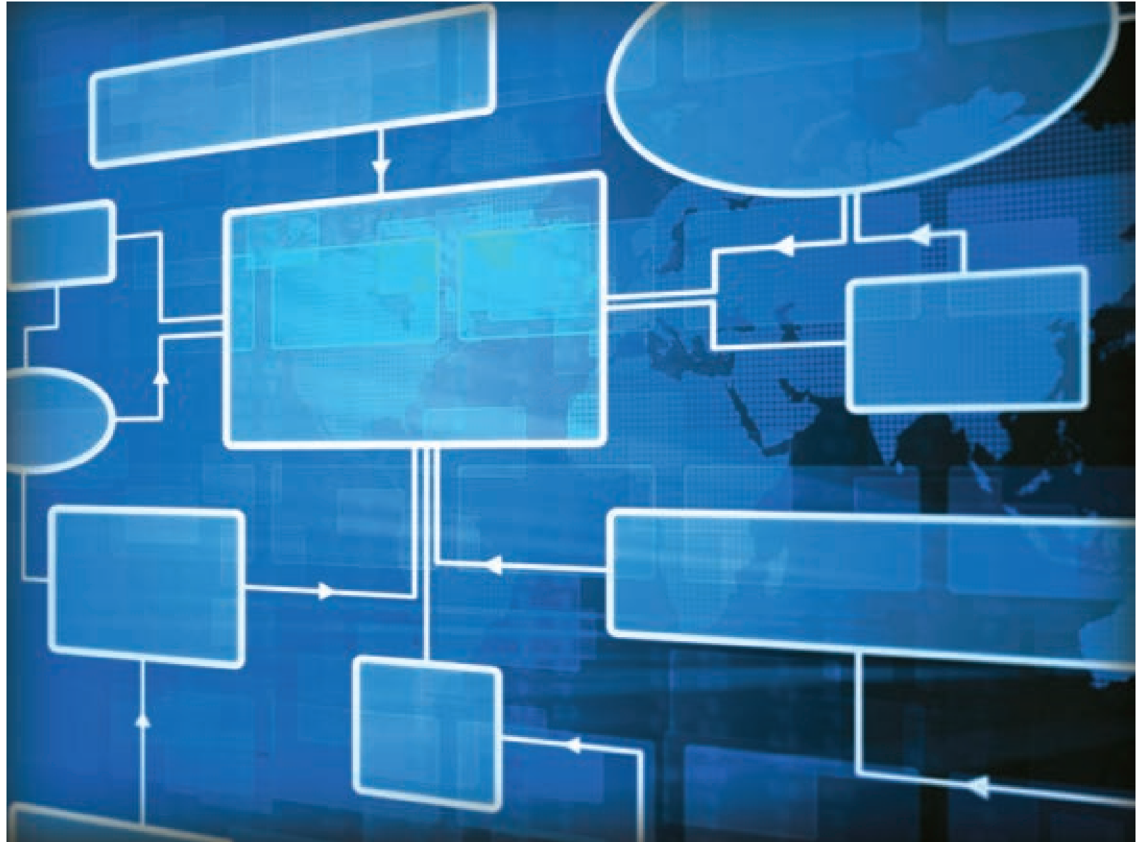
Insurers use ERM to evaluate risks



Regulators force industry to take systematic approach

By MARK A. HOFMANN

Enterprise risk management is becoming ever more deeply embedded in property/casualty insurers' corporate DNA, according to observers.

In part, insurers have little choice than to embrace ERM because of pressure from regulators and rating agencies, they say.

But with ERM insurers also can take a broader view of risk than they might otherwisedo, making it a strategic tool to gather risk information across the enterprise.

"They pretty much have to have ERM," said Howard Mills, chief adviser at Deloitte L.L.P.'s insurance industry group in New York and a former New York superintendent of insurance. "It's pretty much expected that every regulator will expect every company to have an ERM program."

"Both with regard to regulators and rating agencies—they're looking at who owns ERM," said Mr. Mills. "The expectation is that it's done at the board level. Increasingly, you're seeing a restructuring at the board level to deal with risk, with a separate board committee."

Zurich Insurance Co. Ltd. has been involved with ERM for more than a decade, said Linda Conrad, director of strategic business risk for Zurich in New York: "It's very essential to us as a company."

She said ERM began as a means to comply with capital requirement regulations. But it has proved to be "a great strategic tool to start to gather additional information about managing risk across the company," she said. "We've got a risk-based understanding when we're making strategic decisions."

"ERM is a comprehensive network that starts with the very definition of the risk appetite," said Jacob Rosengarten, executive vice president and chief enterprise risk officer for XL Group P.L.C. "It's not a black or white question," but rather a definition of success or failure among multiple tolerances of risk in different areas such as operation risks or liquidity statement, he said. "It's all about trade-offs."

Mr. Rosengarten stressed that ERM has to be embraced by the corporate culture to achieve its goals. "A very strong risk-reward mindset is critical," he said. "We want to have as few barriers as possible to free exchange of ideas."

"ERM means, at its core, companies look at it as an opportunity to enhance their risk management program," said Eric Simpson, Philadelphia-based practice leader for property/casualty consulting at Towers Watson & Co. "It's also an opportunity to take a more integrated view across companies that might have taken a more siloed approach to risk."

> **'ERM is a comprehensive network that starts with the very definition of the risk appetite.'**
>
> Jacob Rosengarten, XL Group P.L.C.

"Traditionally, (property/casualty) insurers focused on risk in silos, and heavily on underwriting risk," said Maryellen Coggins, a Boston-based director with PricewaterhouseCoopers L.L.P.

"ERM allows integration of each individual risk view into an integrated enterprisewide view. Insurers have been developing ERM practices over the past 10 years and have really made significant progress … with embedding ERM processes into existing business and strategy setting processes," she said.

Technology has been key in promoting ERM, said Mr. Simpson.

"Technology has advanced so they can better measure their accumulation of risk and supplement their risk management decision-making and better inform the decision in a host of areas," he said. "It's all about enhancing risk management and enhancing risk performance through a better framework."

Ms. Coggins said insurers face two primary challenges in the ERM process.

The first involves tools, she said. "ERM requires really sophisticated quantitative tools to support management decision-making—such as economic capital models and stress-testing tools," said Ms. Coggins. "It takes time for management to begin to use the results of these models and to really have comfort over the results of these models."

The second challenge involves the timeline for implementing the process, according to Ms. Coggins. "Insurers have been developing the practices over 10 years and doing it in a very measured manner. They're doing it very carefully, but increasing external stakeholder demand for risk information has really accelerated the timeline."

"We've taken a real active approach to invest a positive culture of risk," said Zurich's Ms. Conrad. "A risk assessment is seen as a positive thing," not only as a means to avoid potential pitfalls, she said.

Zurich follows a process called total risk profiling, said Ms. Conrad. She said the insurer performs the process about 200 times a year, going from the board level through the C-suite to the operational level.

"We do this total risk profiling process to lay out in a very organized fashion to see what the major exposures are at the company," and to see what the triggers might be that would cause that risk to come to fruition, she said.

The consequences of the risk can depend on the trigger, she said. To mitigate the risk, each scenario has an action owner assigned to it.

"We can look at improving the risk and look at controls that prevent it from happening. You want this total risk profiling process to occur before budget time," Ms. Conrad said.

Towers Watson's Mr. Simpson said insurers' attitudes toward ERM have shifted considerably during the past decade.

Ten years ago, some companies viewed ERM as a fad and "they had a rough time rationalizing its benefit," he said.

Now "everyone is well beyond that," said Mr. Simpson.

Rating agencies assess ERM processes when scrutinizing insurers

An insurer's enterprise risk management process comes into play as rating agencies determine what rating to assign the company.

Rating agency analysts consider how insurers measure risks, how they approach emerging risks, and how they model risk as part of their ERM assessment.

But an insurer's ERM process is only one of many factors that rating agencies consider when examining property/casualty insurers.

For example, at Standard & Poor's Corp., ERM is one of eight rating components, said Li Cheng, director-financial services ratings in New York. The other components are financial stability, capital, liquidity, investments, operating performance, competitive position, and management and corporate strategy.

According to a presentation Ms. Cheng made this year, the elements of S&P's ERM evaluation include risk controls, emerging risk management, risk models and strategic risk management.

"We have our methodology—we do discuss risk management," said Neil Strauss, vice president/senior credit officer of the U.S. insurance group at Moody's Investors Services Inc. in New York.

"Risk management is listed as a consideration in determining the standalone rating for company. It's not an explicit rating factor," said Mr. Strauss. "There are different factors relating to the business profile and the financial profile."

"Risk management does implicitly influence some of the factors that are explicitly analyzed," he said.

Enterprise risk management is "one of many factors, but we think it's kind of embedded in a lot of our rating analysis," said James Auden, an analyst at Fitch Ratings Inc. in Chicago. "How companies really identify the risks they face and measure them and how they set risk appetites—it kind of all works together and is embedded in our rating process. It's a not a separate pillar of our rating but integrated in many aspects."

"A lot of it is tied to corporate governance," said Mr. Auden.

"How does it impact the day-to-day underwriting and investing activity of the company? What are the real issues they're looking for? For a property/casualty insurer, catastrophe risk is a big source of volatility," he said. "What's your appetite for cat risk and how do you manage the spread of risk and aggregation, and what models are you using to measure that risk and how do you use reinsurance?"

Mr. Auden noted that property/casualty insurers weren't as affected by the financial crisis that began in 2007 as some other financial institutions. Yet the crisis and its aftermath have driven ERM among insurers, he said.

The crisis "shed the light you could have tail events that really could affect your capital," said Mr. Auden. "I think it's still an evolving thing" with the European Union's Solvency II directive and other regulatory issues helping to drive the ERM process.

—By Mark A. Hofmann

UP CLOSE
COMINGS & GOINGS

KIRK STEPHENS

NEW JOB TITLE: Kennesaw, Ga.-based senior vice president and chief compliance officer for OSC, formerly known as Overby-Seawell Co., a subsidiary of Breckenridge Insurance Group.

PREVIOUS POSITION: Washington-based special assistant and senior adviser to the senior deputy director of supervisory examinations for the Federal Deposit Insurance Corp.

LOOKING FORWARD TO: (Retracting) from the bureaucracy of the government. Also, I am looking forward to expanding into to risk management, regulatory and compliance services.

CHALLENGES FACING INDUSTRY: From my standpoint, I see the industry changing so significantly. You look at the amount of legislation that has passed. For banks to stay above water, that's a challenge, especially for the small community bank. It's really important for banks to be vigilant when it comes to the changes. It can be costly for some of them.

BEST THING ABOUT A BAD ECONOMY: In my eyes, I think the best thing is the creation of checks and balances. You have a lot of systems and industries being checked. I think you are looking for what's making (the economy) bad, what's the cause. That can be helpful in eliminating future issues in the economy. You get a feel for where the problems started and existed and how to stop them.

COLLEGE MAJOR: Finance, with an option in banking.

OUTSIDE THE INDUSTRY, A DREAM JOB: Traveling the world and critiquing resorts. I think that would be great ... That, or I'd like to be a pilot.

HOBBIES: I love to travel. I like fitness. I like to go to restaurants and movies.

CAN'T-MISS TELEVISION SHOW: "The Amazing Race." I love the worldwide scavenger hunt.

FAVORITE MEAL: I like a good steak.

ON A SATURDAY AFTERNOON: I do a lot of volunteer work with my church. Or I am at the gym or doing work around the house.

EMAIL OR PHONE, AND WHY: I think I prefer email because I can better provide guidance. I can make sure it is correct.

Comings&Goings

VISIT *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.

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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:

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- John L. Wortham & Son L.P.

INSURERS
- XL Group P.L.C.
- Aspen Insurance Holdings Ltd.

REINSURANCE
- BMS Group Ltd.
- Southport Re

OTHER
- Broadspire Services Inc.
- EisnerAmper L.L.P.

Market Moves

Physicians Insurance buys RRG management firms

Physicians Insurance A Mutual Co. has acquired two risk retention group management companies.

The two RRGs, Emergency Medicine Professional Assurance Co. Risk Retention Group and SCRUBS Mutual Assurance Co. Risk Retention Group, will allow the insurer to offer an alternative risk financing platform to physicians, clinics and hospitals, Physicians Insurance announced in a statement.

The company operates in Idaho, Oregon and Washington.

"This was a strategic decision on our part," said Mary-Lou Misrahy, president and CEO of Physicians Insurance, in a statement. "It leverages our leadership role and enables us to respond to changes in the health care environment. Some of these changes are forcing medical professionals and facilities to rethink their risk financing options, and now they have another tool in their toolbox."

EMPAC is a professional liability insurance company formed by emergency medicine physicians, while SCRUBS offers medical professional liability insurance specifically for urologists.

Financial terms of the acquisitions were not disclosed.

USI expands in Florida with purchase of agency

USI Insurance Services has acquired Suncoast Insurance Associates Inc., a Tampa, Fla.-based insurance brokerage. Terms of the transaction were not disclosed, USI said in a statement.

Suncoast Insurance Associates offers professional liability programs for more than 1,500 professional firms and has offices in Miami Beach, Tallahassee and Tampa, Fla.

"For almost four decades, Suncoast Insurance Associates has been the 'go-to' insurance agency for the design firm marketplace in Florida," said James W. Dunn, USI's regional CEO for the Southeast, in a statement. "In addition to architects and engineers, Suncoast has growing practices providing professional liability for health care, technology, accounting and law firms."

Digital Insurance buys First Benefit Partners

Digital Insurance Inc. has acquired First Benefit Partners. Terms of the deal were not disclosed.

Employee benefits-only agency Digital Insurance also announced that Matt Noe, who was principal at Knoxville, Tenn.-based First Benefit Partners, has been named director of sales for its specialized integrated benefits team.

"Matt brings tremendous experience and industry knowledge to our integrated benefits team," said Wayne Mertel, vice president of integrated solutions at Digital Insurance, in a statement. "With the growing demand in today's market for ancillary and voluntary products, his creativity and tireless energy for finding ways to deliver innovative solutions will well serve our partners and clients."

Atlanta-based Digital Insurance specializes in coverage for small and midsize companies.

Enstar to purchase comp insurer SeaBright

Bermuda-based Enstar Group Ltd. says it will acquire Seattle-based workers compensation insurer SeaBright Holdings Inc. in a $252 million deal.

Enstar acquires and manages insurance and reinsurance companies in runoff. It also provides management and consulting services to the insurance industry.

SeaBright's business unit, SeaBright Insurance Co., is a specialty underwriter of workers comp insurance as well as risks such as those that fall under the U.S. Longshore and Harbor Workers' Compensation Act and the Jones Act.

Terms of the agreement call for a new wholly owned subsidiary of Enstar to merge into SeaBright, with SeaBright surviving as a wholly owned subsidiary of Enstar, the company said.

The $252 million deal still needs stockholder and regulatory approval, among other conditions. Enstar also said that it is discussing opportunities with third-party insurance companies for the assumption of SeaBright's policy renewals.

IN MEMORIAM

Judy Lindenmayer
1941-2012

Business Insurance **salutes the contributions and leadership that Judy provided to the risk management profession and education during her career. We were fortunate to know Judy, to benefit from her support and advice, and were inspired by her accomplishments as our Risk Manager of the Year® in 1997, and one of our 100 Leading Women in Insurance in 2000.**

Mark Stach	Paul Winston	Gavin Souter
Publisher	Associate Publisher	Editor

and the entire staff of *Business Insurance*

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INSIGHTS TODAY FOR THE RISKS OF TOMORROW

Perspectives

Health care facilities face unique pollution liability challenges because of their singular mix of environmental exposures, including transportation issues, indoor air quality, waste management processes—and the fact that many of the people in those facilities have suppressed immune systems. Bill Nellen, executive vice president of the environmental group at Alliant Insurance Services Inc., outlines the potential exposures and the due diligence required to help mitigate them.

Health care facilities face tough environmental risks

By Bill Nellen

Mr. Nellen

There is a strong element of fortuity in pollution incidents which largely cannot be protected against or planned for.

While the adverse balance-sheet consequences of many business risks faced by health care facilities are relatively easy to quantify, that's not always the case for measuring the potential impact of pollution liability on these facilities.

The complex and substantially higher capital requirements of health care facilities compared with traditional industrial, commercial and office real estate holdings—combined with their unique environmental exposures—pose a major risk management challenge for health care facilities.

Pollution liabilities for health care institutions go beyond basic considerations of compliance with applicable standards and regulatory governance. Health care facilities require highly specialized heating, ventilating and cooling systems, along with process equipment, higher resultant floor loads, electrical system capacity, waste management/hazardous material storage systems, audit of disposal facilities, above and/or underground storage tanks and wastewater treatment processes.

Further impacting these facilities is the exposure pathway of third-party patient groups with suppressed immune systems. Pollution incidents can result from hard-to-define indoor air quality issues (mold, methicillin-resistant Staphylococcus aureus, Legionella, fungi and others), to more standard causes like leaking underground storage tanks and presence of dry cleaning chemicals in the subsurface due to historic laundry operations or migration from off-site sources.

The team of professionals that is tasked with risk management responsibility for health care facilities usually consists of some combination of an environmental/health and safety director, facility manager, risk manager and engineer, as well as others. This team of multidisciplinary professionals employs a variety of administrative and engineering controls.

To recognize and fully understand the overall threat posed by environmental hazards to the health care organization, extensive hazard identification and risk management planning is critical, along with preloss and post-loss analysis. Commercially available environmental management systems also can be effective tools in this process when deployed systemwide and adequately maintained.

When tasked with integrating environmental management into the strategic direction of a health care organization, considerations must include the adequacy of the various written documentations required for compliance with regulations (spill plans, emergency contingency, countermeasures and others). Organizations also must demonstrate that adequate training has been delivered to the staff responsible for implementing such controls.

The potential for significant financial losses associated with pollution liability—combined with the broad availability of competitively priced site pollution liability insurance—makes this line of coverage an increasingly essential element in risk management planning for health care facilities.

As one of the administrative controls, environmental insurance coverage serves as a safety net against the unforeseen. For instance, when pollution liability is excluded from other lines of coverage traditionally purchased by health care risk managers—general liability, property, and directors and officers—it may result in unknown environmental exposure.

Environmental implications for health care facilities also can include potential pollution from pre-existing conditions due to prior operations on the property. Often these come to light during due diligence preparations prior to acquisition and development (Phase I Environmental Site Assessments are helpful) or refinancings. With larger health care players consolidating the market segment by purchasing smaller regional players or utilizing sale lease-back arrangements, they often end up acquiring environmentally impaired properties.

Because only a finite amount of due diligence can be performed, the property buyer may end up with an inadequate picture of the pollution risks involved. Therefore, any type of protection that can be provided from a cost-effectiveness standpoint can be invaluable to the property buyer.

On the operational side, possible exposures can include pipe ruptures that expose workers, facility structures and neighbors (commercial, residential or industrial) to environmental injury or damage. Additionally, health care/medical facilities can generate solid or liquid waste materials and can ultimately be held liable for cradle-to-grave disposition of these materials.

Even with strong due diligence and compliance audit protocols, the generator of the wastes can be held financially responsible for cleaning up a landfill or transfer station simply because the company disposed of wastes in those facilities.

There is a strong element of fortuity in pollution incidents, which largely cannot be protected against or planned for. Ultimately, there may be a defense obligation to avoid a suit or allegation, not to mention potential reputational/public relations damage.

Pollution insurance covers liabilities resulting from cleanup, bodily injury and property damage, as well as related legal defense expenses, most often within the limits of liability. As an administrative improvement, insurers recently have been willing to offer the coverage on a blanket basis. In this case, the policy effectively acts like a general liability policy for pollution losses.

Some other enhancements to the off-the-shelf offering include:

- Business interruption
- First- and third-party transportation
- Scheduled underground storage tanks financial assurance
- Historical disposal site liability
- Indoor air quality (mold, Legionella, MRSA, bacterium, fungi)
- Automatic acquisition/divestiture, including agreed-to rates
- Natural resource damages
- Facility disinfection

In addition to strong internal protocols and an environmental management system and controls, pollution liability insurance is an important consideration for any health care risk adviser dealing with complex asset ownership, operation and management, as well as acquisitions and divestitures. However, insurance is not a substitute for good management, knowledge of the exposures and conscientious due diligence.

While environmental liability is a multiheaded beast involving legal, financial, strategic, technical, governmental, compliance and risk management challenges, harnessing these disciplines can lead to positive results while protecting the bottom line of health care provider systems and delivering wellness to the communities they serve.

Bill Nellen is executive vice president of the environmental group at Alliant Insurance Services Inc. In addition to his brokerage expertise in the sector, he has broad technical knowledge about environmental issues, having earned a master's degree in environmental science. Mr. Nellen's experience in the industry niche began at the environmental engineering and consulting firm Roy F. Weston Inc. and continued with later positions with Zurich North America's risk management division and Marsh & McLennan Cos. Inc. He can be reached at 770-325-6655 or bnellen@alliantinsurance.com.

Confidential: Business case needed

CONTINUED FROM PAGE 3

coerce employees, and so constituted an unlawful restraint" of workers' concerted activity rights, the panel ruled.

"It's a huge problem," Jonathan T. Hyman, a partner with Kohrman Jackson & Krantz P.L.L. in Cleveland, said of the ruling. "One of the hallmarks of any successful, thorough investigation is confidentiality," which ensures witnesses neither prepare nor compare their stories.

"There are a multitude of reasons to maintain confidentiality of an investigation," said Jay Sabin, general counsel at Woodbridge, N.J.-based transportation logistics firm Grocery Haulers Inc. "What we intend to do is articulate, or at least be able to articulate, the reason or reasons why we ask either a complainant, a person under investigation or a witness to keep the information confidential."

Russell D. Cawyer, a partner at Kelly Hart & Hallman L.L.P. in Fort Worth, Texas, said the NLRB ruling "is contrary to the advice that most practitioners give to employers about how to conduct investigations."

"When you can't prohibit witnesses from talking amongst each other, you could have issues regarding the preservation of evidence," he said. "They can either destroy or delete that evidence, or alter that evidence. I think it's a terrible precedent."

The ruling "puts employers in a very difficult position to run an investigation that will gather information that is assured to be … new and fresh, without worrying about spoilage" or creating information that defeats the investigation's integrity, said Christine Liu McLaughlin, a shareholder at Godfrey & Kahn S.C. in Milwaukee. The burden created by *Banner* is "going to be pretty hard to meet right out of the gate of an investigation."

If an employee is reluctant to report a problem because an investigation will not be kept confidential, it "makes it more difficult to identify and eliminate wrongdoing," which "could result in increased litigation," said Michael S. Arnold, an associate with Mintz Levin Cohn Ferris Glovsky & Popeo P.C. in New York.

"There's a real conflict between what the NLRB is doing and what the courts and other agencies would say an employer should do under Title VII (of the Civil Rights Act of 1964), or under a host of other employment laws," said Jonathan C. Fritts, a partner at Morgan, Lewis & Bockius L.L.P. in Washington.

John M. Skonberg, a shareholder with law firm Littler Mendelson P.C. in San Francisco, said, "The NLRB does say that if you can demonstrate a good reason for confidentiality, then that's acceptable, but … you don't know if they're going to go out and talk to other people, so it's a difficult standard to meet" and it is "a little bit unrealistic to place the burden on the employer to demonstrate that confidentiality is necessary."

The ruling "fails to recognize the problems it causes in the workplace" to conduct a fair, prompt and impartial investigation, which is in employers' and employees' best interests, said Michael J. Underwood, a partner at Porter Wright Morris & Arthur L.L.P. in Columbus, Ohio.

Renee Inomata, a partner at Burns & Levinson L.L.P. in Boston, said the ruling may be a particular surprise for employers with nonunion workforces because they tend to believe they can control most aspects of an employee's relationships. *Banner* "really puts constraints on those areas where it's a little bit gray as to what the legitimate business interest is," she said.

However, Susan Davis, a partner at Cohen, Weiss & Simon L.L.P. in New York, a law firm that represents the interests of labor and individuals, defended the ruling.

Under the Obama administration, the NLRB has been "going back to what it thinks is the purpose of the statute, which is to protect the exercise of Section 7 rights, and those include the right to talk to one another about various issues that arise in the workplace," she said. "So I think it's an appropriate decision."

An NLRB spokeswoman had no comment.

Confidentiality decision creates dilemma for firms

Experts differ on the advice they plan to offer clients on how to respond to the National Labor Relations Board's confidentiality ruling.

Suggestions they make include to continue to generally maintain confidentiality; to look at each investigation on a case-by-case basis; to determine confidentiality based on the type of investigation involved; and to instruct workers to maintain confidentiality, but for only a limited period of time.

Jonathan T. Hyman, a partner with Kohrman Jackson & Krantz P.L.L. in Cleveland, said that in advising his clients of the potential risks involved, "I would tend to err on the side of preserving confidentiality in all instances because of the potential liabilities if you don't."

However, John M. Skonberg, a shareholder with law firm Littler Mendelson P.C. in San Francisco, said: "Employers really need to approach investigations on a case-by-case basis."

Jonathan C. Fritts, a partner with law firm Morgan Lewis & Bockius L.L.P. in Washington, said, "It's legitimate for an employer to make a judgment" that confidentiality be required in certain categories that present common issues where it can be justified, such as in sexual harassment cases.

Glenn Grant, counsel with law firm Crowell & Moring L.L.P. in Washington, said it may be acceptable to the NLRB for employers to require confidentiality, but only for the duration of the investigation, not for an indefinite period. "I think the board would still find that OK," he said.

Employers must engage in a balancing act, said Lorene Schaefer, a mediator with One Mediation Inc. in Atlanta, who is a former in-house counsel with General Electric Co.

"Your policies have to be procedurally fair. They have to protect confidentiality to the extent possible while still recognizing employees have the right to talk to one another in an effort to improve working conditions," she said.

"Employers need to look at their policies and practices to make sure there is an added step to determine at the very start of an investigation whether a blanket confidentiality admonition is appropriate," said Christine Liu McLaughlin, a shareholder with law firm Godfrey & Kahn S.C. in Milwaukee. "Undertake that analysis, and gather the facts that support the confidentiality admonishment," she said.

Renee Inomata, a partner with Burns & Levinson L.L.P. in Boston, said firms should "make sure the people who are in charge with investigating understand that they do need to make an independent assessment of what the business factors are that need to be protected before instructing an employee of the requirement they keep it confidential."

Write down the reasons why an investigation should be kept confidential and then discuss them with the witnesses interviewed, said Michael J. Underwood, a partner with Porter Wright Morris & Arthur L.L.P. in Columbus, Ohio.

Observers also say the ruling eventually may be overturned, though to their knowledge no appeal on the issue is in the works.

—By Judy Greenwald

Validus: Expands with deal

CONTINUED FROM PAGE 3

target Flagstone in a bidding war.

But not all of Validus' forays into M&As proved as successful. Last year, Validus engaged in a sometimes acrimonious effort involving several suitors to acquire Transatlantic Holdings Inc., which had agreed earlier to be acquired by Allied World Assurance Co. Holdings A.G.

Transatlantic ultimately was acquired by Alleghany Corp.

"I think it's a good deal" for Validus, said Meyer Shields, director at Stifel Nicolaus & Co. in Baltimore.

"They're paying significantly below book value, and they're buying a participant in a line of business that I believe will be consistently and stably profitable: property catastrophe reinsurance," said Mr. Shields. "There are some opportunities to generate higher returns both on the underwriting and investment sides. Validus can really sift through its own portfolio and Flagstone's portfolio of risks and construct an even better, more diversified loss portfolio."

"We believe the acquisition will boost Validus' capital base and property catastrophe premium writings, allowing the combined company to offer increased capacity," said Standard & Poor's Corp. in an analysis of the transaction.

Jason Porter, an analyst at S&P, said that the acquisition would not affect Validus' credit profile.

"Validus' management is happy in that, in their view, it puts them in the position of the No. 1 catastrophe reinsurance writer in Bermuda in terms of premium volume," he said.

Mr. Shields said that while he didn't think Validus' move would attract additional would-be suitors to bid for Flagstone, "it's not a remote possibility."

He said that "Flagstone's been on the block for a while, and anyone who would be interested has had an opportunity to look at it. On the other hand, what we've seen over the past few years is that there is a willingness in the industry to bid competitively for properties when they come up."

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IN THE MATTER OF THE REHABILITATION OF FRONTIER INSURANCE COMPANY

Supreme Court of the State of New York, County of Albany Index No. 000097/2006

NOTICE

By order of the Supreme Court of the State of New York, County of New York (the "Court"), entered October 15, 2001 ("Rehabilitation Order"), Frontier Insurance Company ("Frontier") was placed into rehabilitation and the then-Superintendent of Insurance of the State of New York and his successors in office ("Superintendent") were appointed rehabilitator of Frontier ("Rehabilitator"). The Superintendent of Financial Services of the State of New York has now succeeded the Superintendent of Insurance as Rehabilitator of Frontier. The Rehabilitator hereby gives notice that he has applied to the Court by order to show cause ("Order to Show Cause") for an order: (1) converting this rehabilitation proceeding to a liquidation proceeding; (2) appointing the Superintendent and his successors in office as liquidator of Frontier ("Liquidator"); (3) vesting title to all of Frontier's property, contracts and rights of action with the Liquidator; (4) continuing and granting the injunctions provided for in the Rehabilitation Order and in Insurance Law Section 7419, including permanently enjoining and restraining all persons from: (a) the transaction of Frontier's business; (b) the waste or disposition of its property; (c) interfering with the Superintendent as Liquidator in the possession, control or management of Frontier's property or in the discharge of his duties; (d) commencing or prosecuting any actions, lawsuits, or proceedings against Frontier or the Superintendent as Liquidator; and (e) obtaining preferences, judgments, attachments or other liens or making any levy against Frontier's property or any part thereof; (5) granting injunctions, in addition to the aforementioned injunctions previously granted in the Rehabilitation Order, permanently enjoining and restraining all parties from commencing or prosecuting any actions or proceedings, or efforts to collect on debts or judgments, against Frontier, the Liquidator or the New York Liquidation Bureau, their present or former employees or attorneys, with respect to this proceeding or the discharge of their duties under Insurance Law Article 74; (6) granting injunctions enjoining and restraining all parties to actions, lawsuits and special or other proceedings in which Frontier is obligated to defend a party pursuant to an insurance policy, bond, contract or otherwise, from proceeding with applications for judgment or proceedings on settlement or judgment and the making of all liens, levies or other efforts to execute or collect on debts or judgments, for a period of 90 days from the entry of the order of liquidation; (7) granting injunctions enjoining and restraining all persons who have first-party or New York Comprehensive Automobile Insurance Reparations Act (No Fault) policyholder loss claims against Frontier, from presenting and filing claims with the Liquidator for a period of 90 days from the entry of the order of liquidation; (8) vesting all rights in Frontier's contracts and agreements, including all leases, tax agreements, insurance policies and employment contracts, however described, with the Liquidator, unless the Liquidator expressly terminates such contracts or agreements, in which case all liability under such contracts or agreements shall cease and be fixed as of the date of termination; (9) requiring that any bank, savings and loan association, other financial institution or any other entity or person, which has on deposit or in its possession, custody or control any of Frontier's funds, accounts or assets shall immediately, upon the Liquidator's request and direction: (a) turn over custody and control of such funds, accounts or assets to the Liquidator; (b) transfer title of such funds, accounts or assets to the Liquidator; (c) change the name of such accounts to the name of the Liquidator; (d) transfer funds from such bank, savings and loan association or other financial institution to a bank, savings and loan association or other financial institution designated by the Liquidator; or (e) take any other action necessary for the proper conduct of the liquidation proceeding; (10) requiring that all persons or entities having property and/or information, including, but not limited to, insurance policies, claims files (electronic or paper), software programs and/or bank records owned by, belonging to or relating to Frontier shall preserve such property and/or information and immediately, upon the Liquidator's request and direction, assign, transfer, turn over and deliver such property and/or information to the Liquidator; (11) authorizing, permitting and allowing the Liquidator to sell, assign or transfer any and all stocks, bonds or other securities, and any real or other property of Frontier at market price or at the best price obtainable at private sale, at such times and upon such terms and conditions as, in his discretion, he deems is in the best interest of the creditors of Frontier, and to take such steps as may be necessary to effect and carry out such sales, transfers and assignments; (12) authorizing the Liquidator to pay administrative costs, expenses and other obligations of Frontier out of the assets of Frontier; and (13) granting such other and further relief as the Court may deem just and proper.

The Order to Show Cause provides that pending the hearing and determination of the Rehabilitator's application: (1) the interim procedure order and the injunctions provided for in the Rehabilitation Order shall remain in effect; and (2) the payment of all claims other than workers' compensation claims shall be stayed.

A hearing is scheduled on the Order to Show Cause on the 28th day of September, 2012 ("Return Date") at 9:30 o'clock in the a.m., at Albany County Courthouse, located at 16 Eagle Street in the County and City of Albany, and State of New York.

If you wish to object to the petition, you must serve your objections and all supporting documentation ("Answering Papers") upon the Superintendent so as to be received by the Superintendent at least seven business days prior to the Return Date, and by submitting copies of the Answering Papers, with affidavits of service on the Superintendent, to the Court at the Albany County Courthouse, located at 16 Eagle Street in the County and City of Albany, and State of New York, seven days before the Return Date. Service of Answering Papers on the Superintendent shall be made by hand delivery, overnight mail or first class mail at the following addresses:

-Superintendent of Financial Services of the State of New York, c/o Attorney General Eric T. Schneiderman Office of the Attorney General, The Capitol, Albany, NY 12224,Attn: Assistant Attorney General Edward M. Scher

-William Costigan, Esq., Dornbush Schaeffer Strongin & Venaglia, LLP, 747 Third Avenue, New York, NY 10017

This Notice, the Order to Show Cause and the papers upon which the Order to Show Cause has been granted is posted on the Internet web page maintained by the New York Liquidation Bureau at http://www.nylb.org.

Requests for further information should be directed to Frontier Insurance Company in Rehabilitation at (845) 807-5250.

Dated: New York, New York, August 13, 2012

Benjamin M. Lawsky, Superintendent of Financial Services of the State of New York as Rehabilitator of Frontier Insurance Company

Perspectives

The United Kingdom is considering commercial insurance law changes that would strengthen risk managers' hands by making it more difficult for insurers to void coverage for innocent nondisclosure of information, says Ian Lupson, a partner in law firm Jones Day's London office. While an insurer still would be entitled to a fair presentation of the risk, a Law Commission proposal would in certain circumstances shift more responsibility onto insurers and make the underwriting process less one-sided.

Balance of power may shift in favor of risk managers

Mr. Lupson

How insurers would react if the law changes in this way is unknown, but they could be exhaustive in their questioning.

By Ian Lupson

Risk managers with exposures in the United Kingdom may have a strengthened hand in claims negotiations with insurers if recommended changes to commercial insurance law are approved.

The proposed reforms would leave more room for negotiation in cases where material issues were not disclosed to an underwriter and make it harder for insurers to void an entire insurance policy as a result of nondisclosures.

While it is still uncertain whether the reforms will be approved, they would mark a significant change in U.K. commercial insurance law.

The Law Commissions of England, Scotland and Wales in June issued a joint consultation paper recommending changes in English and Scottish insurance law on the topics of disclosure and warranties. The Law Commissions are independent bodies charged with reviewing law in the United Kingdom.

This article focuses on English law.

As a result of earlier work by the Law Commission, English insurance law in this area as it applies to personal lines business has been dramatically changed by the Consumer Insurance (Disclosure and Representations) Act 2012.

That statute, which comes into force in March 2013, modifies the holy grail of insurance law—an insured's duty of utmost good faith—and replaces it with an obligation to answer questions as asked with reasonable care. It also removes an insurer's rights to rescind coverage for innocent nondisclosure.

The Law Commissions' recommendations for commercial insurance law are less revolutionary and more evolutionary. Still, if enacted, they would represent a significant shift in the balance of power between insurer and policyholder and improve the position of the risk manager in a coverage dispute.

The first point to note is that—unlike the consumer sphere—it is not being suggested that a commercial policyholder should no longer be under a duty to disclose all material facts.

Rather, an insurer will remain entitled to a fair presentation of the risk. Where the change would come is that if a presentation leaves questions unanswered, the proposed law would place the insurer under a positive duty to ask those questions.

While this may still leave room for argument (Was the point unclear? Should the insurer have sought clarity?), imposing any positive duty on the insurer is to be seen as a move towards a more reciprocal and less one-sided underwriting process.

How insurers would react if the law changes in this way is unknown, but they could be exhaustive in their questioning.

When misrepresentation or nondisclosure is established, the proposal is to bring English law more into line with the position in civil code countries where the law is less draconian.

Currently, an insurer can void a policy for nondisclosure of a material fact, leaving a policyholder without any coverage. Under the proposed changes, provided that the nondisclosure was not deliberate, the insurer would be entitled only to a proportionate remedy. For example, if an insurer could establish that it would have charged a higher premium had it known an undisclosed fact at the time of underwriting, it would be permitted to charge an additional premium retroactively, but it still would be obliged to pay claims under the policy.

Voiding or rescinding the policy would be permitted only in cases of dishonest nondisclosure or misrepresentation.

Experienced hands will recognize that this is a change indeed, and one likely to be a significant benefit to commercial policyholders.

It is not to say that there might not still be coverage disputes—there are likely still to be many—but they will be about what the insurance says, not whether it is there at all.

So these are big changes that are being proposed, which I believe will help level the playing field in commercial insurance disputes.

Risk managers responsible for insurance programs that are in part or in whole subject to English law should be pleased with the Law Commission's recommendations thus far.

And there are other elements of the recommendations that risk managers should find favorable.

Another area in which leveling the playing field, from the policyholder's perspective, is proposed is in how English law treats breaches by policyholders of policy terms called warranties.

These are terms where, for example, a policyholder warrants that a building has a functioning fire alarm or sprinkler system.

Under English law, if such a term is breached, then the policy is void and, absent a waiver by the insurer, a claim likely would go unpaid as a result.

This is so even if the breach is not causative of or related to the loss, and even if it has been put right by the time that loss occurs. So, for example, if a building's fire alarm system has been off-line but is subsequently restored, the policy is void and a later loss for, say, theft risks would not be covered.

To help address this perceived unfairness, the Law Commission suggests that a policyholder should be given the chance to remedy a breach of warranty so that, rather than being automatically void, the policy is suspended during the breach period and then reinstated. The Law Commission also suggests that to justify avoidance or recision, a breached warranty must at least be relevant to the loss.

So, in the above example, if the Law Commission's proposals were adopted, it would mean that the policyholder would have the chance to fix the fire alarm so the building is covered if the building subsequently suffers a fire, and the building owner would remain covered for theft, and other unrelated risks, even during the period when the fire alarm system is inactive.

The Law Commission has not gone so far as to suggest, however, that the insurer needs to establish a casual link between a breach of warranty and a loss, so warranties still remain an issue.

Last in terms of warranties, and importantly, the Law Commission suggests that if an insurer requires an applicant for insurance to warrant the accuracy of its information, it must say so. Currently, an applicant who agrees that his answers will be the "basis of the contract"—words that usually appear in very small type just above the signature block—is providing just such a warranty without necessarily realizing it.

It is important to remember that this article is considering proposed—not actual—changes to the law. However, given the way in which the Law Commission's personal lines recommendations went much further in the changes suggested and were accepted by the U.K. government, it seems reasonable to assume that these proposals, or a near likeness, will pass into law.

The spur for examining this area of the law was in part a survey conducted by British risk management organization Airmic Ltd. that found that some 31% of its members had had nondisclosure issues raised against them between 2005 and 2010. These proposed changes in the law are aimed at reducing the incidences of dispute and would, I think, strengthen the risk manager's hand in the event that a dispute does arise.

In the meantime, it's important to remember that English law recognizes freedom of contract. It is therefore perfectly permissible for a policyholder to seek to negotiate the benefits referred to in this article even before any change in the law has been enacted. Many large policyholders already do so. Those that don't, and smaller and midsize players that haven't perhaps thought about it might consult with their brokers and lawyers about doing so.

Ian Lupson is a partner in Jones Day's London office. He is responsible for the firm's policyholder coverage practice in Europe, the Middle East and Africa. He can be contacted at iflupson@JonesDay.com. *This article is for general information only. It is not to be construed as legal advice on any specific facts or circumstances.*

Isaac: Hurricane floods Gulf Coast, tests New Orleans protection system

CONTINUED FROM PAGE 3

"Typically, you wouldn't expect much damage with a Category 1 (hurricane), but with a longer duration, (structural) fatigue builds up over time and you get damage you wouldn't see otherwise," he said. "We may see more tree damage that you might expect" due to the heavily saturated soil.

Isaac's lengthy stay along the Gulf Coast delayed getting claims adjusters on the ground to assess the damage.

Tom Larsen, senior vice president and product architect at Eqecat, said a thorough accounting of Isaac-related insured losses likely will take months, adding that it took years to sort out claims in the wake of Katrina.

> **'Typically, you wouldn't expect much damage with a Category 1 (hurricane), but with a longer duration, (structural) fatigue builds up over time and you get damage you wouldn't see otherwise.'**
>
> Tim Doggett, AIR Worldwide Corp.

"These are very difficult types of events to estimate," Mr. Larsen said. "It's far easier to estimate a loss when everything's wiped out."

As for the offshore oil and gas industry, AIR, citing U.S. Bureau of Safety and Environmental Enforcement data, said 505 platforms and 50 rigs were evacuated in advance of Isaac. AIR and Eqecat said last week they had not yet estimated insured offshore losses.

"Offshore platforms are owned by a very complex set of ownership groupings, so it's very difficult for us to provide a salient loss estimate," Eqecat's Mr. Larsen said.

Terry Leone, New York-based senior industry analyst at SNL Financial L.C., said that, while significant, the losses resulting from Isaac are unlikely to greatly affect insurers' balance sheets.

"Commercial property writers will be affected, but the losses should not be too large for any of the companies to handle," Mr. Leone said. "Another thing to note is that much of the damages appear to be caused by flooding, and flood losses are mainly insured by the federal government and may not have much impact on insurance companies."

J. Nicholas Ciabattoni, vice president-claim home officer property and U.S. marine at Chicago-based CNA Financial Corp., set up a center in Nashville, Tenn., to handle business-related Isaac claims.

"In addition to our group of general adjusters, we have a specialized team for large losses," Mr. Ciabattoni said.

"We overlay the wind fields associated with the storm with our geocoded properties," he said. "This gives us a view of how different customers are impacted in different areas and helps us know how to deploy our people."

AP PHOTO

A car was submerged in Plaquemines Parish, La., after Hurricane Isaac passed slowly through the region as a Category 1 hurricane, dumping more than a foot of rain in some areas.

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DMEC: New approach required

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groceries at a liquor store because of a lack of supermarkets in his neighborhood.

Managers' treatment of workers also has an impact, the panel said.

"When you steal someone's sense of control of their destiny, there is no way they are going to go home and be healthy or behave healthy, and what do they show up as?" Mr. Earl asked. "They show up as an absence. Or they show up as a claim."

To learn how employees feel about their work environment and managers, Sutter conducts an annual work experience survey as part of its leave management efforts, Ms. Messineo said.

"You would think, when you look at our health data, that the very, very sick are really driving our absence," Ms. Messineo said. But departments scoring low on the work experience surveys account for more absence issues.

That means helping managers become better leaders could reduce a negative impact on absence, the panel said.

"We have also noticed a correlation between employee satisfaction and workplace injuries and accidents," said Marlene S. Dines, executive consultant for integrated disability management for Kaiser Permanente in Oakland, Calif.

Kaiser's observation is based on integrated disability management, safety and employee wellness data, Ms. Dines said.

James H. McConville, vice president of group disability product development for MetLife Inc. in Bridgewater, N.J., moderated the session.

Target deploys clinical case management

By ROBERTO CENICEROS

DENVER — A successful pilot program involving tens of thousands of employees and a control group proved to retailer Target Corp. that clinical case management efforts could significantly reduce short-term disability durations.

The pilot program, launched in 2011, involved managing claims from 38,000 employees in the pilot group and the control group. It reduced STD durations by 7%, speakers told the Disability Management Employer Coalition's 17th annual International Conference.

The retailer's adoption of clinical case management included applying medical disability guidelines to make claims eligibility decisions, comprehensive training for case managers, and developing a "trigger list" to help case managers identify situations needing additional input from clinicians or peer review services.

"It was a significant cultural change for us, moving from a completely unmanaged program where for virtually all STD requests … you got your time paid" to a program that was comprehensively managed, said Michelle Steen, Target benefits analyst manager in Minneapolis.

Applying clinical case management practices to address STD claims came amid efforts by Target to outsource the administration of leave programs.

Target consulted Aon Hewitt and applied a two-phase approach: the pilot phase followed by a rollout to remaining eligible Target workers. The pilot phase lasted four months, said Gloria Gillette, claims operation leader for Aon Hewitt.

A control plan gave Target insight into what was happening with claims as it applied new processes, and it helped the employer gauge resulting outcomes, Ms. Gillette said

"The control plan was our way of looking throughout our operation to see what data we could follow to give us that information," Ms. Gillette said. "It was to ensure compliance, tell us how successfully the processes were being implemented, and identify areas for process improvement and training."

Feedback came from several sources including weekly dashboard reports on claims activity, employee satisfaction surveys, and frequent huddles with case managers to discuss what was working well and what needed improvement.

There was also a "comprehensive audit program" for additional feedback, Ms. Gillette said. "The result was an ability to identify needed adjustments quickly."

Target also matched employees in a control group with employees in the pilot program for similar demographic characteristics, disability program use and disability durations, said Deborah LaBonar, manager of analytic consulting in the absence management group for Aon Hewitt.

After four months, durations among the pilot group dropped by 7% compared with a baseline measurement. The control group saw durations increase by 11%.

"What we would assume is that, all other things being equal, had we not implemented this program, then the pilot group would also have trended up at about the same pace as the control group," Ms. LaBonar said.

It was a big step rolling the program out to 135,000 employees after testing it on 38,000 employees, Ms. Gillette said. Target did that by using the "tools and processes" tested in the pilot, with some improvements, she added. Case managers, for example, received additional training in physician contact and caseloads were adjusted to better address complex claims.

"The result was that we were ready to roll out to the remaining 90% of the population immediately after the conclusion of the pilot on the following Monday," Ms. Gillette said.

DMEC DRAWS 603

DENVER — A record 603 people attended the Disability Management Employer Coalition's annual conference held Aug. 12-15 in Denver.

Topics included integrating employer leave, absence management and improving return-to-work programs.

Also, Marcia Carruthers, a DMEC co-founder, announced her retirement as president and CEO of the organization, effective in February 2013. She will become chairman of the board while Executive Director Charlie Fox will become CEO.

DMEC's 2013 conference will be held Aug. 18-21 in Atlanta. More information is available at *www.dmec.org*.

—By Roberto Ceniceros

Reform: Mass. cost limits welcomed

CONTINUED FROM PAGE 4

onerous," said William Graham, vice president of policy and government affairs at Wellesley, Mass.-based Harvard Pilgrim Health Care Inc.

Mr. Graham noted that, among other things, the state has not yet revealed the specific reporting requirements providers and insurers will need to meet.

"There are a number of things in the law that will generate work for us that we really need the government to promulgate regulations and interpretations on before we can do anything," Mr. Graham said. "The state is going to need a whole bunch of data to determine if we're actually meeting those goals, and we're anticipating a decent-size work effort on our part to generate the data and reports that need to be turned in to the state," she said.

Employer groups have been similarly supportive of the legislation.

Aside from the broader aim of reining in price escalation, the law expands exemptions from certain penalties contained in earlier health care reform legislation and includes tax breaks for employers to create incentives for workplace wellness programs.

"Essentially, what it's done is change the way some of the 2006 penalties are calculated so that small employers aren't getting overly taxed," said Alden Bianchi, group leader of the employee benefits and executive compensation practice at Boston-based law firm Mintz Levin Cohn Ferris Glovsky & Popeo P.C.

Under the fair share contribution rules of the 2006 law, businesses with more than 11 full-time equivalent workers that do not provide sponsored health care must pay as much as $295 per employee. Businesses with fewer than 50 employees that do provide health care must demonstrate that at least 25% of their employees are enrolled in the plan.

The new law raises the threshold from 11 employees to 21, and allows employers to exclude workers who are covered under another health plan — through a spouse, Medicare or other means — from their count, making the 25% enrollment minimum for payrolls under 50 full-time workers more attainable.

"Those rules have made it a little bit easier for small and mid-sized businesses to meet the tests of the fair share provisions of the existing health care reform law," Mr. Bianchi said.

The new law also allows businesses, professional partnerships, sole proprietorships and other entities to deduct 25% of their annual wellness program costs from their state tax bills, up to $10,000 per year. Qualification for the tax credit will be determined by employers' compliance with existing regulations for state-sponsored wellness programs.

"From an employer perspective, it all makes sense to us, because having a healthy workforce leads to a more productive workforce," said Shawn Nowicki, policy director for the New York-based Northeast Business Group on Health.

The law does have its critics, however.

Jim Stergios, executive director of the Boston-based Pioneer Institute, said he is worried that compliance costs, fees and penalties associated with the law would be passed on to employers and individual consumers.

In addition, analysts at New York-based Moody's Investors Service Inc. said last month that they believe the law would damage the state's hospital industry by limiting revenue growth and reducing operating flexibility.

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Cyber risk in focus in *Business Insurance* webinar

Cyber breaches are on the rise, and they present a greater financial and reputational risk to companies, experts say.

In the *Business Insurance* webinar, "Cyber Security: Tips to Identify, Prevent and Mitigate Threats to Private Data," Alan E. Brill, the senior managing director of secure information services at Kroll Ontrack Inc., and Larry Collins, managing director and head of e-Solutions at Zurich Services Corp., discuss how to approach cyber breach readiness before and after an incident.

The free, 60-minute webinar can be viewed on demand at *www.BusinessInsurance.com*.

Relying on statistics found in the March 19 and June 25 issues of *Business Insurance*, Mr. Collins tackled the importance of preventative measures, including educating employees about safe Web usage. He recommends employers protect the sensitive information they hold, such as employees' addresses, Social Security numbers and bank account numbers. Breaches can result from people within the company unaware of how to handle a phishing scheme, former employees taking information with them after quitting and companies unaware of a data breach for months or even years after the initial incident.

Afterward, Mr. Brill discussed creating and implementing a response plan to a breach. He particularly stressed the importance of investigating a breach before reacting too quickly. In his first example, a hospital asked him to investigate a stolen laptop that contained 500,000 encrypted medical records.

Although the hospital was preparing to notify those who had their personal information stolen, Mr. Brill and his team discovered that the laptop was taken before the confidential information could be downloaded and no breach had taken place.

Business Insurance Senior Editor Judy Greenwald moderated the webinar.

—By Anna Gaynor

Venezuela: Disaster sparks more scrutiny of refineries

CONTINUED FROM PAGE 1

involvement in the reinsurance program, but they would not give further details.

Despite being one of the largest refinery accidents in recent years, insurers say any potential claim is unlikely to significantly affect the energy property market.

"It is still early days in terms of assessing damage and cause, but the accident in Venezuela was clearly a big event with a major vapor cloud explosion," said Stanley Cochrane, head of mining and onshore energy at Swiss Re Corporate Solutions, a unit of Swiss Re Ltd. "But from a property insurance perspective, it is not likely to be large event," he said.

The refinery did not carry business interruption coverage, an important driver in refinery claims, said Mr. Cochrane, who is familiar with details of the program. Typically, business interruption makes up 70% to 80% of a refinery claim, he said.

In addition, the fire did not appear to have spread to the critical processing area of the refinery, said Mr. Cochrane.

The loss also is unlikely to hit the energy insurance market hard due to the relatively large retention of PDVSA's captive, which is about $50 million, said Carlos Carrillo, Houston-based regional energy head at Allianz Global Corporate & Specialty, a unit of Munich-based Allianz S.E., who is familiar with details of the program.

"The loss is likely to be borne by PDVSA's captive and, even if it were to breach retention levels, it will not represent a catastrophic loss for the international insurance market," he said.

But the explosion at the Los Taques refinery follows several large refinery losses in recent years, said Mr. Carrillo. "There has been an increase in the frequency and severity of refinery losses in the past two years, and losses such as in Venezuela are making underwriters more aware of the potential volatility," he said.

The Jan. 6, 2011, explosion at the Canadian Natural Resources Ltd. refinery in Alberta resulted in a $489 million insured loss.

Last month, a fire caused the temporary shutdown of a refinery owned by Equate, a joint venture between Dow Chemical Co. and Kuwait's state-owned Petrochemical Industries Co. The closure may cost insurers $200 million.

Other refinery losses include a fire last month at a Chevron refinery in Richmond, Calif., although the company has a significant retention.

Underwriters have taken a more conservative approach to pricing refinery operations, and some energy companies have found it more difficult to complete their insurance programs, Mr. Carrillo said.

"The frequency of losses is scary and, if they continue, there will have to be a bigger effort to improve terms and conditions. Underwriters have growing concerns for the volatility and business interruption risk of refineries worldwide," Mr. Carrillo said.

AP PHOTO

Fires burned for days after an explosion at the largest oil refinery in Venezuela. Insurers have paid several refinery losses in the past two years.

Despite recent accidents, insurance capacity for refinery operations remains plentiful, said Andrew Herring, London-based head of energy for the Europe, Middle East and Africa operations of Marsh Ltd. Following higher-than-average energy losses in 2011, however, underwriters are more cautious, and some have pulled back on capacity offered on a per-risk basis. However, energy claims have returned to more normal levels in 2012, he said.

"Following the losses of 2011, underwriters are more nervous and are requesting more information," Mr. Herring said. "Underwriters have been looking to push rates up, especially in catastrophe-prone areas, but momentum has eased as profits improved in the first six months of 2012."

Last week's accident in Venezuela is not expected to change market sentiment, he said.

In the politically charged atmosphere ahead of presidential elections in Venezuela in October, media reports have raised questions over safety standards at the state-run Los Taques plant. Reports have alleged negligence and underinvestment in maintenance at the facility, but the cause of the explosion is not yet known.

In a statement, PDVSA said that it has launched an investigation into the cause of the explosion, although it confirmed that there had been a gas leak at the plant.

PDVSA's program premium has tripled over the past eight years, according to Mr. Carrillo.

"This suggests that the insurance market perceives that the risks is not the same quality it was ten years ago," he said.

inBrief

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ratios typically are experiencing higher increases and nonrenewal notices," Marsh says.

RIMS lobbies to FIO to support TRIPRA

The Risk & Insurance Management Society Inc. is advocating that the federal government maintain its financial support for a terrorism risk reinsurance program and abandon support for legislation that would alter the tax treatment of foreign-domiciled reinsurers. In an official comment letter submitted to Federal Insurance Office Director Michael McRaith, RIMS stressed the importance of federal support for terrorism reinsurance capacity to the insurance industry.

Most employers plan to keep health cover

Most employers say they will continue to offer health care plans after core provisions of the health care reform law take effect in 2014, but most say they will need to make plan changes later to avoid a new excise tax on the most costly plans, according to a new survey. Eighty-eight percent of employers surveyed by Towers Watson & Co. said they have no plans to terminate coverage in 2014 or after for full-time employees.

California debates workers comp reforms

California state lawmakers debated a massive workers comp reform bill last week as substantial workers compensation rate hikes in 2013 grow more imminent. S.B. 863, introduced late last month, aimed to settle many of California's comp woes by increasing permanent disability benefits for workers while limiting costs for various facets of the state's workers comp system.

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Compensation odds and ends in the U.K.

A British county council paid nearly $8,700 in compensation to an employee who alleged that a spinal injury resulted from wearing a too-tight uniform, according to a report.

The Northamptonshire County Council also paid £200 ($316) to a worker whose hand was pierced by a large splinter, according to information the London Daily Mail obtained under a Freedom of Information Act request.

In all, the county council paid out more than £350,000 ($553,350) in compensation to workers over the past five years.

That has taxpayers concerned that the bill for compensation has grown unacceptably large while some workers attempt to fleece the system.

Fend off questionable claims, one taxpayer advocate said. But with 15,000 employees, accidents occasionally happen, a county council spokesman countered.

Other compensation claims paid by the council include $17,600 to a staff member thrown into the air and injured when a shutter door opened, and nearly $12,000 to a claimant who strained her back when a co-worker moved a chair just as she was sitting down.

CONTRIBUTING: Roberto Ceniceros, Sheena Harrison, Bill Kenealy

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Lady Luck frowns on unshuffled deck

An Atlantic City casino is suing a playing card manufacturer after an unshuffled deck allegedly resulted in a lucky payday for several gamblers.

The Golden Nugget Atlantic City says a faulty deck from Blue Springs, Mo.-based card maker Gemaco Inc. allowed 14 mini-baccarat players to win $1.5 million at the casino in April, according to the Associated Press.

In its lawsuit, the Golden Nugget alleges that it used a Gemaco deck that was supposed to be pre-shuffled, but was not. According to reports, the mini-baccarat players were able to win 41 consecutive hands because the cards kept appearing in a repeated sequence while the players were at the table.

The casino also named the gamblers in its lawsuit, saying they violated state gambling laws, according to reports.

Laundromat prankster in hot water

A youthful indiscretion and a strict interpretation of new regulations intended to stop banks from hiring employees convicted of financial crimes have cost a Wells Fargo Home Mortgage employee his job.

According to the Des Moines Register, Richard Eggers of Des Moines, Iowa, was fired from his customer service job on July 2 after the bank learned of his 1963 conviction for "operating a coin changing machine by false means" after he attempted to use a cardboard cutout of a dime at a laundromat.

The decades-old conviction came to light after the bank hired a background-screening firm to scour the arrest records of employees in the wake of new ethics guidelines for bank employees issued in May 2011 by the Federal Deposit Insurance Corp. Intended to thwart people convicted of serious crimes such as money laundering from working in prominent positions at banks, the law instead has affected mostly low-level employees, an attorney for Mr. Eggers said.

While the FDIC provides a waiver for people convicted of small crimes to prove that they are worthy of employment, the process can take six to 12 months.

HEINZ IN A SQUEEZE OVER PACKET DESIGN

An Illinois man has put the makers of Heinz ketchup in legal pickle, claiming the company stole his idea for a better ketchup packet.

On Aug. 1, Scott Alan White filed a patent infringement suit against H.J. Heinz Co. L.P. in U.S. District Court for the Northern District of Illinois. Mr. White claims Heinz's new "Dip & Squeeze" condiment packets bear too close a resemblance to his invention, the CondiCup, which is designed to fit into a vehicle's cup holder and designed to enable either dipping or squeezing of a condiment.

According to lawsuit, Mr. White, a fast food and drive-through window customer, conceived the dual-purpose packet in a "flash of inspiration" and filed a patent application for his invention in October 2005. The lawsuit also states that Mr. White briefed Heinz executives about his invention in the summer of 2006.

Judge Marvin E. Aspen is scheduled to hear the case.

"Heinz won a similar lawsuit earlier this summer," a Heinz spokeswoman said in an email. "This is another frivolous lawsuit, and we will aggressively defend our position and demonstrate that the allegations are groundless and without merit."

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