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Judge rejects fraud charge against surety insurers / 3

French insurers tallying flooding claims / 33

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Loan ban sparks 401(k) worries

Employers fear broad reading of corporate governance law

By JERRY GEISEL

WASHINGTON—Employer fears that the new federal corporate governance reform law could jeopardize 401(k) plan loan programs they offer employees may be unfounded.

Those fears have accelerated in recent weeks as benefit consultants and attorneys have intensified their analysis of the Sarbanes-Oxley Act, legislation Congress passed in July in response to a wave of corporate and accounting scandals.

In particular, benefit experts have focused on Section 402 of the new law, which prohibits public companies from making or arranging, directly or indirectly, personal loans to corporate executive officers and directors.

Benefit experts say the wording of the statute is so broad that it could include loans offered through 401(k) plans, a feature available in most plans.

While the employer is not lending the money, it has arranged for the 401(k) plan and has facilitated the loan, said Ethan Kra, chief actuary for Mercer Human Resource Consulting in New York. "There has been involvement by the employer," he added.

While few believe Congress intended 401(k) plan loans to be covered under its ban on corporate loans to their top executives, the penalties for violating the Sarbanes-Oxley act are so stiff, including multimillion-dollar fines and prison sentences, that some employers aren't taking any chances and have ceased making 401(k) plan loans available to top executives.

"Some employers are choosing to block loans to executives until further guidance," said Valerie Miller, a legal consultant with Hewitt Associates Inc. in Lincolnshire, Ill.

But that action could lead to other legal problems. Under the Employee Retirement Income Security Act, if a savings plan offers loans, those loans must be available on the same basis to all participants. If they aren't, providing loans would be considered a prohibited transaction, which is punishable by fines.

Faced with those possibilities, an employer might be inclined to eliminate 401(k) plan loans

See **401(k)**/page 37

Quality of health care improving

NCQA sees gains in managed care

By MARK A. HOFMANN

The quality of health care provided by managed care organizations is continuing to improve, according to a survey released last week by the National Committee for Quality Assurance.

These improvements come despite rising costs. In fact, some health care experts who commented on the survey's findings after its release at a Washington conference said that increasing prices could enhance the drive toward quality.

"The State of Health Care Quality: 2002" was the sixth such annual report issued by the NCQA. The results were based on information provided by 271 commercial health maintenance organizations and point-of-service plans, plus a number of Medicare and Medicaid managed care organizations. The reporting plans cover about 71 million people—including about

See **NCQA**/page 37

PHOTO: AP/WIDE WORLD

Lloyd's underwriters declared Sri Lanka a war zone and imposed war risk surcharges on airlines there following the July 2001 terrorist bombing of two Sri Lanka Airlines planes.

European airlines fear war will ground fleets

By STACY SHAPIRO

LONDON—European airlines are concerned that they may be grounded by a lack of aviation war risk liability insurance if the United States carries out a large-scale attack against Iraq.

The airlines fear that aviation underwriters will cancel their coverage for third-party and passenger war risk liabilities with short notice, forcing the airlines to ground their fleets.

"We are extremely concerned at the moment," said a spokesman for the Assn. of European Airlines in Brussels. The threat of war in Iraq "really, really worries us."

Tensions remain high between the United States and Iraq, and the Bush administration has threatened military action to force Iraq's compliance with U.N. Security Council resolutions on weapons of mass destruction.

See **WAR RISK**/page 38

Late News

SCOR ends negotiations on buying Gerling book

French reinsurer SCOR S.A. has called off negotiations to acquire the life operations and certain nonlife reinsurance operations of Gerling Group. A spokeswoman for Paris-based SCOR said that, given recent stock market movements, the company decided that the deal would not add any value for SCOR shareholders. SCOR earlier this month entered into exclusive negotiations with Gerling over the possible acquisition of the group's life reinsurance business and much of its nonlife reinsurance business. The proposed deal would have involved a mix of equity and debt.

Judge seals documents on WTC placement

A federal judge overseeing the World Trade Center property insurance litigation has sealed documents produced by Willis Group Holdings Ltd. related to the brokerage's potential errors and omissions exposure on the placement. Judge Martin ruled earlier this month that Willis must produce the documents demanded by WTC insurer Swiss Reinsurance Co., which is seeking to show that Willis officials' worries about an E&O claim influenced their testimony in favor of WTC leaseholder Silverstein Properties Inc. Silverstein issued a statement denying any plans to sue Willis.

Projects stalled by terror risk grow

A lack of terrorism insurance has delayed or canceled more than $15.5 billion worth of real estate projects in 17 states, according to survey by a real estate trade group. The Real Estate Roundtable released the data, drawn from an ongoing survey of its members, during a meeting with Treasury

See **LATE NEWS**/next page

Spotlight

REINSURANCE RENDEZ-VOUS REPORT

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Inside

Consumer-driven plans may have downside

Widespread use of consumer-driven health plans could lead to drastic adverse selection in health plans, damaging the nation's health care system, one researcher warns. Page 4

Looking for cycles in cycles

Editor Paul Winston suggest new ways of looking at what makes the insurance world go around, now that we know the cycles did not disappear for good. Page 6

Clarification needed on executive loan ban

Congress should make clear that it did not intend for corporate governance rules barring executive loans to apply to 401(k) plan lending provisions, one of this week's editorials says. Page 8

NAIC compact proposal revised

The president of the National Assn. of Insurance Commissioners is urging a vote on a proposal to speed up the introduction of new life and annuity products. Page 26

FSA examining finite risk rules

Reinsurers are welcoming proposals for tougher U.K. regulation of "financial engineering" by insurers, which they say could help the market for financial reinsurance. Page 33

U.K. pension changes may spur labor actions

U.K. unions may increasingly call for labor actions to try to prevent employers from closing defined benefit occupational pension plans to new participants, warns the Trades Union Congress. Page 33

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REPORTING WEEKLY ON CORPORATE RISK, EMPLOYEE BENEFIT AND MANAGED HEALTH CARE NEWS

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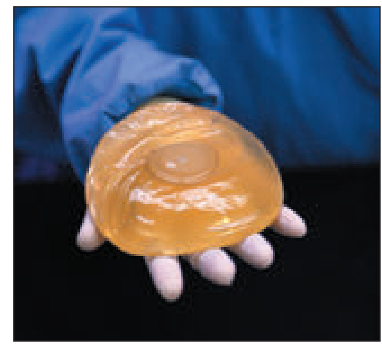
CONTINUED FROM PAGE ONE

Secretary Paul O'Neill. The group had reported on Sept. 4 that at least $10.5 billion worth of projects in 13 states had been adversely affected by the terrorism insurance crunch.

Late News



Judge OKs Dow Corning breast implant settlement

The judge overseeing the bankruptcy of Dow Corning Corp. has approved a $9.8 million settlement the company reached with the U.S. government over breast implants Dow Corning manufactured. The settlement will reimburse federal agencies for funds paid for the removal of Dow Corning breast implants in women who were beneficiaries of government assistance, such as Medicare or Medicaid. The settlement brings Dow Corning one step closer to wrapping up the $3.2 billion global settlement the court approved in 1999.

Tribune sues Swiss Re over workers comp claims

Tribune Co. is suing Swiss Reinsurance America Corp. for $20 million in workers compensation claims it says are owed under a program Times Mirror Corp. placed with Reliance National Indemnity Co. in 1998. Tribune, which acquired Times Mirror in 2000, charges that Times Mirror paid Reliance more than $40 million to administer and pay all its workers comp claims after Jan. 1, 1977. According to the suit, Reliance fronted the coverage, passing it through to Swiss Re.

RMS releases terrorism risk model

Risk Management Solutions Inc. has a risk model that is designed to help insurers and reinsurers quantify risks from catastrophic terrorist attacks in the United States. The model is based on so-called "game theory," which holds that the likelihood and targets of future terrorist attacks can be modeled by understanding the operational and behavioral characteristics of terrorist groups.

N.Y. malpractice crisis overstated: Report

New York state physicians do not face a medical malpractice crisis, a report suggests. The report by the New York Public Interest Research Group states that, contrary to doctor groups' assertions, the number of medical malpractice payouts has increased only slightly in the past 10 years, to 2,090 in 2001 from 1,943 in 1992. The report does note, however, that the average payout for the three New York counties with the largest number of claims has increased.

School district settles civil rights case

The bulk of a $7.5 million settlement over a longstanding civil rights dispute involving a suburban Seattle school district will be paid by the Washington State Risk Management Pool. Puyallup School District is one of 70 school districts and five educational service districts that participate in the pool, which writes various liability and property coverages. The lawsuit, filed in 2000 on behalf of 23 parents and 36 students, charged that racial harassment and discrimination continued in the school district despite a 1998 agreement with the federal Office of Civil Rights to implement a no-tolerance policy against such behavior.

Louisiana considering changes to insurance laws

Acting Louisiana Insurance Commissioner J. Robert Wooley is seeking feedback from insurers on whether regulatory and legislative changes would attract more insurers to the state. "We will try to put together legislation to address their concerns," Mr. Wooley said last week, after sending a letter to insurers soliciting comment. "We're trying to give them what they are asking for, a healthy competitive atmosphere where they can do business," Mr. Wooley said.

Briefly noted

Moody's Investors Service has downgraded its insurance financial strength rating of **Munich Reinsurance Co.** to Aa1 from Aaa. Moody's also downgraded Munich Re subsidiary American Re-Insurance Co. to Aa2 from Aaa. Moody's put the ratings under review after the Munich, Germany-based reinsurer in July said it would increase American Re's reserves by $2 billion and raised its loss estimate for the Sept. 11, 2001, terrorist attacks by $500 million....**Walter B. Kielholz**, chief executive officer of Swiss Reinsurance Co. and vice chairman of the board of Credit Suisse Group, has been named chairman of Credit Suisse. The board of Swiss Re will determine whether Mr. Kielholz will retain his position at the reinsurer, a Swiss Re spokesman said....**Oxford Health Plans Inc.** Chairman and Chief Executive Officer Dr. Norman C. Payson will retire at year end. He will be succeeded by current President and Chief Operating Officer Charles G. Berg. Dr. Payson became of chairman of the Trumbull, Conn.-based managed care company in 1999....Lloyd's of London company **Advent Capital Holdings P.L.C.** plans to merge its marine syndicate 2 into its nonmarine syndicate 780. If Lloyd's approves the merger, the combined syndicate would have £250 million ($388.1 million) in capital for 2003. Advent also said it has raised £30 million ($46.6 million) through a share issue....Oldwick, N.J.-based A.M. Best Co. has placed its financial strength ratings of **Allianz A.G. Holding's U.S. subsidiaries** under review, with negative implications. Best also affirmed Allianz's A++ rating but changed its outlook to negative from stable. Best cited Allianz's move to boost U.S. unit Fireman's Fund Insurance Group's asbestos and environmental reserves by $750 million.

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To get breaking news as it occurs, visit *Business Insurance*'s free online Daily News, at *www.businessinsurance.com.* Sign up for your daily e-mail of breaking news. All the material in the Late News column, as well as other content in this week's issue, is generated from daily news postings that appeared on the *BI* Web site in the previous week.

Online this week:

- Cast your vote in *BI*'s latest **online poll**: Will your company offer a defined contribution health plan next year?
- Check the **Datebook** calendar for upcoming industry meetings and events or add your own.
- The **online forum** lets readers exchange ideas and information.
- Keep track of insurance stock activity with the *BI* **Stock Ticker.**

Discounted reservation deadline nears for annual event

Work comp conference to examine changes

By MEG FLETCHER

SAN FRANCISCO—The deadline nears for discounted reservation fees for *Business Insurance*'s 10th Annual Workers Compensation and Disability Management Conference on Oct. 21-23.

Staying on top of the latest developments in workers compensation and disability management is all the more important to employers in today's difficult market.

The need to stay abreast of such changes will be a key focus of the 40 speakers at the upcoming conference, which is presented in conjunction with IBF Conferences Inc., of Rockville Centre, N.Y. The conference will be held at the Hyatt Regency San Francisco in Embarcadero Center.

The presenters—a diverse group of risk and benefit managers, loss control specialists, attorneys and consultants from private industry as well as the Occupational Safety and Health Administration—will share their insights and suggestions about how employers can weather this challenging time.

The conference also will present an extensive update on legislative and legal trends that may create new liabilities for employers.

Conference topics were chosen and developed with the help of nearly two dozen members of an advisory board, which is chaired by Jeffrey W. Pettegrew, vp-insurance and risk management at Westaff Inc. in Walnut Creek, Calif.

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WORKERS COMPENSATION AND DISABILITY MANAGEMENT CONFERENCE

Preceding the formal conference is the annual Employers' Private Roundtable, at which employer representatives can candidly discuss pressing concerns and seek advice from their colleagues. Moderating the roundtable will be *Business Insurance* editor Paul Winston and Mr. Pettegrew.

This year's conference will also feature a new event, the Service Providers Roundtable, which will be held concurrently with the employer discussion. Service providers will be able to exchange ideas about employers and how to address their needs and expectations. The discus-

See **CONFERENCE**/page 38

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Federal group health program to see 11.1% premium hike

By JERRY GEISEL

WASHINGTON—Insurance premiums for health plans covering federal employees and retirees will increase by just over 11% on average next year, which is a much smaller hike than most large employers are likely to see for 2003.

The Federal Employees Health Benefits Program—the nation's largest group health program, with 8.6 million participants—will also make some changes in its benefit offerings next year, including adding flexible spending accounts.

Next year's 11.1% average increase in the FEHBP compares with a 13.3% hike for 2002 and a 10.5% increase for 2001. Premiums charged by health maintenance organizations in the federal program next year will rise by an average of 13.6%, while hikes for other types of health care plans will climb by an average of 10.5%. In all, 188 plans are offered, though some are limited to certain regions.

The FEHBP's 11.1% average premium increase is substantially lower than what some large organizations have projected for 2003. For example, earlier this year, the California Public Employees Retirement System, the nation's second-largest group purchaser of health care benefits, said that premiums for the HMOs it offers would rise next year by an average of about 25% (*BI*, April 22).

In addition, benefit consultants have been warning employers to expect rate hikes of at least in the low teens next year, while respondents to a recent survey of the Washington Business Group on Health reported that premiums would rise by an average of 14% in 2003, said Helen Darling, president of the employer group.

FEHBP officials attribute their success in holding down premium increases—at least compared with other big health care purchasers—to tough negotiations and to the design of the program, in which dozens of insurers compete for the business.

"Having a choice of plans promotes healthy competition among carriers for subscribers and helps contain costs," said Kay Coles James, director of the Office of Personnel Management, the federal agency that administers the FEHBP.

In addition, changes in plan design, such as

See **FEHBP**/page 37

PHOTO: ROLL CALL

The American Postal Workers Union next year will offer a consumer-driven health plan option as part of changes in the Federal Employees Health Benefits Program.

Judge dismisses Chase fraud suit against insurers

By DOUGLAS McLEOD

NEW YORK—A federal judge has dismissed fraud charges leveled by JPMorgan Chase Bank against 11 insurers that have refused to honor surety bonds securing nearly $2 billion in purported Enron Corp. oil and gas deals.

The insurers are seeking to rescind the bonds, charging that the prepaid oil and gas deliveries they supposedly secured were in fact fraudulently disguised loans that Chase made to Enron through a Jersey, Channel Islands, entity called Mahonia Ltd. Enron defaulted on the Mahonia contracts when it filed for bankruptcy last year.

Chase earlier this year amended its original breach-of-contract lawsuit against the insurers to add fraud charges. The bank alleged that the insurers knew that the deals were financing transactions and that the insurers concealed from Chase that the bonds might violate New York insurance laws.

U.S. District Court Judge Jed S. Rakoff, however, threw out the bank's fraud claims in a one-paragraph order. The order leaves intact Chase's original claim for breach of contract.

A Chase spokesman expressed disappointment but said, "We will vigorously pursue our original claim for breach of the surety bonds."

National Conference of the Profit Sharing/401(k) Council of America

Fiduciary duties demand attention

By RODD ZOLKOS

CHICAGO—The recent spate of company stock disasters and the general downturn in the markets overall has created a setting not unlike that in which Congress implemented existing employee retirement plan fiduciary rules, a retirement plan law expert said.

"I think it's interesting because there are a lot of similarities between now and 30 years ago when ERISA was implemented," said R. Eric Starr, assistant general counsel of INVESCO Retirement Inc. in Atlanta. "So I think that means we're going to see a lot of activity on the pension reform front."

Speaking at the 55th National Conference of the Profit Sharing/401(k) Council of America last week in Chicago, Mr. Starr noted that in crafting the Employee Retirement Income Security Act of 1974, Congress created a uniform set of rules for fiduciary plans, as well as reporting and disclosure requirements for those plans.

ERISA defines the activities under which one has fiduciary responsibilities to a retirement plan, Mr. Starr said, as well as establishing that functions considered "ministerial" in nature—such as calculating benefits, holding records, accounting and consulting—are not subject to fiduciary requirements.

But, despite those definitions, in participant legal actions against plans, "These lines are being constantly blurred," Mr. Starr said.

More conference coverage on page 36

"When a plan doesn't do well, participants are going to be looking for anybody who could've contributed to that."

Among the standards of conduct in ERISA is that the fiduciary act "solely and exclusively in the interests of the participants," Mr. Starr said. The law also includes "the prudent man rule," requiring fiduciaries to act "with the care, skill, prudence and diligence of a prudent man."

"This is one that I think is very important and is sometimes misinterpreted," Mr. Starr said. He noted that the rule requires that if fiduciaries lack expertise, they must obtain expert advice, but also that they understand and evaluate that expert advice before following it. "Even if you have an expert giving you advice, you have to understand it," he said.

See **PENSION**/page 36

IUMI 2002

Terrorist threats spur security efforts

By DOUGLAS McLEOD

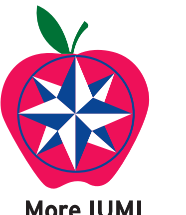
NEW YORK—The threat of a terrorist attack using cargo containers and ports is leading government agencies and private groups to create new security procedures for shipping, several experts report.

The U.S. Customs Service, U.S. Coast Guard and the International Maritime Organization are among the agencies developing programs ranging from inspecting "high-risk" containers to creating a system of security alerts and accompanying procedures for ships and ports.

"Shipping is an international business. Terrorism is an international threat. What we need to work on are meaningful international solutions," Joseph Angelo, a director of standards for the U.S. Coast Guard in Washington, told an audience at the 2002 meeting of the International Union of Marine Insurers in New York.

About 90% of the world's cargo moves by container, with 200 million containers moving between major seaports globally each year and more than 16 million arriving in the United States by ship, truck and rail, the Customs Service said.

The threat of nuclear or other weapons in containers is real: The Central Intelligence Agency has concluded that the United States is more likely to be hit by a nuclear device delivered by container than by intercontinental ballistic missile, said Capt. Jon Helming, an associate professor with the U.S. Merchant Marine Academy in Kings Point, N.Y.



More IUMI conference coverage page 28

The Customs Service earlier this year launched a Container Security Initiative intended to keep out potentially dangerous cargo. Under new Customs regulations, carriers must provide U.S. Customs officials in foreign seaports with cargo manifests 24 hours before vessel loading. Customs officers use various criteria to identify "high-risk" containers, and those containers are "pre-screened" before they are shipped. Inspectors have also begun testing tamperproof electronic seals on screened containers.

Ports in Canada, Singapore, Netherlands, France and Germany are among those that have agreed to participate so far. In June, the Brussels, Belgium-based World Customs Organization adopted a resolution allowing ports

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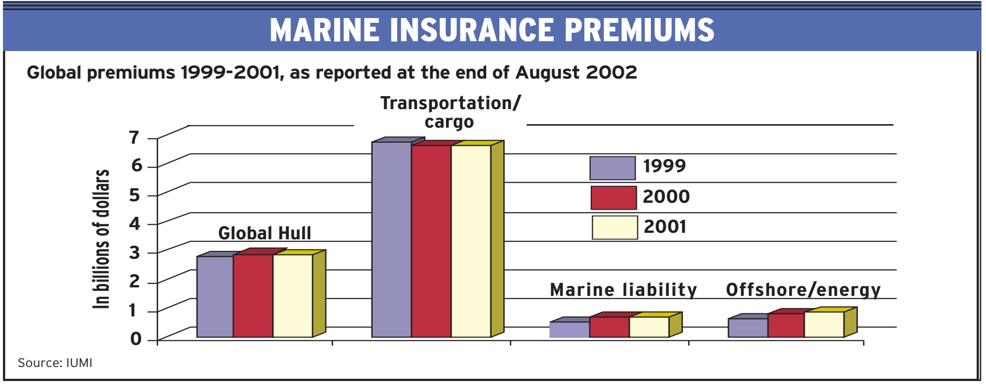

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Consumer-driven care may have unintended results

By MICHAEL PRINCE

NEW YORK—Turning health care users into health care consumers might resolve some problems with the health care system, but there is also a risk that it could do more harm than good, a researcher warns.

Given a choice, young and generally healthy employees would be more likely to opt for consumer-driven health plans, which could leave older and unhealthy people in traditional managed care arrangements. Such adverse selection could eventually destroy the employer-based health care system, said Humphrey Taylor, chairman of Harris Interactive in New York, a research and polling organization that has conducted considerable research on health care issues.

Consumer-driven health plans can be "a recipe for unraveling the health care system," Mr. Taylor told attendees at a conference in New York last week sponsored by the New York Business Group on Health.

Despite his dire warnings, Mr. Taylor said the impact of consumer-driven plans on the health care system has been small to date.

Surveys of consumers indicate that few desire to make more decisions about their health care purchasing.

Only 8% of people in a Harris survey welcome the idea of becoming more involved in purchasing decisions by basing their health care choices on what they regard as the best value for their money.

Twenty-eight percent of people surveyed fell into a group he called the "reluctantly empowered." Such people are forced to make decisions but "don't necessarily want to," he explained.

About a quarter of respondents are "needy shoppers" and are either low-income or sick and buy health care when they can afford it.

The remainder did not yet fall into any of those categories.

Mr. Taylor said that few people thus far have become true health care consumers. A consumer, he explained, is someone who looks for information about a product or service and is then influenced by that information.

Using that standard, a true consumer market for health care has not yet arrived, he said.

For example, only 22% of surveyed consumers said they have seen quality rating information on hospitals. Of those, only 4% have considered making a change based on those ratings, and only 2% actually made a change.

"As yet, not many people are making changes on information that compares different providers," Mr. Taylor said.

But that could change as people pay more for their health care, as health costs grow and their share of the premium rises, he said.

With health care costs rising and the economy in a slump, Mr. Taylor said he expects the issue of health care to rise in importance with the public. For support, he cited the "Health Insurance Misery Index" which reflects increases in health care costs and the unemployment rate. For 2002 the index stands at 17.8%, the highest level since 1994, he said. And such a level historically indicates a rising interest in health care as a political issue and with employers.

The consumer mentality will also increase as employers shift more costs on to employees.

Mr. Taylor said that 74% of surveyed employers plan to increase employees' premium contribution in the next two years, the most commonly cited cost-shifting strategy. In addition, 68% of employers plan to increase cost-sharing efforts, including raising deductibles and copayments. As a result, employers expect this will make employees better health care consumers and reduce utilization of unnecessary health care services.

"Cost-shifting is forcing individuals to behave like consumers," he added.

But this shift of mentality might have unintended consequences, he warned.

While many people will become health care consumers, this is not a role they want, he said.

"People don't necessarily want to be empowered," he said.

In addition, given a choice people will select the health plan that best meets their needs and "this is a recipe for adverse selection," he said, leading to a "death spiral" where some health plans absorb greater numbers of sick people and then are forced to raise rates, further driving out the healthy.

"On health care, an educated consumer could end up being our worst nightmare" and could lead to the end of employer-sponsored health care, he said.

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Errors & omissions

• A Sept. 9 chart of the largest U.S. reinsurers' first-half 2002 results, as reported to the Reinsurance Assn. of America, listed an incorrect figure for Folksamerica Reinsurance Co. Folksamerica Re's policyholder surplus for the first half was $817.1 million.

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Benefit managers recommend consumer-driven plan option

By MICHAEL PRINCE

NEW YORK—More employers should dip their toes in the water and get into the pool of companies adopting consumer-driven health care plans, a trio of benefit managers recommends.

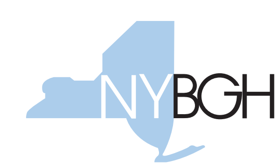
The benefit managers said they were pleased so far with their experience using three different plans and recommended that others join them in offering consumer-driven health care plans.

"Don't wait, get started" with a pilot program, advised Don Broecker, director of employee benefits at Charter Communications in St. Louis.

"Get the concept going and start the education program," he added.

The benefit managers recommended that employers offer a consumer-driven plan as an option while educating employees about the plans.

William Flannery, director of compensation and benefits at Novartis Corp. in New York, told attendees they should look closely at consumer-driven plans "as another alternative to your other health care products."



Novartis began offering one such plan developed by Lumenos to about 6,000 retirees starting in 2001 and extended it to active employees this year. While few employees have joined the plan this year, that number will grow as more learn about it, he predicts.

The Episcopal Church Medical Trust started offering Aetna Inc.'s consumer-driven product this year to about 1,000 employees studying in the church's seminaries, said Timothy Vanover, manager-products and marketing for the trust in New York. So far, the health plan has been well received by the seminary students, who appreciate having control over the money in their medical accounts, he said.

The consumer-driven approach has also pleased employees at Charter Communications, Mr. Broecker said. "By giving choice, we felt our employees would value the health benefit more," he said.

To date, about 6% of the company's employees have joined the plan offered by Definity Health, he said. "So far we're very pleased."

Paul Winston

Cycle reappears, with attitude

Cycles in the insurance industry are generally regarded as a recurring force of nature, just like Halley's comet, the tides and bell-bottom pants.

Sure, there were a few years in the 1990s when buyers and sellers alike thought the cycle had disappeared for good, and some pundits made heartfelt proclamations like: "The cycle is gone forever and *this* is the market." I bet these are the sort of people who boldly make declarations like "rum won't give you a hangover," with predictable consequences.

Last year, though, the cycle came roaring back with a vengeance that surprised even insurers and reminded us all that you can run, but you can't hide from a force of nature. And now we are all suffering from that hangover.

If you look at academic explanations of insurance market cycles, you generally find they are described as dislocations between capital and pricing. If rates are high, as they are now, it attracts more capital to business. But as industry gains excess capital, it lowers rates, which eventually drives away capital. Throw in wild cards like claims and investment losses and you have the sort of mess we find the market in today.

The cycle came roaring back with a vengeance that surprised even insurers.

But I think there are other aspects of the cycle than these dry economic factors that are worth examining. I regard these as basically attitudinal about-faces that occur in the minds of the insurance-buying public. Some of these have to do with perceptions of—and tolerance for—the pricing cycle. Many of them are shaped by reaction to the cost of insurance, though some are attitudes that probably shouldn't flip flop but instead remain constant regardless of price.

I'm only going to present the polar opposites of these opinion cycles, for simplicity's sake. This is the same reason that people simply say hard or soft market, rather than attempting to label the myriad degrees of rigidity or softness as if describing a piece of cheese (e.g., a nice semi-soft ripe market).

So here are what I regard as some possible cycles within The Cycle:

- Wanting tort reform to restrict runaway damage awards vs. support for relying on a jury's common sense.
- Regarding insurance as a relationship vs. a commodity.
- Mistrust of insurers vs. appreciation for the security that an insurer provides.
- Trying to keep costs down to avoid losses/insurance claims vs. the attitude that losses are of no consequence because insurance will cover them.
- Shopping around for the lowest price vs. sticking with a longstanding insurer. (A corollary: Providing coverage to the policyholder who will pay the most vs. giving a break to a longstanding customer.)
- The willingness to retain risk vs. the desire to transfer risk.
- Direct markets vs. broker markets.
- Enterprise risk management vs. traditional risk management.
- Wanting insurance services to be unbundled and transparently priced vs. wanting everything bundled under a single premium.
- Investing in stocks vs. investing in bonds.
- In-house risk management vs. outsourcing risk management.
- Trying exotic risk financing alternatives vs. buying traditional insurance products.
- Investing in Lloyd's of London vs. buying coverage from Lloyd's of London.
- Being risk tolerant vs. risk averse.
- Multiyear insurance contracts vs. single-year contracts.
- Turning to the surplus lines market for coverage vs. sticking with admitted markets.
- Excess of loss vs. pro rata.
- Covering multiple lines of risk under a single vertical insurance limit vs. separate limits for each silo of risk.
- Retrospectively rated programs vs. paying up front.
- Focusing on domestic business vs. global expansion.
- Seeking a one-stop financial services provider vs. shopping for each service in individual "boutiques."

It's interesting to consider how such cycles within cycles might accelerate or decelerate the big cycle, but after a while, tracking these little orbits might make your head spin. It's probably easier to just grit your teeth and wonder if the soft market will ever return or if *this* is the market.

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Susan Watson & Jim Nealon,
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Editorial

Clarifying ban on loans is crucial

DID CONGRESS intend for 401(k) plan loans to be included when it banned, as part of a broad corporate governance reform bill, companies from making loans to top executives?

We certainly don't think so. The ban on company-provided or -arranged loans came in response to stunning revelations of companies that made—and did not always disclose the fact to shareholders—huge, low-interest loans to executives who were already richly compensated. As icing on the cake, some of these companies also later forgave the loans and bumped up the execs' salary to cover taxes owed on the forgiven loans.

"Outrageous" hardly overstates such arrangements. Certainly, Congress acted correctly to rein in those practices.

Regrettably, in their haste to put a stop to such corporate wrongdoing, federal legislators were not as precise as they should have been in drafting the ban on loans. Some employee benefit experts are now concerned that the ban on corporate loans to top executives could also prevent 401(k) plan loans to other employees.

While it may be preposterous to believe that Congress had such an intent—borrowing from one's 401(k) account balance is hardly the same thing as a top executive getting a fat loan from his or her employer—the legislative language, we believe, is so vague as to require clarification of this issue either from Congress or the Securities and Exchange Commission.

It likely would be no big deal to highly paid executives if Congress did, in fact, intend to stop them from being able to borrow from their 401(k) plans. The maximum amount that can be borrowed from a 401(k) account is small change for most senior executives.

Unfortunately, though, the way another federal law—the Employee Retirement Income Security Act—is drafted, if loans are not available to all plan participants, including top executives, then any loans provided by the plans would be considered prohibited transactions.

In other words, banning 401(k) plan loans to top executives could effectively kill the ability of the plans to provide loans for other participants.

That truly would not be in the public interest.

There is no question that the availability of loans encourages rank-and-file employees to contribute to the retirement savings plans. They know if they ever really need the money in their account balance, a certain amount is available.

Take away loans and the net effect is less savings for retirement. Regulators and Congress must not let that happen. Prompt clarification of the issue is in order.

Managed care quality makes gains

A RECENT SURVEY on health care quality should serve as a reminder that employers can ill afford to make cost the sole criterion when determining what coverage to offer employees.

As we report on page 1, the National Committee for Quality Assurance found that managed care plans showed improvement in the delivery of care in a variety of areas—ranging from the use of beta blockers to the percentage of children receiving chicken pox vaccines—for the third straight year. And, in an ironic twist, these quality gains have come at a time when managed care has lost much of its luster and is in fact under assault from lawmakers and some portions of the public.

Meanwhile, health care costs continue to rise. To no one's surprise, a recent Kaiser Family Foundation study showed, employers are cutting back coverage and asking employees to shoulder more of the burden of their health care. That's fair enough, for there is no legal obligation for an employer to provide coverage, let alone foot the entire bill for it.

But the NCQA survey underscores the fact that, even in a time of medical inflation, cost can't be the sole measure when designing a plan. As NCQA President Margaret O'Kane noted, every child who doesn't get chicken pox probably means there's a parent who isn't missing two days of work, thus cutting into productivity and profit. And that's at a minimum—a child who suffers complications from a disease often dismissed as a mere rite of passage can perhaps even go blind—and parental lost work time that could be prevented by a shot.

That's a powerful argument for continuing the emphasis on quality health care. For employers to focus only on the direct costs, of providing the minimum acceptable amount of coverage as cheaply as possible without taking indirect costs into account as well, could prove once again the folly of being pennywise and dollar—or indeed many dollars—foolish.

Schillerstrom

"HOLD ON...I THINK WE MAY HAVE FOUND SOMETHING HERE...."

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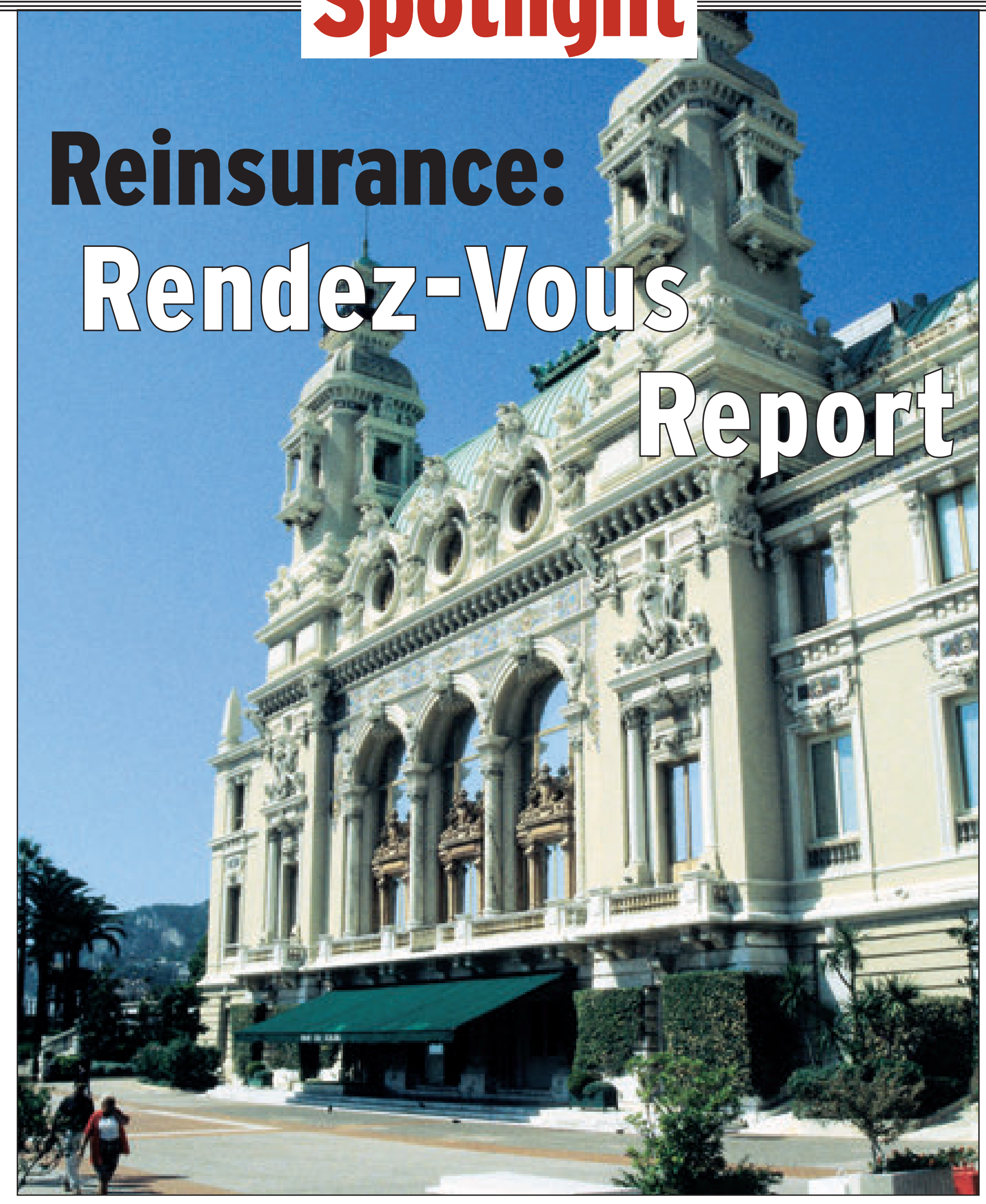

Investor scrutiny reducing demand for ART

By PAUL WINSTON
and GAVIN SOUTER

MONTE CARLO, Monaco—Regulatory and accounting changes that followed the collapse of Enron Corp. last year are having a huge impact on the alternative risk transfer market.

Financial reinsurance remains available but is seeing less interest from ceding companies as an alternative to higher priced traditional reinsurance.

This reflects buyer concern that such coverage would be subject to more intense scrutiny from investors, auditors and regulators in the wake of recent accounting scandals and regulatory inquiries into whether such products obfuscate the true financial health of some companies.

While some reinsurance companies report continued strong interest in structured reinsurance products, such as finite risk reinsurance, it often is being written with more underwriting risk to satisfy those concerns. Lower investment returns also make the programs less competitive.

> **'There is still a role for financial and finite reinsurance, but interest has waned. Buyers are leery of the 'explanation risk' associated with these deals, and auditors will be nervous.'**
>
> *Dirk Lohmann*
> *Converium Ltd.*

At least one financial reinsurance specialist, Max Re Capital Ltd., is adjusting its strategy in light of the current environment for financial products (see story, page 22).

"There is still a role for financial and finite reinsurance, but interest has waned. Buyers are leery of the 'explanation risk' associated with these deals, and auditors will be nervous," said Dirk Lohmann, chief executive officer of Converium Ltd. of Zurich, Switzerland. "These deals likely will increase the amount of underwriting risk they assume relative to funding risk, to avoid any problems," he said.

Less finite risk coverage is being placed, agreed Paul Ingrey, chairman and chief executive officer of Arch Reinsurance Ltd. in Hamilton, Bermuda. "We have not written

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Losses, asset erosion prolong hard market

By GAVIN SOUTER
and PAUL WINSTON

MONTE CARLO, Monaco—Continued poor investment returns and massive recent losses will ensure that reinsurance rates remain firm at least through 2003.

Reinsurers find themselves in one of the most challenging markets in decades, as poor investment returns fail to offset record underwriting losses and inadequate reserves at several companies. This situation is prompting many reinsurers, including the crop of Bermuda startups, to stress underwriting fundamentals.

As firming continues in the reinsurance market, cost increases and coverage restrictions are likely to be passed on to policyholders by ceding companies that have increased their loss exposure through increased retentions.

Those were some of the observations of reinsurance industry executives meeting at the Rendez-Vous de Septembre in Monte Carlo, Monaco, earlier this month. The Rendez-Vous traditionally marks the start of the year-end renewal season.

"I don't believe that there is a single commercial or corporate client or insurance company who doesn't feel the massive impact of what occurred over the past 12 months," said John M. Pelly, chairman and chief executive of reinsurance at Willis Group Ltd. in London.

Rates were increasing before the terrorist attacks of Sept. 11, 2001, but increases were greatly accelerated by the attacks and subsequent events, including several corporate collapses in 2001 and 2002, he said.

"We've seen a lot of claims, increased asbestos reserves, the stock market downturn, poor underwriting in 1998, 1999 and 2000; and with that combination, the insurance industry needs a very good spell of significant underwriting profits," Mr. Pelly said.

"This is the most unsettling time that anyone can remember," said John Berger, president and chief executive officer of Chubb Re in Bernardsville, N.J.

World politics, economic woes, reduced equity returns, insurance losses, reserving problems, years of underpricing and the high expectations of investors all are hitting the insurance industry at once, he said.

While the losses of 2001 continue to push up rates, declining equity markets worldwide have also hit hard in 2002, several reinsurers said.

"The pressure is on reinsurance companies due to the very volatile financial markets. Even though fundamentals have improved, there is still asset impairment. Reserve adjustments are another factor" that will continue to fuel price hikes, said Dirk Lohmann, chief executive officer of Converium Ltd. in Zurich, Switzerland.

Nonequity assets are also a problem, noted

See **MARKET**/page 12

Bermuda startups' discipline keeping prices up

By GAVIN SOUTER
and PAUL WINSTON

MONTE CARLO, Monaco—The influx of new reinsurers formed in Bermuda after the terrorist attacks last year has not yet reduced rates in the reinsurance market.

Representatives of the new Bermuda reinsurers insist that they are underwriting conservatively and not undercutting existing reinsurers. And most of their competitors agree.

And unlike the crop of reinsurers that set up in Bermuda after 1992's Hurricane Andrew to offer property catastrophe reinsurance, the companies established over the past year are offering a broad range of property/casualty coverages.

"The new Bermuda capital has provided only minimal constraints on pricing in the market," said Charles P.T. Cantlay, chairman of marine and energy reinsurance and deputy of the reinsurance board of Aon Ltd. in London. The recent Bermuda startups are run by well-known people with good contacts, he said.

> **'The new companies aren't really more aggressive, despite what one might hear. There will always be cases where they might win an account, but those are anomalies and one-off situations.'**
>
> *Robert Cooney*
> *Max Re Capital Ltd.*

"The general consensus is that the Bermuda startups are not putting enormous pressure on the established market. They have to put that capital to use, but to get the investor returns they desire, they are taking a longer-term view" and not seeking to undercut existing players, said Grace Osborne, director of financial services ratings at New York-based Standard & Poor's Corp.

"The new companies aren't really more aggressive, despite what one might hear. There will always be cases where they might win an account, but those are anomalies and one-off situations," said Robert Cooney, chief executive officer of Max Re Capital Ltd. in Hamilton, Bermuda. "They need to write business, but are being fairly consistent."

Generally, the startups have been disciplined in their underwriting, said James P. Bryce, chief executive officer of IPCRe Ltd. in

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Limited terrorism capacity available, page 21

Max Re modifies its strategy, page 22

Terrorist attacks change views on risk, page 24

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Market: Reinsurance rates to remain firm in 2003

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Dennis Mahoney, chairman of Aon Re Ltd. in London. "Bonds today may be more volatile than equities; defaults are a problem. And governments cutting back on long-term Treasury instruments exacerbates the situation," he said. "Volatility is as bad on the asset side as it is on the liability side."

"We are in a business where returns are declining in two core areas—asset management and reinsurance underwriting. The financial markets react very quickly to change—it is amazing how quickly money can disappear in a short time—whereas reinsurance underwriting changes occur more slowly," said Rudolf Kellenberger, deputy chief executive officer at Swiss Reinsurance Co. in Zurich, Switzerland.

Focus on underwriting

The poor investment environment is forcing reinsurers to underwrite more carefully.

"There is more focus on underwriting profits and less on investments," said James P. Bryce, president and chief executive officer of IPCRe Ltd. in Pembroke, Bermuda.

"In order to service their capital, reinsurers can no longer afford to write risks that produce a high combined ratio," said Michael Handler, the Zurich-based managing director and continental Europe chief executive of New York-based intermediary Guy Carpenter & Co. Inc. "That's no longer acceptable; it has to be under 100%."

Because reinsurers won't be able to offset underwriting losses with investment income, "104% combined is not going to be enough. They should be looking at 90% to be attractive to investors," said Willis' Mr. Pelly.

"The environment on the primary side will be a continuing hard market. (Directors and officers and errors and omissions liability), in particular, will see reduced capacity. One is a function of large losses, the other is due to reduced reinsurance capacity," Mr. Lohmann of Converium said. "In other areas you can get the capacity, but it will remain costly," he said.

While rates will remain high, "year-end renewals will not be as calamitous as last year," Mr. Lohmann predicted.

The rate increases at year end could average in the low double digits, "but the range is going to be quite wide," said Jacques Blondeau, chairman and chief executive officer of SCOR S.A. in Paris.

Complex casualty risks should expect substantial rate increases, but some reinsurance rates appear to have flattened out over the past three months, said Mr. Pelly.

For example, property catastrophe rates for some cedents have seen only small increases, though rates generally have been increasing by anywhere between 10% and 100% for property cat reinsurance so far this year, he said.

On the property side, "the market has stabilized—that does not mean it is flat, but that rates are not increasing or decreasing from current levels—with adequate capacity, and the rationale for pricing is reasonably understood," said Max Taylor, vice chairman of Aon Ltd. in London.

But cedents are unlikely to see any decreases for property cat rates, despite an influx of capacity in the Bermuda market, several executives said.

'In order to service their capital, reinsurers can no longer afford to write risks that produce a high combined ratio. That is no longer acceptable; it has to be under 100%.'

Michael Handler
Guy Carpenter & Co. Inc.

The wide use of computer-based catastrophe models has led to a greater acceptance of technical rates for catastrophe risks. As a result, reinsurers are reluctant to quote below the rates that the cat models calculate.

"If the price is right, you can find 180% of the capacity you need. But if it is 5% below the magic price, then you can only place 40%," said Mr. Handler of Guy Carpenter.

Similar catastrophe exposures are quoted a consistent rate, said Grahame Chilton, chief executive of London-based Benfield Group P.L.C. "There is a technical price that does not allow for supply and demand," he said.

"During the soft market, the modeling of catastrophe risks helped keep pricing in a good condition. As a result, this could be one of the first areas where rate increases begin to slow. Energy and aviation might be other areas where the degree of rate firming starts to slow," said Hans Rohlf, managing director and chief underwriting officer-North America of Hannover Reinsurance Co. of Hannover, Germany.

In addition to hiking prices and adopting more technical approaches to underwriting, many reinsurers say they are turning away significant amounts of business, as well as exiting some lines.

Endurance Specialty Ltd., one of several reinsurers that set up in Bermuda to take advantage of rising

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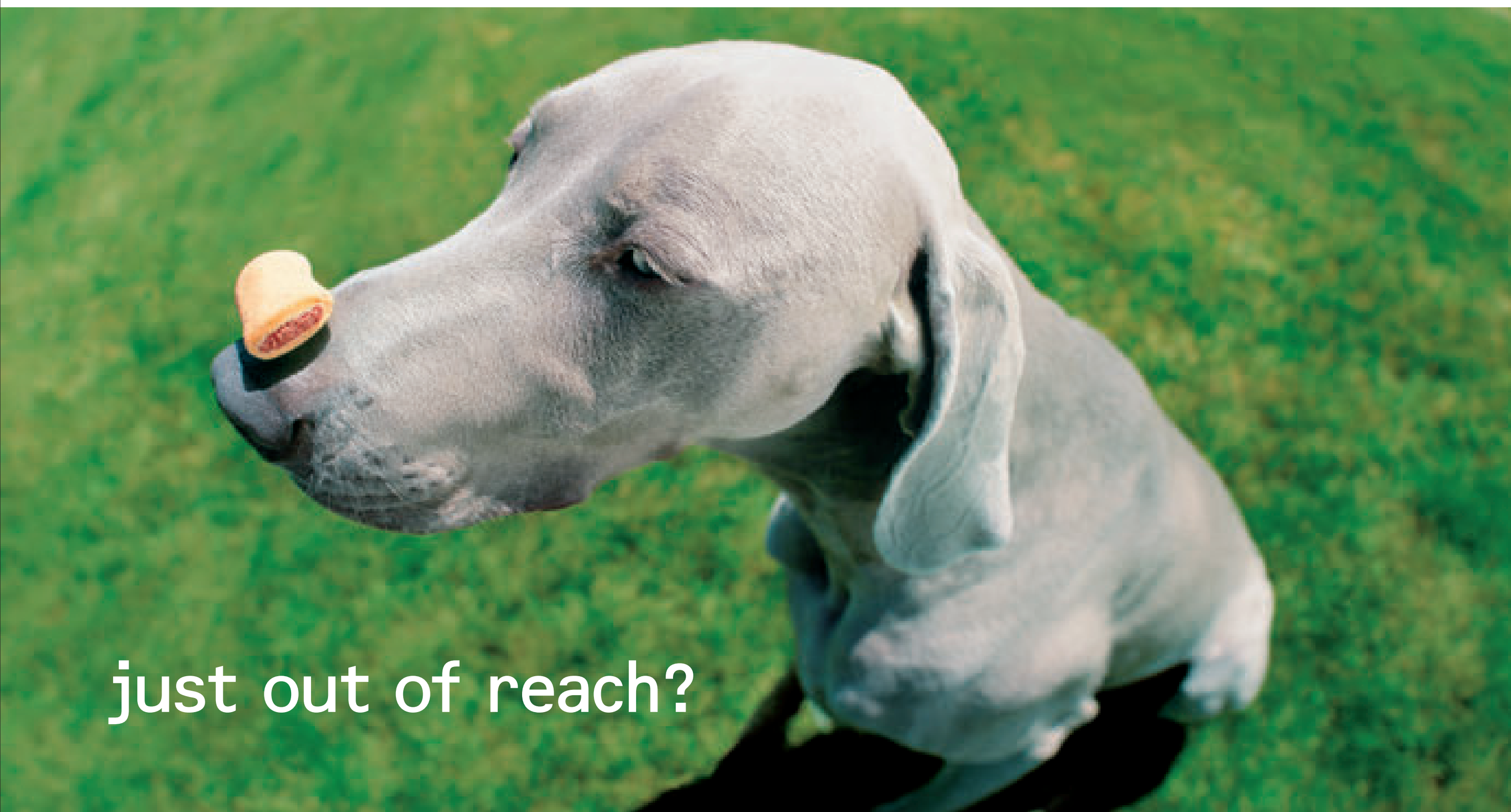

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Market: Reinsurance rates to remain firm in 2003

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rates last year, is declining two-thirds to three-quarters of the submissions that it receives, said Kenneth LeStrange, chief executive officer.

Employers Reinsurance Corp. has not renewed 35% of its book so far this year, said Richard F. Smith, president and CEO, global P&C Re at the Overland Park, Kan.-based reinsurer. "We are serious about underwriting discipline," he said.

This year, ERC has significantly scaled back its D&O writings, as well as program business and national account umbrella coverage, he said. In addition, it has exited the nonstandard auto market.

However, ERC's gross premiums have changed little compared with the same period last year, Mr. Smith said. The company has increased the amount of business it writes for the cedents and lines of business that it has retained, he said.

SCOR S.A. has also withdrawn from program business in the United States, said Mr. Blondeau. In addition, the reinsurer is extremely cautious about credit reinsurance, surety coverage and several casualty lines, he said.

"The legal environment in the U.S. is not improving, and we don't foresee tort reform," Mr. Blondeau said. "D&O rates are going through the roof, but what about the risk? We've got to be very careful about risk selection."

"In the current market, I think there is a reluctance by companies to go after market share. They need to adhere to that discipline," said Grace Osborne, director of financial services ratings with Standard & Poor's Corp. in New York.

"Net premiums written through June barely increased," Ms. Osborne said. "We think this is because less business was being written as ceding companies retained more. This limited growth will affect the rate at which reinsurers can improve their position," she said.

But the rising prices are also prompting some reinsurers to go back to business they had previously exited. XL Re Ltd., for example, will likely return to writing more specialty casualty business at year end, because prices are increasing significantly, said Henry C.V. Keeling, chief executive officer of XL Re in London. "There are some really good opportunities in that area, because it is an area where there is a shortage of capacity and talent."

And other specialty lines, such as credit reinsurance, also are presenting opportunities, said Michael E. Satz, chairman and chief executive officer of American Capital Access, a New York-based credit reinsurer. The economic downturn and revelations about corporate fraud over the past year have increased demand for credit reinsurance, he said.

Changing conditions

As a result of the challenging market conditions, the scope of reinsurance coverage is being reduced.

In the current hard market, "one tends to talk about rate increases only, but it is also important to note that coverage has been reduced—and extensions of coverage are given in a more limited way and only at an appropriate price," said Mr. Kellenberger of Swiss Re.

"We also have to be much more aware when we give coverage that proper definitions are in place. The (terrorist attacks have) shown what can happen and that these risks are difficult to price, they are unexpected and rare," he said.

In the current hard market, 'one tends to talk about rate increases only, but it is also important to note that coverage has been reduced.'

Rudolf Kellenberger
Swiss Reinsurance Co.

Although rates were the main negotiating point during the Jan. 1, 2002, renewals, current discussions are focused more on conditions and the scope of coverage that reinsurers are willing to offer, said Nikolaus von Bomhard, member of the board of management at Munich Reinsurance Co. in Munich, Germany.

Reinsurers have become reluctant to offer all-risk coverage with exclusions, he said. Instead, the coverage is offered on a named-peril basis, and limits are being applied.

And this approach is being used for both nonproportional business and proportional treaties, whereas the latter traditionally offered broad coverage to cedents, Mr. von Bomhard said.

Reductions in coverage terms are part of a fundamental change that should perpetuate the hard reinsurance market at least through 2004, he said.

Investors in reinsurers are more knowledgeable about reinsurance than they were previously, and there is a limited amount of capital that is prepared to invest in volatile businesses, Mr. von Bomhard said. As a result, the period of high prices will last longer, and when prices do go down, they will not fall as sharply as in previous cycles, he said.

The hard market should last at least through 2004, said Robert

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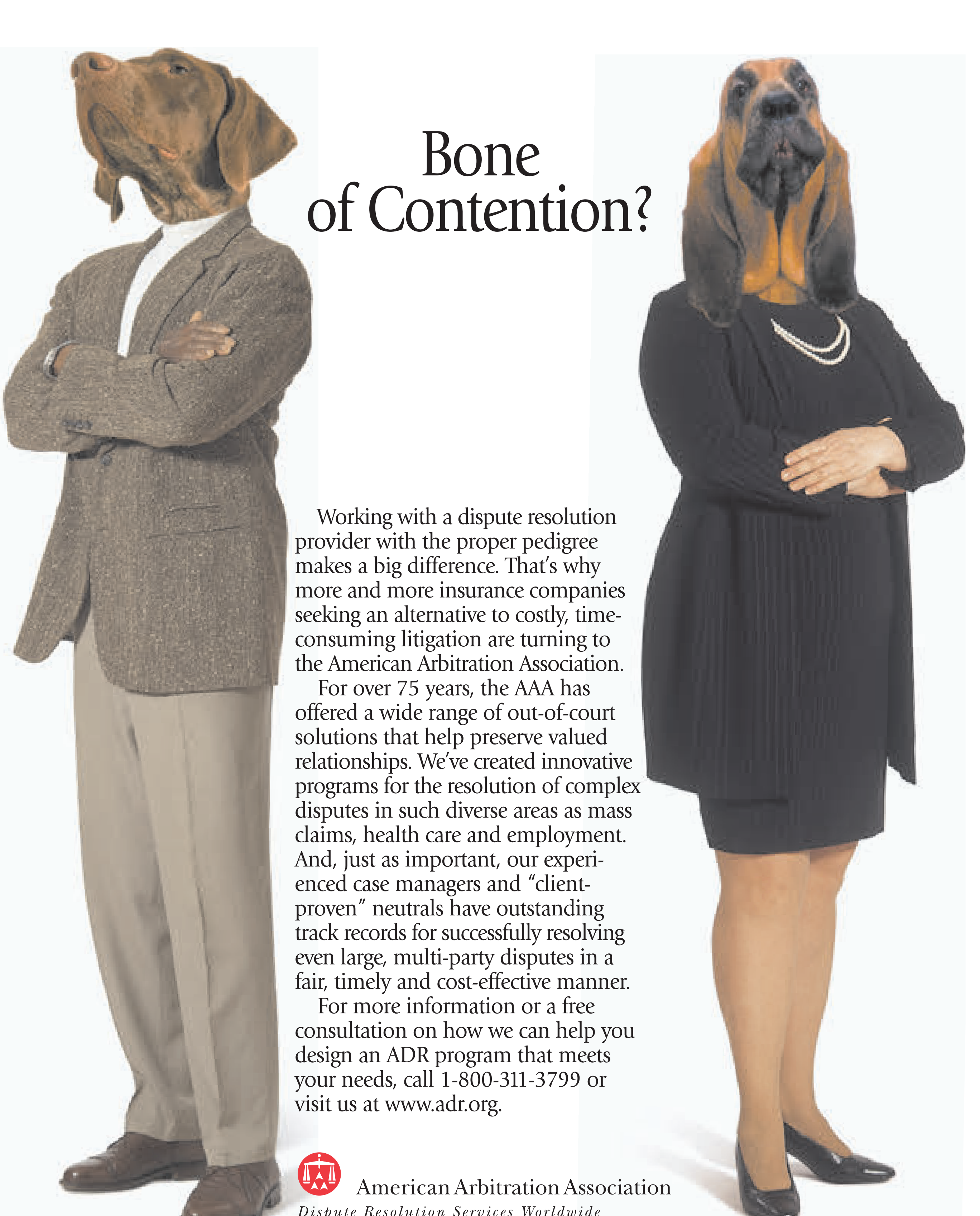

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Cooney, chief executive officer of Max Re Ltd. of Hamilton, Bermuda. "Companies have not reserved enough. Many of the 1990s accident years have not fully developed and will still produce losses in future calendar years," he said. "Also, the investment climate is more challenging than it has ever been."

"As a consequence, more difficult casualty lines will see less appetite for the business, and it will cost more," Mr. Cooney said.

"In the 1990s, the market was driven for years by meeting the client's needs; now, it is driven by shareholders," said Aon's Mr. Taylor.

"I expect that hardening rates will continue for a while in casualty, beyond 2003. This is because all sorts of factors are coming together at once, such as losses on D&O and (medical malpractice), as well as reserving issues," said Mr. Rohlf of Hannover Re. "D&O seems to be seeing the most drastic rate increases, and not all D&O risks will get placed," he said.

Restructuring

The tightening market will lead to further consolidation and restructuring among reinsurers, several executives said.

"More marginal players are likely to exit the market. Also, you will continue to see conglomerates still looking to exit reinsurance by selling off their operations, spinning them off or closing them down," said Converium's Mr. Lohmann. Converium was spun off from Zurich Financial Services Group last year.

"If the bearish financial markets continue, we will see additional consolidation," said Swiss Re's Mr. Kellenberger.

But financial difficulty is not the only factor driving such activity.

"The consolidation that occurred previously was often done to fill geographic gaps, with Europeans buying U.S. companies and vice versa. I'm not sure there are too many holes left to fill on that basis, so consolidation will be done to add specialties and niches," Aon's Mr. Taylor said.

"Already, there is an expectation that consolidation will occur among the new companies in Bermuda, as happened with the last round of new formations in the 1990s," he added.

But the new capital in Bermuda also signals that there still are investors that are interested in insurers and reinsurers, said Mr. Berger at Chubb Re. "As soon as someone leaves, there is someone else with their nose pressed against the window waiting to come in."

And while new reinsurers are forming to take advantage of rising rates, some existing reinsurers are restructuring during the hard market.

AXA S.A. is currently unraveling its AXA Corporate Solutions unit, which was formed in August 2000 and comprises the former operations of AXA Re, AXA Global Risks and AXA's reinsurance buying arm, AXA Cessions.

'Already, there is an expectation that consolidation will occur among the new companies in Bermuda, as happened with the last round of new formations in the 1990s.'

Max Taylor
Aon Ltd.

Now, ACS will handle only large commercial business, the parent company will buy the group's reinsurance and AXA Re has been reformed as an independent company, headed by Philippe Donnet. AXA Re's former head, Jean-Marie Nessi, is forming a new reinsurer in Bermuda (see story, page 10).

"We want to get back to the historical strengths of AXA Re," Mr. Donnet said. "When we put ACS together, it was a good idea, but now, the world of reinsurance and insurance is very different. There remain synergies between reinsurance and insurance for large corporate risks, but we don't feel that you need to have common functions."

Capital

In light of continued hard market conditions, many ceding companies are favoring established, highly rated reinsurers, some observers note.

"Companies are demanding top-rated reinsurers, because significant bad debt from reinsurance on a balance sheet is not something any management will accept," said Charles P.T. Cantlay, chairman of marine and energy reinsurance and deputy chairman of the reinsurance board at Aon Ltd. in London. "We struggle to get anyone to accept less than A- rated companies; most demand at least an A."

"There is more appreciation of capital," said Mr. Bryce of IPCRe.

The losses over the past year have made cedents more aware of the potential for huge catastrophic losses that affect all lines of business, he said. Consequently, most cedents are looking for reinsurers with at least $1 billion in capital. "There are many things that are important, but the biggest thing is capital. That is the No. 1 thing that you can't live without," Mr. Bryce said.

First STate management
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Bermuda: Startups keeping discipline on pricing

Continued from page 10

Pembroke, Bermuda. IPCRe, which was established in 1993, underwrites property catastrophe business for one of the new reinsurers, Allied World Assurance Co. Ltd.

And the new reinsurers are more highly capitalized and are writing a more diverse book of business than those that established after Hurricane Andrew, he said. However, the players that remain from the 1993 class of Bermuda reinsurers have increased their capital and, in several cases, expanded their lines of business, he noted.

"After Andrew, the critical issue was the availability of property catastrophe capacity.... The difference now is that a lot more capital has been taken out of the market, and there is a lot more need for insurance and reinsurance. And the new markets are satisfying those demands," Mr. Bryce said.

Arch Reinsurance Ltd., which was established in Bermuda last October, has written about $800 million in business so far in 2002.

Arch is writing only about half of the property catastrophe reinsurance business that it expected to, and its largest single line of business is directors and officers liability reinsurance, which accounts for 10% of its book, said Paul B. Ingrey, chairman and chief executive officer of the Hamilton-based company.

"We're seeing rates go up in multiples" for D&O coverage, he said. But established property catastrophe reinsurers are maintaining much of their business, Mr. Ingrey said, noting that because most reinsurers use similar catastrophe models, there is little variation in the technical rates.

Arch intends to select a few "pockets" of business where it can underwrite profitably and hold its prices even if competitors offer lower rates, he said. "We want to be like an excess and surplus company but in reinsurance," he said.

Another Hamilton-based startup, Endurance Specialty Insurance Ltd., has written about $570 million in gross premiums so far in 2002, said Kenneth J. LeStrange, chief executive officer.

But the market has not been what Endurance executives expected when the reinsurer was established late last year, he said. The market for property catastrophe reinsurance "was much more stable than we expected."

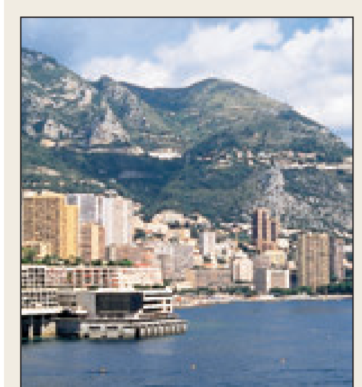
And excess casualty and D&O rates were still lower than they needed to be in the first half of the year, Mr. LeStrange said. "We've seen them increasing at (July 1 renewals), but I still think they have a ways to go."

Endurance is writing an array of property/casualty reinsurance, including property catastrophe, excess liability, excess workers compensation, D&O, property risk excess and alternative risk transfer products, Mr. LeStrange said.

In addition, Endurance is establishing onshore subsidiaries in London and New York. The Bermuda company will focus on high-severity, low-frequency business, and the onshore units will concentrate on business that generates more frequent claims, Mr. LeStrange said.

Another reinsurer was setting up in Bermuda during the Rendez-Vous de Septembre. D'Artagnan Holding Ltd. will be headed by former AXA S.A. executives, including Jean-Marie Nessi and Jean-Pierre Benoit.

Messrs. Nessi and Benoit were unavailable for comment, but sources say the executives are working on raising more than $700 million to capitalize the new reinsurer, which will likely have offices in Bermuda and Paris.



Attendance flat at conference

MONTE CARLO, Monaco—Attendance at the 46th annual Rendez-Vous de Septembre was flat, though attendance by U.S. participants was down 15% compared with a year ago, according to official figures.

The annual gathering of the reinsurance industry, Sept. 7-11 in Monte Carlo, attracted 2,200 participants from 78 countries, according to organizers. Of those, 168 people were from the United States, down 15 from a year earlier. The terrorist attacks of last Sept. 11 occurred during the 2001 Rendez-Vous.

Next year's meeting is scheduled for Sept. 6-11; registration must be completed before June 30, 2003.

For more information on the 2003 Rendez-Vous, visit *www.rvs-monte-carlo.com.fl*

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ART: Accounting scandals depressing deal activity

Continued from page 10

as much as we thought we would," he said.

Cedents are becoming more sensitive about the accounting concerns regarding finite risk coverage, and reinsurers have suffered more losses from finite risk contracts than they had previously thought possible, Mr. Ingrey said.

"There's are lot more risk in these products than people thought there was," he said.

The increased scrutiny of accounting practices is hampering finite risk reinsurance, said John Berger, president and chief executive officer of Chubb Re in Bernardsville, N.J.

"With the accounting environment, it's getting tougher and tougher to do these transactions," he said. "There are legitimate transactions that are being done, but there are a lot that would have passed muster two years ago, but when you take the same deal to an auditor today, they say 'No.'"

Over the past year, Chubb Re has shifted its focus from finite and nontraditional reinsurance to traditional reinsurance, Mr. Berger said.

"There are more opportunities in traditional reinsurance now," he said.

Increasingly, risks that were previously covered by finite risk coverage and other alternative risk transfer products are being placed in the traditional reinsurance market, said Grahame Chilton, chief executive of London-based Benfield Grieg Group P.L.C.

"With all of those transactions, an important part of the deal is legal and audit sign-off," he said.

But, finite and financial reinsurance deals still are being completed.

"The hardening market still drives interest in financial reinsurance. Without Enron issues, we would see even more interest in these kinds of products," said Hans Rohlf, managing director and chief underwriting officer-North America for Hannover Reinsurance Co. of Hannover, Germany.

"Alternative risk transfer vehicles and capital markets do not present a challenge to traditional insurance. Post Worldcom/Enron, there is tougher regulatory scrutiny of such deals. Even so, we'll still support these as alternatives for clients, but they are not taking away the dominant position of the traditional market," said Charles P.T. Cantlay, chairman of marine and energy reinsurance and deputy chairman of the reinsurance board of Aon Ltd. in London.

"There is generally a recognition that the tried-and-true means of risk transfer work. We continue to support and develop alternatives, where needed, but traditional reinsurance remains viable. Ultimately, there is room for all," said Max Taylor, deputy chairman of Aon Ltd.

Terrorism reinsurance available—for the right price

By GAVIN SOUTER and PAUL WINSTON

MONTE CARLO, Monaco—Reinsurers are still unwilling to offer comprehensive coverage for terrorism exposures, but, for a price, several are offering limited capacity for such risks.

The recent introduction of computer-based terrorism models, a modified approach to underwriting the coverage and the high price charged has encouraged some reinsurers to offer stand-alone coverage.

Still, no reinsurers are prepared to broadly include terrorism coverage as part of a standard reinsurance program in the way they did before the Sept. 11, 2001, attacks. And several reinsurers continue to regard terrorism risks as unquantifiable and uninsurable.

Arch Reinsurance Ltd. does offer some terrorism capacity, said Dwight R. Evans, president of the Hamilton, Bermuda-based startup.

"Our normal maximum line is $10 million on any one layer on any one program," he said, though Arch sometimes offers additional capacity, depending on the risk.

Although techniques for underwriting terrorism coverage are still developing, reinsurers are attempting to use a technical approach, he said. For example, reinsurers are using catastrophe models to examine exposures in a quarter-mile radius, Mr. Evans said.

"But I don't think anyone knows what the technical price is," he said.

XL Re Ltd. also offers a limited amount of stand-alone terrorism coverage, but it excludes the risk from its other coverages, said Henry C.V. Keeling, chief executive officer in London.

"We've seen people come into the market, and we've supported them when the price was reasonable," he said.

The reinsurance market is starting to offer some terrorism coverage for property and workers compensation risks, said Hans Rohlf, managing director and chief underwriting officer-North America at Hannover Reinsurance Co. of Hannover, Germany.

"These large placements get done, but at a sizable price," he said. "As a new line of business, terrorism coverage offers the underwriter diversification and a new source of premium...because the risk no longer should be bundled without charging for it," Mr. Rohlf said.

Many commercial policyholders and cedents are considering buying stand-alone coverage, though they often are deterred by the high price, said Grahame Chilton, chief executive officer of Benfield Group Ltd. in London.

"They can find the capacity, but they may not like the price," he said.

Employers Reinsurance Corp. is considering offering terrorism coverage for property/casualty risks now that some computer-based models have been developed by catastrophe modeling firms, said Richard F. Smith, president and CEO, Global P&C Re at the Overland Park, Kan.-based reinsurer. One cat modeling company, Risk Management Solutions Inc., introduced a model for terrorism risks last week (see story, page 39).

> **'It is interesting to try and create models for terrorism, but I don't see how you can do that when you don't have historical statistics. It's a useful tool to give you a rough idea, but you can't use it to establish a rate.'**
>
> *Philippe Gaudibert*
> *AXA Corporate Solutions*

"The challenge is, can you price it right?" he said.

Other reinsurers are skeptical about the use of models and remain unwilling to offer the coverage.

"It is interesting to try and create models for terrorism, but I don't see how you can do that when you don't have historical statistics," said Philippe Gaudibert, chief operating officer of AXA Corporate Solutions in Paris. "It's a useful tool to give you a rough idea, but you can't use it to establish a rate."

Insurers and reinsurers can offer some coverage through government-backed pools, but in countries where there is no government backstop in place, such as the United States, it is difficult to offer stand-alone terrorism coverage, said Jacques Blondeau, chairman and chief executive officer of SCOR S.A. in Paris.

"In the U.S., the very little coverage we are giving is to regional companies," he said.

Munich Reinsurance Co. participates in Extremus A.G., the German government-backed terrorism facility announced last month, and has offered limited stand-alone terrorism coverage in several countries that do not have a government-backed program, said Nikolaus von Bomhard, member of the board of management at the Munich, Germany-based reinsurer.

Munich Re offers limits of about 50 million euros ($48.6 million) and includes a 14-day cancellation clause, he said.

The coverage is not offered in the United States, though, Mr. von Bomhard said. "The exposure there is too great," he said.

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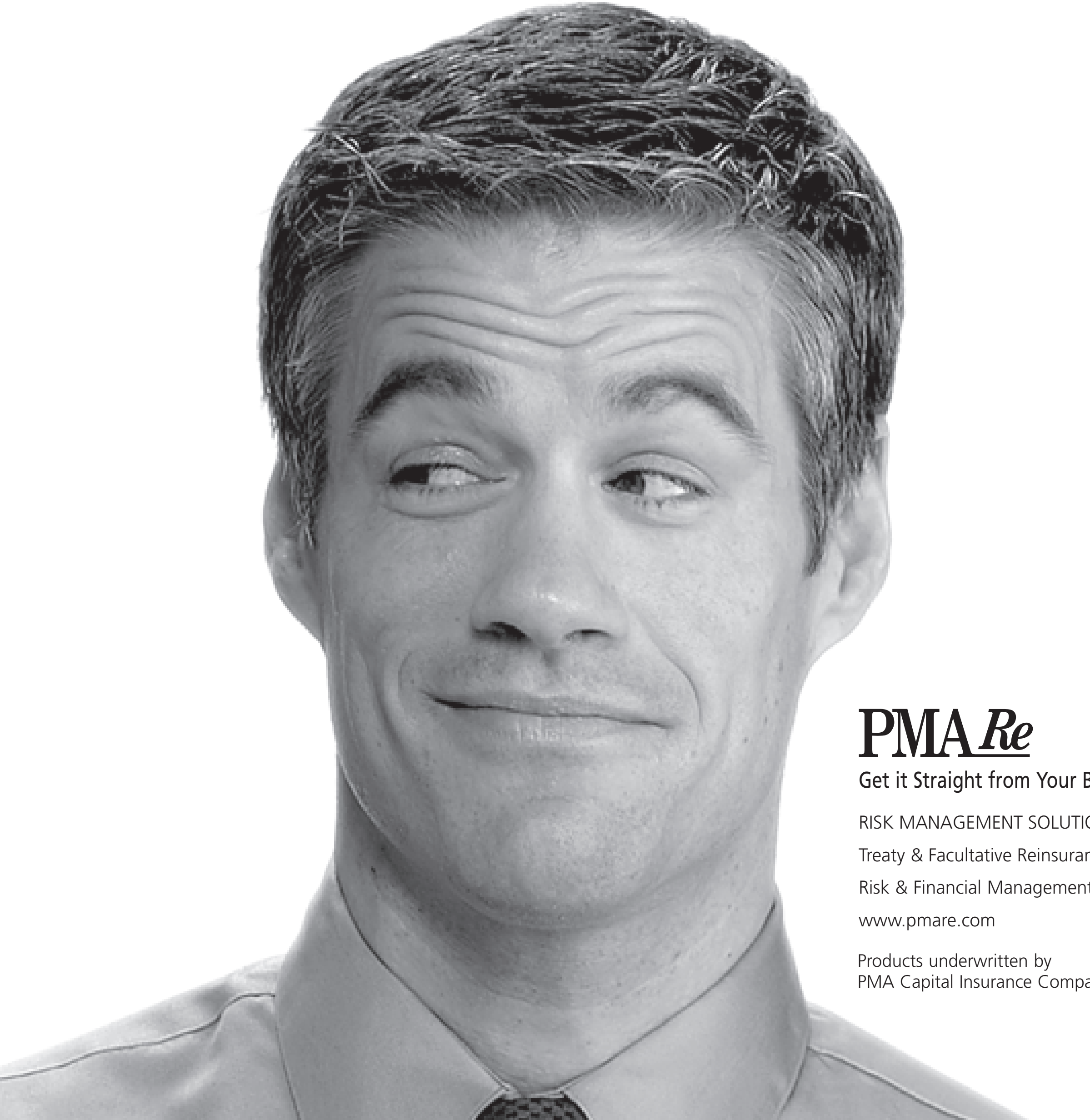

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PHOTO: PAUL D. WINSTON

Monte Carlo's Cafe de Paris remains one of the central meeting places for reinsurance executives attending the Rendez-Vous.

Market change spurs evolution in Max Re business strategy

By PAUL WINSTON

MONTE CARLO, Monaco—As global financial markets remain depressed, a company founded on the premise of maximizing investment returns to generate high returns for itself and its customers is altering its strategy.

Hamilton, Bermuda-based Max Re Capital Ltd. is gearing up to write more traditional reinsurance programs in addition to the structured financial reinsurance programs it first focused on when it formed in 1999. Max Re also aims to target large corporate buyers that may be seeking alternatives to self-insurance in the hard market.

"When Max Re was set up, it was with the idea of matching asset classes and hedge funds to our long-term liabilities," said Chief Executive Officer Robert J. Cooney. Max Re invests a portion of its funds in hedge fund-type investments and shares returns with cedents.

"We aimed for a 103% to 108% combined ratio, with higher returns on investments by investing in bonds and hedge funds to maximize the spread," Mr. Cooney said of the reinsurer's original strategy. "Now, if we fast forward to the current market, we've been successful in the property/casualty business with this model.

"We've written a bit over $1.7 billion over two-and-a-half years of operations. But the return on asset rates we envisioned has not materialized. In the current 5% return environment, the spread business is less attractive."

At the same time, clients still are looking to transfer their risks. To continue to meet their needs, Max Re this year began writing more traditional reinsurance contracts, as the potential returns from underwriting are greater than current investment returns.

"We're counting more on making an underwriting profit, not counting on strong investment gains," Mr. Cooney said.

'We're counting more on making an underwriting profit, not counting on strong investment gains' in the current market.

Robert J. Cooney
Max Re Capital Ltd.

As the reinsurer adjusts its strategy, Max Re's CEO said that the company aims to operate in three key areas:

- Structured business. This comprises financial reinsurance products where the goal is to maximize the spread through asset management.
- Alternative risk transfer products. This business is structured so that the reinsurer assumes significant risk transfer while limiting its ultimate exposure, such as through aggregate loss caps and occurrence limits.
- Traditional risk transfer. This third component is the newest of the trio, and the company aims to add resources—by hiring staff with specialized expertise and underwriting talent—in time to provide more traditional reinsurance coverage at year-end renewals.

"We will try to avoid open-ended risk participations where you can't quantify the risk. The company isn't paid enough to take that kind of risk, and there are many other interesting opportunities without writing that kind of business," Mr. Cooney said.

One of the areas targeted for traditional risk transfer is workers compensation, a line for which the company already has experienced underwriting staff, Mr. Cooney said. Expanding in other areas, such as property excess, might require partnering with someone else, or forming a joint venture with another entity, he said.

Max Re has entered into some

See MAX RE/page 24

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Max Re: Taking traditional turn

Continued from page 22

partnerships already. At the beginning of the year, it acquired a $50 million stake in DaVinci Re Holdings Ltd., a property catastrophe reinsurer managed by Renaissance Underwriting Managers Ltd. in Bermuda.

In May, it purchased a 7.5% stake in Grand Central Re Ltd., a joint venture with Germany's HypoVereinsbank A.G. that is managed by Max Re. Grand Central writes specialty coverage, such as credit derivatives, and provides quota-share retrocessional coverage to Max Re.

Max Re also believes there is a market for its ART products among corporate insurance buyers.

"As the hard market continues, large corporate buyers will look to self-insure more of their risk. They will refuse to pay higher prices. ART structures that offer multiyear protection but cap the ultimate risk transfer are a new opportunity for Max Re to cater to this demand," Mr. Cooney said.

"These kinds of deals are especially suitable in instances where a corporate client might be willing to retain some losses, but also wants some degree of protection. It is less costly than fully self-insuring their exposure," he said.

Mr. Cooney predicted that ART would be an area of growth for the company if traditional insurance coverage remains expensive or becomes even more costly. "Companies will seek alternatives rather than pay the piper," he said.

He said that the shift Max Re is pursuing "is an evolutionary change, not revolutionary. To get the returns on capital needed, one has to make such changes as the environment changes. If the cycle turns, the company is positioned to return to its original model."

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Industry executives, insurance buyers rethinking risk

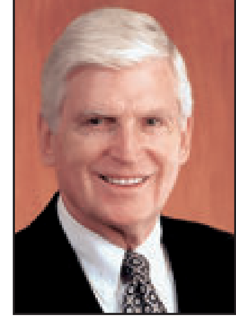
By GAVIN SOUTER

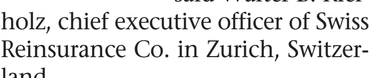
MONTE CARLO, Monaco—The past year has seen a radical reassessment of risk by policyholders, insurers and reinsurers, according to two prominent insurance industry executives.

Insurance buyers have become greatly concerned about exposures they gave little thought to a year ago, and insurers and reinsurers have become much more wary of taking on exposures they believe are difficult to quantify.

As a result, the demand for coverage and the appetite for providing it have shifted significantly.

The terrorist attacks of Sept. 11, 2001, changed everyone's perception of risk, said Patrick G. Ryan, chairman and chief executive officer of Aon Corp. in Chicago. In particular, before the attacks, few policyholders, insurers or reinsurers viewed the risk of losses from terrorist attacks as they do today, Mr. Ryan said during a speech at the formal session of the Rendez-Vous de Septembre in Monte Carlo, Monaco, earlier this month.





The terrorist attacks of Sept. 11, 2001, changed everyone's perception of risk.

Patrick G. Ryan
Aon Corp.

"And none of us know where the capacity to meet that risk will come from," Mr. Ryan said. Currently, there is limited capacity for terrorism, and the rates for stand-alone coverage are extremely high, he said.

But it is not just terrorism coverage that has seen changes, as insurers are generally less willing to cover potentially volatile risks, Mr. Ryan said. Several insurance companies have curbed their reinsurance activities and are concentrating on what they regard as more stable business, such as life insurance, he said.

Many insurers are also reducing their capacity for directors and officers liability insurance and are increasing rates by multiples of the expiring premiums, Mr. Ryan pointed out.

In addition, risks such as brand and reputational risks and Internet-related exposures are becoming increasingly important concerns for policyholders, Mr. Ryan said.

And the troubles for insurers and reinsurers go beyond risk volatility and the large losses in recent years, he said. Plummeting stock prices throughout the world are reducing insurers' and reinsurers' capital and, as a consequence, their ability to take on risks, Mr. Ryan said. This, he said, is forcing some buyers to consider alternatives.

"Our clients are saying, 'We want to transfer more risk, we want to buy more insurance,' but if they can't, then they will use the captive facilities that so many of them have. Sometimes, those premiums never come back," he said.

To address the new conditions in the market, all of the participants in the market must work together, Mr. Ryan said. "It will need a partnership of insurers, reinsurers, brokers, commercial and industrial organizations, and in some places, government," he said.

In particular, governments need to take a lead in changing tort law to reduce the exposure of commercial policyholders and insurers, and they need to play a role in providing some coverage for terrorism risks, Mr. Ryan said.

Insurers and reinsurers do have a lower risk appetite as a result of the huge operating and investment losses they have faced since the terrorist attacks of Sept. 11, 2001, said Walter B. Kielholz, chief executive officer of Swiss Reinsurance Co. in Zurich, Switzerland.

Previously, the insurance industry was focused on the opportunity that risk presented. "We look now at the risk in opportunity, not the opportunity in risks," he said.

"We think about survival as an industry, (as) individual companies, individual underwriters and individual investors," Mr. Kielholz said.

In an attempt to ensure their survival, insurers and reinsurers are "going back to basics," he said. With the reduction in investment income stemming from falling equity values worldwide, companies are focused on underwriting, seeking to lower their combined ratios below 100%, Mr. Kielholz said.

And reinsurers are trying to write more contracts on a nonproportional basis, rather than a proportional basis, in an effort to limit their liabilities, he said.

In addition, reinsurers are reviewing their policy wordings to remove unlimited coverages and to provide only named-peril coverage, Mr. Kielholz said.

And the insurance industry will strive to change its claims management process to try to ensure that it does not pay invalid claims, Mr. Kielholz said.

Previously, insurers and reinsurers had tried to deal with increasing claims costs simply by increasing premiums, he said. "We have to develop a claims-handling concept that's a defensive strategy and is a defense against unjustified claims."

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Group president wants vote by month's end

NAIC proposal calls for product, advertising review

By MEG FLETCHER

NEW ORLEANS—The president of the National Assn. of Insurance Commissioners wants regulators to vote by the end of the month on a proposal that would speed up the introduction of new life and annuity products.

The goal of the proposal is to establish a central clearinghouse to review, using uniform standards, insurers' product filings and advertisements for individual and group life, annuity, disability and long-term care products (*BI*, June 17). The clearinghouse would be created by an interstate compact that would have to be adopted by state legislatures.

The latest draft of the proposal, released Sept. 5, includes several changes, including clarification of the make-up and authority of the management committee.

"We've made tremendous progress on this compact in the past month and have come up with solutions that take into account comments from interested parties as well as insurance regulators," NAIC President Terri Vaughan said at the organization's annual fall meeting, held Sept. 9-12 in New Orleans.

However, several key issues related to the compact proposal continue to divide some industry and consumer representatives.

For example, the Washington-based American Council of Life Insurers is concerned about provisions in the current draft that would make it easier for regulators to opt out of participating in the compact, said Patricia Parachini, senior director in the ACLI's general counsel's office. She noted that the ACLI also is concerned about advertising restrictions and "vague" language about pre-emption that may allow a state to apply its existing standards. Ms. Parachini said she was speaking unofficially, though, as ACLI members had not been able to thoroughly review the new document.

Meanwhile, several representatives of consumer groups voiced their concerns about the inclusion of long-term care insurance in the compact proposal as well as the need to give a consumer groups a significant role in the oversight of the proposed compact commission.

> **'We've made tremendous progress on this compact in the past month and have come up with solutions that take into account comments from interested parties as well as insurance regulators.'**
>
> *Terri Vaughan*
> *National Assn. of Insurance Commissioners*

One consumer representative, though, said he is philosophically opposed to the concept of a compact. With each draft, the NAIC is "still adding more ornaments and lights on a Christmas tree that is on fire," said Kevin Hennosy, executive secretary of Spread the Risk Inc. in Kansas City, Mo., a consumer advocacy group. Mr. Hennosy said he believes the compact to be unworkable, as states will be reluctant to share their authority.

In other action at the NAIC meeting, state insurance regulators:

- Acknowledged the one-year anniversary of the terrorist attacks with an interfaith prayer service. Many at the service wore red, white and blue stars or ribbons that were distributed by the National Council on Compensation Insurance.

  The Boca Raton, Fla.-based NCCI faced employee and public backlash last fall when it temporarily banned the display of the American flag, in keeping with a policy to avoid divisive displays. Then-NCCI President and Chief Executive Officer Bill Schrempf subsequently apologized and rescinded the ban.

- Established a new Market Conditions Working Group to target its monitoring of the most distressed lines of business and to propose regulatory responses. It will operate under the Property/Casualty Insurance Committee.

  The group, which will be headed by Texas Insurance Commissioner Jose Montemayor, plans to study medical malpractice coverage first.

- Approved on the working group level an amendment to the NAIC's privacy model regulation that, if formally adopted by the NAIC, would require insurers to provide "initial, annual and revised notices" about privacy to the employers who purchase their workers compensation policies.

  The change is "a Hobson's choice" for insurers, because the alternative would be for them to provide notice to each individual workers comp claimant covered by employers' policies, said J. Stephen Zielezienski, assistant general counsel with the American Insurance Assn. in Washington.

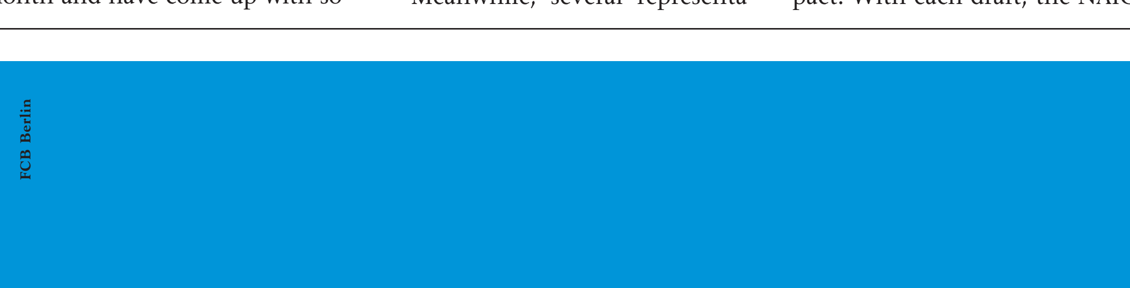
  Insurer representatives generally opposed the change.

  "We think they are going down the wrong course at the wrong time," said David Anderson, vp and assistant director of workers compensation/health for the Alliance of American Insurers in Downers Grove, Ill. Most states have already adopted privacy regulations, and this change may cause some to reconsider the issue, he said.

- Took a 5-4 subgroup vote recommending that the NAIC reduce the number of annual meetings to three from four, by eliminating the spring meeting when many state legislatures are in ending their sessions.

  Regulators are expected to debate the controversial proposal. Some observers fears that such a change might lead to an increase in interim meetings or conference calls, where it is more difficult for industry members to comment. In addition, a few regulators supported holding all meetings at a single site, such as Washington, as a way to increase the organization's stature and efficiency.

  If the NAIC adopts the proposal, such a change could not take place until the spring of 2005, due to previous contract commitments, according to NAIC staff members.



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IUMI 2002

U.N. cargo liability standards slowly taking shape

By DOUGLAS McLEOD

NEW YORK—A United Nations panel is slowly gaining ground in an effort to standardize an increasingly tangled and costly patchwork of international cargo liability laws.

The United Nations Commission on International Trade Law held its latest meeting last week to discuss a draft proposal that would set uniform rules governing liability of shippers, carriers and others for damage to international cargo.

"The UNCITRAL project is not complete, and…there is still a lot of work to be done on the path to a new multimodal convention," said Vincent M. DeOrchis, a partner with DeOrchis, Walker & Corsa in New York.

"However, progress is being made, and it is being motivated by a consensus that there is an obvious need to modernize the world's ocean transport law," he told an audience at the 2002 meeting of the International Union of Marine Insurers last week in New York.

The need for a revised law is rooted partly in complications arising from containerization, where a cargo container may be transferred several times among trucks, trains and ships in multiple countries before delivery.

Existing international conventions haven't kept up with the increasingly complex liability issues that have resulted from changes in cargo transportation, he said.

"The Hague Rules of 1924, the Hague-Visby Rules of 1968, the Hamburg Rules of 1978 and even the Multimodal Transport Convention of 1980 have all failed to provide the necessary guidelines for assessing liability for cargo loss or damage in an era that is now dominated by containerization, multimodal transport" and shipments that involve a growing number of carriers and subcontractors, Mr. DeOrchis said.

> **A carton of watches shipped from Geneva, Switzerland, to Buffalo, N.Y., would today be subject to about 10 different sets of laws during its journey.**
>
> *Vincent M. DeOrchis*
> *DeOrchis, Walker & Corsa*

In response, several nations—including Australia, Canada, China, Germany and Scandinavian countries—have modernized their own domestic laws, but this has only widened differences among the various statutes covering international shipments, Mr. DeOrchis said.

The U.S. Senate has put off action on proposed revisions to the 66-year-old Carriage of Goods by Sea Act pending the outcome of the UNCITRAL project.

UNCITRAL is now developing a final version of a cargo liability convention after receiving a draft version in January from the Comite Maritime International, a group of maritime law associations, he noted.

One of the key issues still being hammered out is the scope of the new law, particularly whether it will cover cargo "door to door"—from point of origin to final destination—or only port to port, as the Hamburg Rules do.

The U.S. Maritime Law Assn. favors a door-to-door approach as the best way to overcome the patchwork of laws that now govern multimodal shipments, Mr. DeOrchis said.

For example, a carton of watches shipped from Geneva, Switzerland, to Buffalo, N.Y., would today be subject to about 10 different sets of laws during its journey, he noted.

"If that cargo is damaged during transport or arrives short, a judge is compelled to determine exactly where the loss or damage took place in order to apply the appropriate law," he said, noting that the different legal regimes impose different burdens of proof, time bars, limitations of liability, defenses and jurisdictional requirements.

At the same time, though, many European countries are concerned that a single door-to-door convention would conflict with existing international agreements, including conventions that now govern truck and rail transportation in Europe, he said.

In the end, UNCITRAL will probably adopt a limited "network" system, in which the UNCITRAL convention would give way to existing international land transport conventions but would supersede national or domestic laws, he said.

Another matter still being debated is the need to widen the definition of cargo carriers to include carriers' subcontractors, such as terminal operators, truckers and railroads. The UNCITRAL draft—which classifies carriers and subcontractors as "performing parties"—would allow a cargo owner to sue the contracting carrier and its subcontractors together, rather than suing only the carrier and creating a string of suits in which each party seeks indemnification from others, he said.

The U.S. Maritime Law Assn. "continues to believe that all of the parties who may be responsible for loss or damage to cargo should be subject to one law—and, if possible, sued in one proceeding—so as to avoid the inefficient and expensive multiplicity of suits that are now spawned by many multimodal carriage losses," said Mr. DeOrchis, a former director of the association.

Another issue still being hammered out is shipper liabilities. The UNCITRAL draft requires a shipper to provide information and instructions the carrier needs to handle a cargo, and UNCITRAL has recognized that shippers must warn carriers when a cargo is hazardous. The current draft provides that carriers may refuse to load goods—and may even unload and destroy goods—that appear likely to become a danger to people, other property or the environment, Mr. DeOrchis noted.

While UNCITRAL has made progress in developing the draft convention, its pace is deliberate, he suggested.

After last week's meeting, UNCITRAL members are next expected to meet in the spring of 2003, and further meetings may follow.

"It is impossible to predict how long the entire process…will take, but there are many who are estimating that the project will be completed within two or three years at most," Mr. DeOrchis said.

Carvill America
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IUMI: Threats loom

Continued from page 3

in its 161 member nations to develop programs similar to CSI.

Another U.S. Customs program begun this year is dubbed Customs-Trade Partnership Against Terrorism. To participate, carriers, freight forwarders, importers and others must meet security requirements, including:

- A self-assessment, following C-TPAT guidelines, of such areas as physical security of buildings and storage areas; personnel screening procedures and background checks; and employee security training.
- Developing and implementing a program to enhance security.
- Forwarding C-TPAT guidelines to other companies in the supply chain and encouraging their use.

Benefits to participants include fewer customs inspections and streamlined billing.

"The key theme to these initiatives is pushing out the borders," Capt. Helming said. "If there actually is a weapon in that (container), it's probably too late to begin searching for it once it's arrived in the U.S."

The London-based International Maritime Organization, meanwhile, is preparing a set of security requirements included in a proposed International Ship and Port Facility Security Code, parts of which will become mandatory worldwide through amendments to the Safety of Life at Sea Convention.

Among other things, the code would create three security levels representing normal, medium and high threat situations, along with procedures that ships and ports must follow for each level.

The code would also require shipping companies to appoint security officers; outline steps to be taken at each of the three security levels; and maintain a record of each vessel's identification, ownership, registration and classification, according to the IMO.

Despite these steps, the array of terrorist threats has rattled a London war risk insurance market that was already "pretty jittery" before the Sept. 11 attacks, said Christine Dandridge, the lead underwriter with Atrium Underwriting P.L.C. syndicate 609 at Lloyd's of London.

War risk insurers are concerned not only about further Al Qaeda attacks, but also about the possibility of war in Iraq, with potential Iraqi missile attacks on regional ports; tensions between India and Pakistan leading to a naval blockade of Karachi, Pakistan; and cruise ships as potential terrorist targets.

War risk underwriters have already developed and amended exclusion for radioactive contamination and are in the process of producing new exclusions for biological and chemical attacks, she said.

IUMI gathering attracts 450 to New York

NEW YORK—A year after the Sept. 11, 2001, terrorist attacks, the International Union of Marine Insurers conference drew about 450 participants from around the world to New York City.

Attendance at this year's meeting, held Sept. 15-18, was up from last year's conference in Genoa, Italy, when the attacks caused many last-minute cancellations.

The 2003 International Union of Marine Insurers conference is scheduled to take place Sept 14-18 in Seville, Spain. For more information, visit IUMI's Web site at *www.iumi.com*.

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IUMI 2002

Deeper water means greater risks for oil drillers

By DOUGLAS McLEOD

NEW YORK—Offshore oil and gas drilling is moving to progressively deeper water, and deepwater operations are creating new and greater risks for drillers and their insurers, a panel of experts says.

While only 28% of oil and gas production on the U.S. outer continental shelf five years ago was in water deeper than 2,600 feet, that share is expected to rise to 69% by 2007, said Larry H. Flak, a senior blowout adviser with well control specialist Boots & Coots Group in Houston.

Deepwater wells are bringing a variety of potentially disastrous problems, though, including so-called "shallow water flow" and underground blowout risks, Mr. Flak told an audience at the 2002 meeting of the International Union of Marine Insurance in New York.

Shallow water flow occurs when high-pressure water in sand layers under the ocean floor flows into a wellbore, eroding the sides of the hole and potentially causing a collapse of the casing that lines the well.

The risk is especially high in the Gulf of Mexico, where about 70% of drilling projects have had to deal with shallow water flow, Mr. Flak said.

Since the first known occurrence in 1985, drillers have spent $30.6 million preventing shallow water flows and $137 million remediating flows at deepwater wells in the Gulf of Mexico, he said.

"It's not an unexpected problem," he observed, adding that for this reason it should probably not be insurable.

Underground blowouts occur when oil or gas in a high-pressure reservoir flows uncontrolled through a wellbore into a lower-pressure reservoir, an event that can cause the well to be "bridged," or crushed, he said.

To date, Boots & Coots has handled seven underground blowouts in deepwater gas wells, including one that involved a failure of a blowout preventer, a valve that is designed to seal the well and that is attached to the wellhead on the sea floor.

These seven blowouts cost drillers a total of $40 million, though only two of the seven resulted in insurance claims, with drillers bearing all losses in the other five.

Big energy companies have shouldered the burden of many of their deepwater drilling losses so far, Mr. Flak said. As smaller drillers move into deep water, though, hugely expensive blowout claims are likely to become more common, he warned.

No deepwater oil well blowouts have occurred yet, Mr. Flak added, but a sustained blowout of this type could easily cost more than $100 million to control.

"You've got to find a way to reduce your exposure on these underground blowout claims—if you can't exclude them, then at least mitigate them," he advised underwriters.

Worldwide, there are now 89 deepwater oil and gas production platforms operating in water 3,500 feet or deeper, comprising 62 semisubmersible rigs that float on pontoons and 27 drilling ships, according to Kevin Jarman, London-based group managing director with Matthews-Daniel, a risk assessment and loss adjusting firm.

Insurers face an array of increasingly costly risks on these facilities, Mr. Jarman observed.

One is the high cost of the rigs themselves and related equipment. Deepwater rigs can range in value from $300 million to $600 million, he noted, while individual pieces of equipment such as a blowout preventer can cost as much as $10 million.

While most rigs have mooring systems to secure them during storms, most also rely on "dynamic positioning systems," computerized engine-control systems designed to keep the rig stationary over wellheads several thousand feet below.

A computer glitch in such a system could cause a rig to drift, breaking the riser that connects the rig to the well's blowout preventer, he said.

Strong undersea currents can also tear the riser away from the wellhead or cause a driller to disconnect the riser intentionally to avoid damage, Mr. Flak said. Reconnecting the riser can be very difficult in deep water, where divers can't be used, he added.

Deepwater locations also make it difficult, if not impossible, to recover lost or damaged equipment on the sea bed, Mr. Jarman noted. The more remote the location, the more expensive it becomes to deliver well-control supplies and replacement equipment.

In addition, the components of deepwater rigs are typically made to order rather than off-the-shelf products, meaning that replacement parts take time to manufacture and can create expensive delays in restoring production, he said.

Finally, deepwater drilling often involves new and relatively untested technology, increasing the unpredictability of results for underwriters, Mr. Jarman suggested.

PHOTO: ZUMA

Deepwater oil wells present greater risks than their shallow water counterparts.

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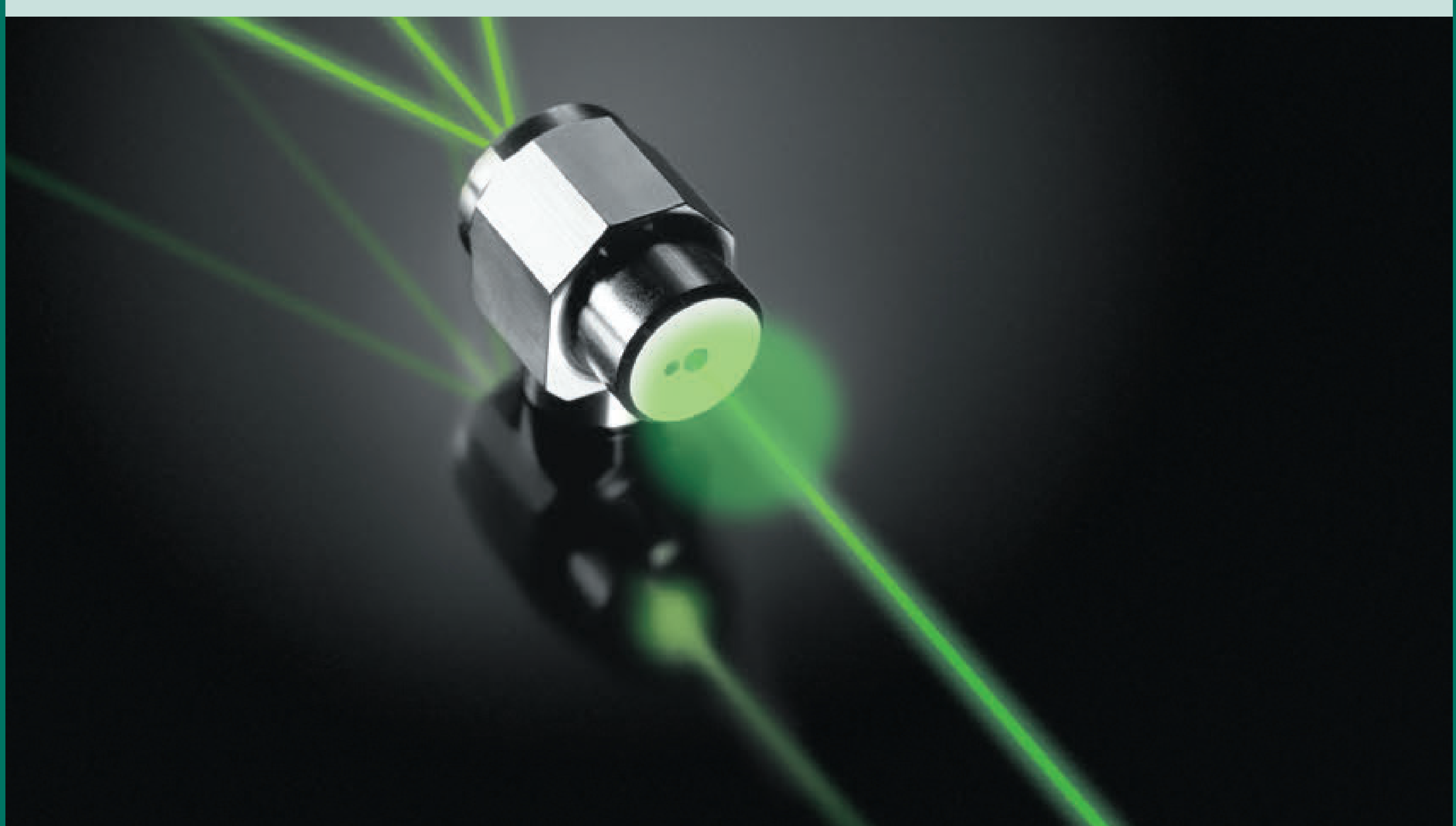

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Comings & Goings

Insurers:

James D. Engel has been named executive vp, customer services at Zurich North America. He will be responsible for the claims and risk engineering operations of the Schaumburg, Ill.-based unit of Zurich Financial Services Group. Previously, he was executive vp of ACE USA and president of Brandywine Holdings.

Steve Ward has been named executive vp, commercial division of Royal & SunAlliance USA. He formerly was senior vp for the manufacturing business group of the Farmington, Conn.-based insurer, which is a unit of Royal & SunAlliance Insurance Group P.L.C.

Mr. Ward

Scott Carmilani has been promoted to senior underwriting officer of Allied World Assurance Co. of Hamilton, Bermuda. He previously was executive vp.

Ken Koreyva and **Sabra Purtill** have joined ACE Ltd. in Hamilton, Bermuda. Mr. Koreyva was named treasurer of ACE, while Ms. Purtill will serve as vp of corporate finance at ACE Asset Management.

Also at ACE, **Dave Brodsky** has been named to head ARM Custom Casualty, the newly created unit of ACE Risk Management that specializes in general and product liability coverage for policyholders with difficult-to-insure exposures. Mr. Brodsky, a senior vp, will be based in New York.

Safety National Casualty Corp. has named **Russell M. Simmons** director of business development. In this newly created position, Mr. Simmons will serve in the underwriting department at the St. Louis-based workers compensation insurer, identifying and developing new business opportunities with insurance brokers nationwide. Mr. Simmons previously served as second vp of Employers Reinsurance Corp., based in Overland Park, Kan.

Agents/Brokers:

Walter Robertson was named president and chief executive officer of Richmond, Va.-based Scott & Stringfellow. Mr. Robertson, who has served as chief operating officer of the brokerage since October 2001, will replace John Sherman, who was named vice chairman.

Karl L. Snearer has been promoted to senior vp and director of brokerage operations at Apex Insurance Agency Inc., a subsidiary of Penn Independent Corp. in Richmond, Va. Mr. Snearer previously was vp of marketing.

Reinsurance:

Hank Sulikowski will assume the role of chief executive officer of Hampton Re Holdings Ltd., replacing **Bill Walker**, who is retiring. Mr. Sulikowski has served as chief operating officer of the Hamilton, Bermuda-based reinsurer.

Other suppliers:

Berkley Risk Administrators Co. L.L.C. has named **Mark C. Tansey** chairman and CEO, while **Kenneth R. Hopkins** has been appointed president and chief operating officer. Previously Mr. Tansey was president and CEO, and Mr. Hopkins was senior vp and COO. BRAC, a unit of W.R. Berkley Corp. in Minneapolis, provides comprehensive risk management services and third-party claims servicing nationwide.

Rafael M. Villalobos Jr. has joined the Philadelphia-based law firm of Christie Pabarue Mortensen & Young as a shareholder. Mr. Villalobos, who has nearly a decade of experience defending medical malpractice cases, was previously with German Gallagher & Murtagh.

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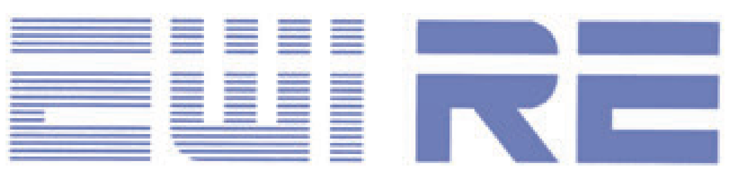

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May you live in interesting times! The insurance industry is certainly in the midst of such times. The events of 9/11/01 have changed the world and dramatically affected the insurance industry. On the heels of that catastrophe came the Enron collapse and ensuing turmoil in the surety, D&O, and professional liability lines of business. On many fronts changes are ongoing and will continue for some time.

The most direct effect of 9/11 is the enormous losses incurred by the insurance industry. It will take years for the full effect of these losses—variously estimated at $60 billion to $80 billion—to be fully recognized by the industry. The hard market in place on 9/11 has been intensified by those losses. How long will this hardening last? Is the new emphasis on quality underwriting just another phase in the cycle, or is it a fundamental shift in how the industry operates? What must the industry do to achieve longer-term stability and profitability?

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Moderator
Paul Winston, Editor, Business Insurance

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CB 09-23-02 A 33 9/20/02 4:04 PM Page 1

Protests belabor pension sponsors

Unions seek to continue defined benefit plans

By SARAH VEYSEY

LONDON—U.K. unions may increasingly call for labor actions to try to prevent employers from closing defined benefit occupational pension plans to new participants, warns the Trades Union Congress.

Last week, U.K. steelmaker Caparo Steel P.L.C. said it would reinstate a defined benefit occupational pension plan following protest strikes by union employees. The series of one-day strikes took place in June at three Caparo plants, after the London-based company announced it would close its defined benefit pension plan to new participants and replace it with a stakeholder pension plan. Stakeholder plans are a type of low-cost pension plan introduced last year that are dependent upon individual savings rather than employer or government contributions.

Following negotiations with the steelworkers' union, the Iron & Steel Trades Confederation, Caparo reached a compromise with workers and agreed to reinstate the defined benefit plan to operate alongside the new stakeholder plan.

The ISTC welcomed Caparo's move. "The agreement that we will be recommending to our members not only delivers a secure pension to ISTC members, but will also reduce their contributions to the final salary scheme by 1% and limit the pension liability of the company in future" by keeping the stakeholder plan open as well, Michael Leahy, general secretary of the London-based union, said in a statement.

The TUC is a vocal opponent of a trend among U.K. employers to close defined benefit plans to new entrants and instead offer defined contribution plans, which the TUC considers less beneficial to workers.

A recent study of 940 employers, conducted by the Confederation of British Industry and Mercer Human Resources Consulting, found that 24% of respondents have closed their defined benefit plans to new participants within the last five years, while a further 12% are considering doing so.

A TUC spokeswoman said the organization welcomed Caparo's decision, and she said that other employers considering closing defined benefit plans could expect similar opposition from union workers.

"We would like to think that unions don't

See **BENEFIT**/next page

PHOTO: NEWSCAST

A U.K. steelmaker recently agreed to reinstate a defined benefit plan after steelworkers had threatened strikes over the plan's closure.

Reinsurers say changes could benefit financial reinsurance market

FSA mulling tougher rules for finite risk

By CAROLYN ALDRED

LONDON—Proposals for tougher U.K. regulation of "financial engineering" by insurers are being welcomed by reinsurers, who contend the new rules could help rather than hinder the market for financial reinsurance products.

Finite risk and other financial reinsurance contracts have come under regulatory scrutiny following the collapse of several insurers—including Independent Insurance Co. Ltd. and HIH Insurance Ltd. (*BI*, Feb. 25). Regulators contend the financial contracts can mask an insurers' true financial condition, while reinsurers defend them as a tool for managing balance sheet risk.

"We absolutely welcome the work" by the U.K. Financial Services Authority, said Clement Booth, a member of the board of Munich Reinsurance Co. in Munich, Germany. He said that a clearer regulatory framework would help the buyers and sellers of finite risk and financial reinsurance.

"The introduction of clear guidelines is good, as long as they are not too prohibitive," said Tom Doran, chief underwriter for Hannover Re Advanced Solutions Ltd. in Dublin.

Mr. Doran pointed out that such contracts already are under much greater scrutiny from accountants, lawyers and regulators, following concerns arising from the collapse of insurers that used the contracts.

Although demand for such business slowed in the first quarter of this year, it since has picked up and "we are seeing a greater number of submissions and inquiries for finite reinsurance," he noted.

A spokesman for Overland Park, Kan.-based GE Employers Re, which writes financial reinsurance for property/casualty and life insurers through its Dublin-based unit, Irish European Reinsurance Co. Ltd., also welcomed the moves by the FSA to "give the business more transparency and clarification and create a level playing field."

The FSA is "doing a great job to clarify the rules for financial reinsurance and we have had constructive and open discussions with them on this issue," said the spokesman.

Reinsurance policies written by IRECO for Independent Insurance helped trigger regulatory concern about the growing use of such policies by cedents.

According to the FSA consultation paper, "im-

See **FINITE**/page 35

PHOTO: AFP

Flash flooding across southern France, including at this stable in Nimes, are resulting in a growing number of insured losses.

Flooding claims rising in France

By EDWIN UNSWORTH

PARIS—Recent flooding in France could cost insurers up to 300 million euros ($291.7 million), according to initial estimates from the French insurer association.

The Paris-based Federation Francaise des Societes d'Assurances said last week that it is too early to provide official figures for the flooding on Sept. 8-9, as many potential claims have not yet been filed. The flooding caused serious damage to parts of southeastern France, killing at least 21 people.

Although most French property insurance policies include flood risks, insurer payouts will be offset by the Caisse Centrale de Reassurance, a government program that reinsures economic losses from natural disasters.

France's largest insurer, Paris-based AXA S.A., said it expects to pay claims of around 75 million euros ($72.9 million) for flood losses. A spokesman emphasized that reimbursement from CCR and other reinsurance would significantly reduce the insurer's net losses.

World Updates

French group urges better loss response

High-risk industrial companies should be required to have a catastrophe management strategy, and insurers should accelerate claims payments to victims of industrial disasters, the French insurance federation says. The Federation Francaise des Societes d'Assurances has proposed several measures to help policyholders and insurance companies better manage the aftermath of large industrial losses. The recommendations were part of an analysis of the Sept. 21, 2001, explosion of a TotalFinaElf petrochemical plant in Toulouse, France.

ZFS says offering fully underwritten

Zurich Financial Services Group said last week that its planned $2.5 billion private stock offering to shareholders has been fully underwritten by a consortium of banks. The Zurich-based insurer said it hopes to complete the rights issue by the end of October, as part of a plan to increase its capital by up to $5 billion. Separately, Zurich Financial Services Group is paying former Chairman and Chief Executive Officer Rolf Hueppi 6.2 million Swiss francs ($4.1 million) in severance compensation, ZFS said. Mr. Hueppi resigned from the Zurich-based insurer in April and was replaced by James Schiro as CEO.

Berkshire deal boosts Trenwick capacity

Trenwick Group Ltd. and Berkshire Hathaway Inc. have entered into an agreement to boost Trenwick's capacity at Lloyd's of London by more than 75% to $512 million for the 2002 year of account. Berkshire Hathaway has agreed to provide $93 million in capacity to Trenwick Managing Agents' composite syndicate 839. In addition, syndicate 839 will benefit from a $119 million quota-share reinsurance deal between Trenwick and Berkshire Hathaway. Both deals have received Lloyd's approval.

Forbes acquires U.K. pension firm

Alexander Forbes Ltd. and its majority-owned consulting actuary unit Lane Clark & Peacock L.L.P. are buying the pension administration business of Schroder Financial Services Ltd. for up to £22.5 million ($34.9 million), the net asset value of the business. The purchase of London-based Schroeder gives Forbes a platform to expand its pension administration business in the

See **WORLD UPDATES**/page 35

Benefit: Plan sponsors facing protests

Continued from previous page

have to resort to strike action," she said, but said that the outcome of the Caparo workers' strike might influence other employers that are considering closing their defined benefit plans. "Employers will maybe see this decision as a warning not to go down the same road as Caparo," she said.

But the effect that the threat of labor actions will have on companies' decisions about their occupational pension plans depends very much on the type of company in question, according to Russell Beaumont, a consultant at Watson Wyatt in London.

Many employers are closing defined benefit pension plans to new-hires in an effort to limit their pension costs, he explained.

"If certain industry sectors really need to cut costs, then industrial action might not have any impact (on their decisions) at all," he said.

"It depends on what sort of influence the workforce has on management," he added. If a company clearly communicates to workers the reasons behind its pension provision decisions, then industrial disputes will more likely be avoided, he said.

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LEGAL NOTICE

UNITED STATES BANKRUPTCY COURT SOUTHERN DISTRICT OF NEW YORK

In re:

Petition of Colin Graham Bird and Paul Anthony Brereton Evans, as Joint Provisional Liquidators of NORTH ATLANTIC INSURANCE COMPANY LIMITED, f/k/a BRITISH NATIONAL LIFE INSURANCE SOCIETY LIMITED and BRITISH NATIONAL INSURANCE COMPANY LIMITED,

a Debtor in a Foreign Proceeding.

Return Date: October 17, 2002
Time: 3:00 p.m.
Objection Deadline:October 7, 2002
5:00 p.m.,

In a Proceeding Under Section 304 of the Bankruptcy Code
Case No. 97-B-41602 (RDD)

NOTICE OF MOTION FOR PERMANENT INJUNCTION PURSUANT TO SECTION 304(b) OF THE BANKRUPTCY CODE

PLEASE TAKE NOTICE that pursuant to an order of the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court"), a hearing will be held on October 17, 2002 at 3:00 p.m., or as soon thereafter as counsel may be heard (the "Return Date"), before the Honorable Robert D. Drain in Courtroom 610 of the Bankruptcy Court which is located at The Alexander Hamilton Custom House, One Bowling Green, New York, New York, 10004, to consider the motion (the "Motion") of the Provisional Liquidators of North Atlantic Insurance Company (the "Company") for entry of an order pursuant to 11 U.S.C. §§ 105(a) and 304(b) granting the Petition in this case and permanent injunctive relief (the "Order") giving full force and effect in the United States to the Scheme of Arrangement (the "Scheme") between the Company and its Scheme Creditors (capitalized terms not defined herein shall have the meaning defined in the Scheme).

The Provisional Liquidators have proposed the Scheme pursuant to section 425 of the Companies Act 1985 of Great Britain. If the requisite statutory majorities of creditors (*i.e.* a majority in number representing 75% in value of those in each class present and voting in person or by proxy) approve the Scheme, a hearing to sanction the Scheme will be held before the High Court of Justice of England and Wales (the "High Court"). The date of the hearing to consider whether to sanction the Scheme has been scheduled for October 16, 2002. If the High Court sanctions the Scheme, the Provisional Liquidators will proceed with their Motion and request entry of the Order that would: (A) grant the Petition in this case, recognize the Scheme Administrators as the exclusive representatives of the Company, and give effect to the Scheme in the United States so that it binds all Scheme Creditors; (B) except as provided expressly in the Scheme or at the express written direction of the Scheme Administrators, permanently enjoin all entities from (i) transferring any property of the Company or property involved in the Scheme, or the proceeds of such property (collectively, the "Related Property") to third parties; (ii) drawing down any letter of credit established on behalf of the Company (a "Letter of Credit"), or withdrawing from, setting off against or otherwise applying property that is the subject of any escrow or trust or similar arrangement (an "Escrow") in which the Company has an interest, in excess of what is expressly authorised by any related agreement; (iii) commencing or continuing any legal action or proceeding (including, without limitation, arbitration or any judicial, quasi-judicial, administrative or regulatory action, proceeding or process whatsoever) (an "Action") involving the Company or the Related Property, or any of the Company's representatives or agents (the "Agents") or any of their property, or seeking discovery against the Company; (iv) enforcing any judgment, assessment, order or award, or commencing or continuing any Action to create, perfect or enforce any lien, set-off or other claim against the Company or the Related Property, or any of the Agents or any of their property; (v) enforcing any statute, rule or requirement of federal, state, or local law or regulation (a "Security Requirement") requiring the Company, or any of the Agents to establish security of any kind as a condition of prosecuting, defending or appealing any Action and such Security Requirement will be rendered null and void for such Actions but the Order shall not affect any security in existence at the Effective Date or its replacement; (vi) commencing or continuing any Action against the Company, the Provisional Liquidators, the members of the Informal Creditors' Committee or any of their respective directors, officers, agents, employees, representatives, financial advisers or attorneys (the "Pre-Scheme Parties") or any of them with respect to any claim or cause of action in law or in equity, arising out of or relating to any action taken or omitted to be taken as of the Effective Date by any of the Pre-Scheme Parties in connection with the section 304 case or in preparing, disseminating, applying for or implementing the Scheme or the Order; (vii) commencing or continuing any Action against the Scheme Administrators, the Company, the members of the Creditors' Committee, the Scheme Actuary, the Independent Actuary, the Scheme Adjudicator, or any of their respective directors, officers, agents, partners, employees, representatives, financial advisers or attorneys (the "Scheme Parties"), or any of them, with respect to any claim or cause of action, in law or in equity, which may arise out of the construction or interpretation of the Scheme or out of any action taken or omitted to be taken by any of the Scheme Parties in connection with the administration of the Scheme;(C) require (i) all entities in possession, custody or control of property of the Company, or the proceeds thereof, to turn over and account for such property or its proceeds to the Scheme Administrators; (ii) all entities in possession, custody or control of any records of the Company to deliver such records to the Scheme Administrators, and all persons having any records relating to the Company's business or to any matter which may affect the administration of the Company's estate or the Scheme, to preserve them and submit them to the Scheme Administrators for examination; (iii) all entities that are beneficiaries of Letters of Credit, or any parties to any Escrow, to provide notice to the Scheme Administrators and their United States counsel of any drawdown on any Letter of Credit, or any withdrawal from, set-off against, or other application of property that is the subject of any Escrow (any of which, a "Draw"), together with information sufficient to permit the Scheme Administrators to assess the propriety of such Draw, including, without limitation, the date and amount of such Draw and a copy of any agreement pursuant to which such Draw was made and provide such notice and other information contemporaneously therewith; and turn over and account to the Scheme Administrators for all funds resulting from a Draw in excess of the amount expressly authorised by the agreement pursuant to which such Letter of Credit or Escrow was established; (iv) parties to any Action in which a liability of the Company may be established to place the Scheme Administrators and their United States counsel on the master service list of any such Action and ensure that such counsel receives copies of all documents served by the parties to such Action or issued by the tribunal or other official having jurisdiction over such Action and all correspondence circulated to parties named on any service list; and (D) further provide that (i) except as specifically set forth in the Order, nothing in the Order prevents the continuance or commencement of an Action against or involving any party other than the Company but no settlement or judgment in any such Action shall be binding on or enforceable against the Company or the Related Property; (ii) the High Court has exclusive jurisdiction to hear and determine any Action and to settle any dispute relating to the interpretation of the Scheme, or to any action taken or omitted by any of the Scheme Parties in connection with the administration of the Scheme; (iii) the Scheme Administrators are authorized to transfer to the foreign proceedings any property of the Company located in the United States; (iv) the Bankruptcy Court shall retain jurisdiction with respect to the Order, requests for any additional relief in the case and all adversary proceedings in connection therewith; and (v) no action taken by the Provisional Liquidators or the Scheme Administrators, their successors, the Agents, or any of them, or their counsel, in acting in connection with the Scheme, the Order, the section 304 proceeding, any further order for additional relief in the section 304 proceeding, or any adversary proceeding in connection therewith as the Court may make shall be deemed to constitute a waiver of the immunity afforded to the Provisional Liquidators, the Company or the Scheme Administrators, their successors, agents or representatives pursuant to section 306 of the United States Bankruptcy Code.

Copies of the Scheme Document, the Motion, the form of the Proposed Permanent Injunction Order to be presented on the Return Date and the Memorandum of Points and Authorities in Support of the Motion are available to review and download at www.northatlanticinsurance.co.uk, as well as by fax, email or written request to the Provisional Liquidators' counsel at:

Allen & Overy
1221 Avenue of the Americas
New York, New York 10020
(212) 610-6399 (Facsimile)
Attention: Theresa D'Agostino
theresa.d'agostino@allenovery.com

PLEASE TAKE FURTHER NOTICE that objections, if any, to the Motion must be made in writing describing the basis therefor and shall be filed with the Court electronically in accordance with General Order M-182 by registered users of the Court's electronic case filing system, and by all other parties in interest, on a 3.5 inch disc, preferably in Portable Document Format (PDF), Word Perfect or any other Windows-based word processing format, with hard copy to the Chambers of the Honorable Robert D. Drain, and served upon Allen & Overy, 1221 Avenue of the Americas, New York, New York 10020 (Attention: Ken Coleman and Stephen Doody), counsel to the Provisional Liquidators so as to be received on or before October 7, 2002 at 5:00 p.m., New York time.

Dated: New York, New York
September 17, 2002

ALLEN & OVERY
Attorneys for the Provisional Liquidators by:
Ken Coleman (KC 9750)
Stephen Doody (SD 9768)
1221 Avenue of the Americas
New York, New York 10020
(212) 610-6300

LEGAL NOTICE

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

IN THE MATTER OF THE LIQUIDATION)
OF AMERICAN HORIZON INSURANCE COMPANY) 02 CH 12796

NOTICE OF CLAIM FILING DEADLINE AND PROCEDURES

PLEASE TAKE NOTICE, that on July 11, 2002, the Circuit Court of Cook County, Illinois, entered an Agreed Order of Liquidation With a Finding of Insolvency ("Agreed Order of Liquidation") against American Horizon Insurance Company ("American Horizon"). Nathaniel S. Shapo, Director of Insurance of the State of Illinois, is the statutory and court-affirmed Liquidator of American Horizon (the "Liquidator").

TAKE FURTHER NOTICE, that pursuant to the Agreed Order of Liquidation, all rights and liabilities of American Horizon and its policyholders, creditors and stockholders, and all other persons interested in its property or assets, are fixed as of July 11, 2002, unless otherwise provided in subsequent orders of the Court.

TAKE FURTHER NOTICE, that on September 10, 2002, the Circuit Court of Cook County, Illinois, entered an Order Providing for the Filing of Claims and the Setting of Claim Filing Deadlines ("Claim Filing Order"). Pursuant to the Claim Filing Order, all persons, companies or entities who have, or may have claims against American Horizon, its property or assets, or against an American Horizon insured or policyholder, shall have the right to present and file with the Liquidator proper proofs of claim on or before July 11, 2003 at 4:30 p.m. (C.D.T.).

TAKE FURTHER NOTICE, that any insured under an insurance policy issued by American Horizon shall have the right to present and file with the Liquidator a proper proof of claim setting forth a contingent claim on or before July 11, 2003 at 4:30 p.m. (C.D.T.). No contingent claim shall be allowed for purposes of participating in any distribution of estate assets that may be made at the fourth priority level, 215 ILCS 5/205(1)(d), unless such claim has been liquidated and the insured claimant has presented and filed evidence of payment of such claim to the Liquidator on or before July 12, 2004 at 4:30 p.m. (C.D.T.). Any contingent claim for which a proper proof of claim is filed on or before July 11, 2003 at 4:30 p.m. (C.D.T.), but which is not liquidated on or before July 12, 2004 at 4:30 p.m. (C.D.T.), may be estimated pursuant to 215 ILCS 5/209(4)(b) for purposes of participating in any distribution of estate assets that may be made at the fifth priority level, 215 ILCS 5/205(1)(e), unless otherwise directed by the Court.

TAKE FURTHER NOTICE, that the form and required contents of all proofs of claim are described in 215 ILCS 5/209. Proofs of claim, along with supporting documents, if any, are to be filed with, and may be obtained from, the Liquidator of American Horizon, c/o the Office of the Special Deputy Receiver, located at 222 Merchandise Mart Plaza, Suite 1450, Chicago, Illinois 60654. A proof of claim shall be deemed "filed" with the Liquidator upon the Liquidator's receipt thereof. The Liquidator reserves the right to require such additional information with respect to any claim filed with him as he may deem necessary. The Liquidator further reserves any and all defenses available to American Horizon upon all filed claims. All proofs of claim must be duly sworn to before an officer authorized to take oaths.

THE LAST DATE FOR THE FILING OF PROOFS OF CLAIM WITH THE LIQUIDATOR IS SET FORTH ABOVE. NO PERSONS, COMPANIES OR ENTITIES HAVING OR CLAIMING TO HAVE ANY CLAIM AGAINST AMERICAN HORIZON, ITS PROPERTY OR ASSETS, OR AGAINST AN AMERICAN HORIZON INSURED OR POLICYHOLDER, SHALL PARTICIPATE IN ANY DISTRIBUTION OF THE ASSETS OF THE COMPANY UNLESS SUCH CLAIMS ARE PROPERLY FILED WITH THE LIQUIDATOR ON OR BEFORE JULY 11, 2003 AT 4:30 P.M. (C.D.T.)

Cathleen M. Travis
Special Deputy Receiver

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Finite: Proposals welcomed

Continued from page 33

proper use of financial engineering has contributed to the difficulties seen in several insurance companies in the U.K. and overseas."

Financial engineering—which according to the FSA includes financial reinsurance among other instruments—is "used to improve, or sometimes to smooth, reported profits, or to improve the reported balance sheet position," the FSA said. Financial engineering can be a valid method of strengthening a firm's solvency position or accessing surplus "economic reserves," the FSA acknowledged.

However, it added, "concerns arise when its use obscures the underlying financial condition of a firm or is designed to mislead consumers or regulators."

The boundaries between "traditional" and "alternative" reinsurance "are often blurred," the FSA stated. Potential regulatory issues include the application of current accounting rules to these contracts and whether financial reinsurance arrangements are truly risk transfer products or merely funding arrangements, according to the FSA report. "This uncertainty may in some circumstances present scope for obscuring poor results," it stated.

The FSA consultation paper also proposes there should be a clearer presentation of information on financial engineering transactions in insurance regulatory returns.

The FSA has "already begun to strengthen (its) regulatory and supervisory approach to financial engineering, especially concerning the adequacy of management controls. The new reporting requirements should significantly improve supervisors' ability to identify issues relating to individual firms' use of financial engineering and, where necessary, to develop effective risk mitigation programs."

Comments on the FSA consultation paper, No. CP144, should be received by the authority no later than Oct. 31, 2002.

Copies of CP 144: "A new regulatory approach to insurance firms' use of financial engineering" and other consultation documents on insurance regulation can be found on the FSA's web site

Exec predicts losses from financial risks

By CAROLYN ALDRED

The involvement of reinsurers and insurers in increasingly exotic and complex financial risks during the soft market will lead to some large and unexpected losses, a reinsurance executive warns.

Dirk Lohmann, chief executive officer of Zurich, Switzerland-based Converium Ltd., voiced his personal concerns at a breakfast meeting hosted by PricewaterhouseCoopers during the Rendez-Vous de Septembre in Monte Carlo. His comments met with much agreement among reinsurance executives at the meeting, according to a PwC spokesman.

Financial market risks, including "residual value coverage, film financing, credit enhancement business and credit derivative risks from investment banks, have been written by insurers and reinsurers, and not all this business will go very well," Mr. Lohmann told *Business Insurance* last week.

Such losses will disappoint and surprise the investors who are being encouraged to bring new capital into the industry because traditional property and casualty rates are increasing, he added.

Mr. Lohmann said his primary concern is with the "generalists who migrated into this business at the end of a soft market" more than the specialist monoline insurers and reinsurers specializing in financial business.

Some reinsurers last week were eager to downplay their involvement in financial market risks following Mr. Lohmann's remarks.

Clement Booth, a member of the board of Munich Reinsurance Co., said that Munich Re and subsidiary American Re-Insurance Co. have had only limited involvement in credit derivatives and credit enhancement business. What business it did write was "stress-tested to the depression of the 1920s," he added.

Munich Re has always looked at alternative risk transfer and financial and credit reinsurance "very, very cautiously," Mr. Booth said.

See LOSSES/page 36

World Updates

Continued from page 33

United Kingdom.

European floods to hit ACE quarter

Hamilton, Bermuda-based ACE Ltd. said the recent European flooding will reduce its third-quarter operating income by about $90 million after taxes. ACE was exposed to flood claims both directly and as an excess-of-loss reinsurer.

Moody's reviews French P/C market

The French property/casualty insurance industry remains healthy, despite reductions in investment income, according to Moody's Investors Service Inc. Premium growth among French property/casualty insurers outpaced inflation in 2000, 2001 and 2002, the ratings agency said. The French property/casualty market is the third largest in Europe, accounting for gross premiums of 3.6 billion euros ($3.50 billion) in 2001, Moody's notes. But to maintain their strong position, French property/casualty insurers must trim costs, Moody's said.

Kiln posts profit, raises capital

Lloyd's of London company Kiln P.L.C. has announced a £3.5 million pre-tax profit for the first half of 2002. Kiln also announced that it had completed a capital raising exercise of £47.2 million ($73.2 million) for the 2003 underwriting year.

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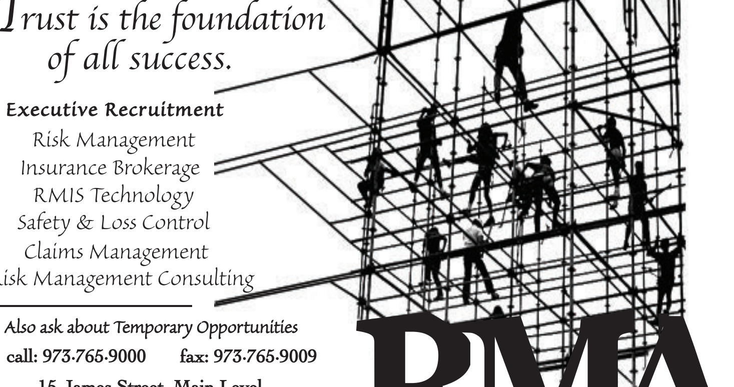

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Losses: Financial reinsurance risky

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However, there has been an attitude in the ART market that the "more complex, the better, and I imagine some of the deals might unwind," he said.

There has been unease for some time among stock analysts about the reinsurance industry's expanded involvement in financial products, and comments from someone in the industry at such a high level as Mr. Lohmann will fuel the concern, said Roger Hill, an analyst with UBS Warburg in London.

The International Monetary Fund recently voiced concerns about the financial market activities of insurance and reinsurance companies in a Global Financial Stability Report published this summer.

"In the 1990s, periods of soft premiums and low bond yields spurred innovations that fostered convergence between insurance and capital markets," such as catastrophe bonds and the development by reinsurers of other alternative risk transfer products, the IMF report stated.

Insurance companies also "sought to diversify their large investment portfolios and funding sources. For example, they became more important participants in credit derivatives markets, helping banks to hedge and diversify their credit exposures," it added.

Uncertainties remain, however, about "whether insurers hold adequate capital against financial risks, whether their management of market risk has kept pace with their involvement in the market, the size and extent of their off-balance sheet activities and the potential migration of financial risks from banking to insurance sectors," the report concluded.

Standard & Poor's Corp. earlier this year relaunched its Financial Enhancement Ratings, which are designed to help investors evaluate the willingness of insurers, as well as their capacity, to make timely payments.

S&P said it first introduced FERs in 2000 because of concerns about the expansion of multiline insurers into guarantee and credit enhancement business and the fact that the "multiline industry, unlike the monoline bond insurers that traditionally dominated this sector, normally delays claims payment pending the resolution of contract disputes."

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Pension: ERISA duties outlined

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ERISA also requires that fiduciaries diversify plan assets unless it is imprudent to do so, bars fiduciaries from making certain prohibited transactions on the part of the plan and requires that fiduciaries act in accordance with plan documents.

"A plan fiduciary has to follow the terms of the plan, and, oddly enough, this is one that really makes people struggle," Mr. Starr said. When questions arise about a plan, he suggested, "The first thing you should do is look and see what the plan says."

Mr. Starr said written investment policy statements can help reduce a fiduciary's liability exposure. "If a question ever comes up about having a bad fund in the plan, you'll want to have something you can go back and look at, something objective so you can say, 'Here's why we did it.'"

Without a documented process for making investment decisions, "That's when you're going to start getting in trouble," he said.

And fiduciaries must be aware that they can be held liable for another fiduciary's breach of ERISA rules, Mr. Starr said. "If you knowingly participate in that breach or if you do something to conceal it, then you're going to be responsible for that," he said. "Especially with what's gone on in the last couple of years, if you know of something going on…you've got to go above and beyond to get that fixed."

'A plan fiduciary has to follow the terms of the plan, and, oddly enough, this is one that really makes people struggle. The first thing you should do is look and see what the plan says.'

R. Eric Starr
INVESCO Retirement Inc.

In the current environment, communication with plan participants is also essential for fiduciaries, Mr. Starr said. "These days, you really want to communicate with the participants," he said. "If you're changing the plan, make sure you explain why you're changing it."

Ultimately, plan fiduciaries generally can steer clear of ERISA violations by creating and following procedures, avoiding conflicts of interest, being consistent and documenting all decisions and the reasons behind them, the lawyer said.

"What you need to do is follow a process. If you follow a process and if you're reasonable about that, you should be fine," Mr. Starr said. "Courts nine times out of 10 aren't going to second-guess the decision a fiduciary made if (the fiduciaries) can document they went through a decision-making process."

Profit Sharing/401(k) Council of America's 55th National Conference

Choice critical in educating better 401(k) plan investors

By RODD ZOLKOS

CHICAGO—While the retirement plan industry has devoted considerable resources to educating plan participants to be better investors, those efforts can't succeed if participants don't have the proper choices, according to one retirement plan expert.

"The participants can only do so much with what they've got to work with," said Ryan L. Bauer, a vp in the retirement plans division of Mutual of Omaha Insurance Co. in Omaha, Neb. And providing a list of fund options alone doesn't necessarily offer choice, he said.

Speaking at the Profit Sharing/401(k) Council of America's 55th National Conference last week in Chicago, Mr. Bauer said surveys suggest only a small percentage of plan participants are knowledgeable about investing. "In an environment where the assets are participant-directed, that has to concern us as an industry," he said.

Meanwhile, surveys also have shown that the typical plan participants use only a handful of available funds in their allocation mix. "It's very difficult to put together a sound portfolio using three choices in most plans," Mr. Bauer said.

"I think education definitely works to get people to participate. It definitely works to get people to put in more money," he said. But investor education efforts have failed to teach participants to be disciplined, strategy-oriented investors, Mr. Bauer said. "Although we've spent a lot of money on education, I think it's time to examine how we're spending that money."

Many plan participants need and want help with their asset allocation decisions, he said. But, while asset allocation funds—which provide a portfolio of assets aimed at meeting the participant's investment goals and risk tolerance—are often included among plan options, many times they are presented to investors as just another "fund," and consequently are being used improperly, he said.

'I think education definitely works to get people to participate. It definitely works to get people to put in more money'

Ryan L. Bauer
Mutual of Omaha Insurance Co.

Mr. Bauer suggested that plans offer choices ranging from hands-off guided selection options featuring professional investment portfolios, to do-it-yourself options for those seeking to self-direct their investments. The plan should offer an ability to blend choices and should be supported by online access and retirement planning tools, he said.

"What we think is going to become best practices is you really have to have the full spectrum of choice in your investment lineup," Mr. Bauer said.

"A good analogy is the difference between taking a guided tour and going off on an expedition alone," he said. "There's nothing wrong with either of those."

While some plan participants do want to take a very hands-on approach to directing their assets, many do not, Mr. Bauer said.

Mr. Bauer referred to what he called "The Wild West, Wild Bill Hickock environment." That's where participants are told "We're going to teach you how to use the gun and how to put the bullets in but you're on your own," he said. "That's a tough environment for a lot of our participants to be in."

Mutual of Omaha's surveys have shown a majority of plan participants would be interested in professional investment portfolios, Mr. Bauer said. In such funds, decisions on strategic asset allocations and portfolio rebalancing are made for the participant, with participants guided to the appropriate fund based on long-term investment needs, time horizon, risk tolerance and return objectives.

Once plans have the proper choices in place, plan sponsors should then work to shift their asset allocation education efforts to focusing on the "why" of allocation decisions, not the "how," Mr. Bauer said.

A plan sponsor, Anne McKillips, president of Atlanta-based consulting firm AH Enterprises Inc., said while formal education efforts are necessary, also important are "water cooler conversations."

Ms. McKillips said she'll often direct conversations among employees to the subject of their 401(k) plan. "I want them talking about it," she said. "I want them teaching each other."

It's also important to provide investor education in manageable doses, she said.

"You've got to give your people a very bite-sized, constant feeding of information," Ms. McKillips said. "I do think you should have mandatory meetings. But then you should follow up with bite-sized pieces of information the rest of the year."

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401(k): Rules on executive loans causing concerns

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entirely. That action, in turn, could hurt employee participation in the plan, especially by rank-and-file employees for whom access to account balances is a powerful incentive to contribute.

"Having loans available gives employees a comfort level," said Marilyn Scalia, a vp with Mellon HR Solutions in Fort Lee, N.J.

"If you eliminate loans, participation will go down, and the amount of retirement savings will decrease," Mr. Kra said.

But such scenarios, which many have feared, may not happen. Officials at the Securities and Exchange Commission, the federal agency with primary responsibility for interpreting and enforcing the Sarbanes-Oxley law, has informally put out word that they do not consider 401(k) plan loans to be the type of company-provided or arranged credit that is banned under the law, say benefit attorneys who have spoken to SEC staff.

A source close to the SEC confirmed, though, that there are no current plans for official guidance on the issue.

In addition, several top benefit attorneys have concluded that 401(k) plan loans would not be affected by the Sarbanes-Oxley ban on companies arranging or providing credit to top executives because so-called 401(k) loans, despite the term, really are not loans.

"The only amount a participant can take is a portion of the vested account balance. It really is an advance of money that is already owed to the participant," explained Rosiana Barker, a partner with Ivins, Phillips & Barker in Washington.

Others say putting in a loan provision in a 401(k) plan which is available to all plan participants, is not equivalent to extending credit to a top executive.

"Taking that step in plan design is not the same thing as arranging a loan for an executive. You are acting to achieve a much broader goal," said Mark Wincek, a senior partner with the law firm of Kilpatrick & Stockton L.L.P. in Washington.

Still, the only way the issue can be resolved definitely is for the SEC to issue guidance or for Congress to clarify the law.

"There is going to be a lot of trouble and confusion if clarification isn't provided," said Mark Ugoretz, president of the ERISA Industry Committee, a Washington-based employer benefits lobbying organization.

But guidance could be a while in the making.

"This issue is not a priority with the SEC," said Kyle Brown, an attorney with Watson Wyatt Worldwide in Washington.

Alternatively, experts say, the Labor Department could issue a special so-called class exemption stating that denying 401(k) plan loans to top executives for purposes of complying with the Sarbanes-Oxley law, while making loans available to others, would not be considered a prohibited transaction.

"This could be resolved very quickly and simply by the Labor Department," Mr. Kra said.

While the Labor Department is aware of the issue, it believes responsibility lies with the SEC, a spokeswoman said.

However the issue is resolved, few believed that Congress intended to include 401(k) plan loans as part of a ban on corporate loans to top executives, a provision that triggered by outrage over actions such as former WorldCom Inc. Chief Executive Officer Bernard J. Ebbers receiving a low-interest loan of more than $400 million from the company he once headed.

"You are talking about borrowing your own money, not dipping into company assets," Hewitt's Ms. Miller said.

Loan provisions have become a nearly universal feature of 401(k) plans. Last year, 94% of plans sponsored by major employers offered loans, according to a Hewitt survey.

The 401(k) plan loans are attractive to participants because of such features as an easy application process, repayment through salary deduction and because the interest paid goes back into the account and not to a third-party commercial lender, said Rachel Kugelmass, a director in Mellon HR Solutions' product management group in Fort Lee.

In addition, financially, 401(k) plan loans are far more attractive than taking a hardship distribution from the plan. A 10% excise tax, as well as regular taxes, are imposed on hardship withdrawals, while loans are exempt from taxes, unless they are not repaid on time.

On the other hand, borrowing funds from a 401(k) plan reduces the amount of assets on which to earn investment income.

"Individuals don't always consider the downstream impact," Ms. Kugelmass said.

Plan participants, under law, can borrow up to the lesser of $50,000 or half of their vested account balance.

401(k) LOAN PROVISIONS POPULAR

More employers are adding loan provisions to their 401(k) plans

percentage of plans offering loans to participants

Year	1991	1993	1995	1997	1999	2001
%	67	74	81	90	92	94

Source: Hewitt Associates Inc.

FEHBP: Federal plan benefit costs rising

Continued from page 3

increases in copayments, have helped to restrain cost increases. Benefit changes reduced premium hikes next year by 0.6%, according to OPM.

Observers note that the unmatched purchasing power of the federal government is a key factor in its ability to hold down premium hikes.

"They should do better, because they are so big," Ms. Darling said.

"They have such huge negotiating power. It would be difficult for a health plan not to view the government as one of its key clients," said Mark White, a consultant with Watson Wyatt Worldwide in Washington.

Still, observers say it is depressing that inflation in the health insurance market is so high that an 11% increase in premiums would be considered good news.

"We have completely changed our expectations," Mr. White said.

For federal employees, the biggest change next year will be the addition of flexible spending accounts, a feature now nearly universal in the private sector. Starting July 1, 2003, the federal program will begin offering FSAs to employees to pay for uncovered health care and dependent care expenses on a pretax basis. Although the final amount will not be decided until OPM selects an administrator, the government is considering annual contribution limits of $3,000 for health care and $5,000 for dependent care.

Adding an FSA feature will help keep the federal program competitive with the private sector, OPM's Ms. James said.

In another first, one plan sponsor, the American Postal Workers Union, will offer a type of consumer-driven health care plan. Under that plan, enrollees can draw upon a government-funded account to pay the first $1,000 of health care expenses. Enrollees pay the next $600 of expenses, and the plan pays 85% of expenses after that. Enrollees can roll over $500 of unused account balances annually to pay for expenses in subsequent years. Up to $4,000 can be accumulated in an account, but the balance is forfeited when the employee terminates employment.

Also new are Web-based tools that will help participants compare the benefits, costs and other features of health plans available to them. In addition, plans' customer-service, satisfaction and accreditation records will be available online.

On average, the government pays 72% of premiums in the FEHBP. Next year, employees, on average, will pay $4.45 more per pay period for individual coverage and $10.21 more per period for family coverage. As is the case with most private sector plans, federal employees pay their share of the health insurance premium with pretax dollars.

NCQA: Care quality growing

Continued from page 1

10 million Medicare and Medicaid recipients—or roughly 28% of the U.S. population.

The report marked the third consecutive year of improvement, reflecting significant gains on a range of clinical measures as reported by the participating organizations.

Among the key findings:

- The percentage of patients who had their high blood pressure under control rose to 55.4% in 2001, compared with 51.5% in 2000 and 39.0% in 1999.
- Heart attack patients receiving beta blocker treatment after the attacks rose to 93.5% in 2001, compared with 89.4% in 2000 and 85.0% in 1999.
- Children receiving chicken pox inoculations reached 75.3% in 2001, compared with 70.5% in 2000 and 63.8% in 1999.
- The percentage of eligible participants receiving cervical cancer screening reached 80.0% in 2001, compared with 78.1% in 2000 and 71.8 in 1999.

NCQA President Margaret E. O'Kane pointed that even the most slowly improving quality measure—use of asthma medication—is growing at a rate of about 3% annually, which would mean that nearly 100% of the asthmatics who need treatment will be receiving it in 10 years if current trends continue.

Ms. O'Kane used the increased prevalence of chicken pox vaccination to demonstrate the indirect benefits of quality health care. The wider use of chicken pox inoculations to date has probably prevented 620,000 cases of the disease, which even though many people dismiss as a minor childhood malady, can lead to serious complications, she said. Even without complications, each case of chicken pox that didn't happen "probably means a parent somewhere didn't miss two days of work," she said.

While the notion that rising health care costs could enhance the drive toward quality seems "bizarre," employers are paying indiscriminately now for health care, regardless of quality, said Francois de Brantes, program leader-health care initiatives for Fairfield, Conn.-based General Electric Co. Employers must make "a true business case for quality" with providers, he said.

"If we can rewarded those providers that do a better job," then no providers will be able to afford not to do a better job, said Jay Fulkerson, president of Appleton, Wis.-based Touchpoint Health Plan. NCQA recognized Touchpoint as the "highest-performing plan in the nation overall" in this year's survey.

Mr. Fulkerson said that Touchpoint set up a system whereby physicians can share data and to see how they measured against others in terms of quality of care, and built a reimbursement system built around achieving specific goals. "I think this is transportable across the country," he said.

"People need to buy health care based on value, just like any other product," said Mr. Fulkerson.

Dr. Nathaniel Clark, vp-clinical affairs for the American Diabetes Assn. in Washington, cited several ways to reward quality. "We have to create an incentive financially," not necessarily for providers to make more money but to assure that they don't lose money while improving quality. This includes financial support from health plans for improvements such as systems to track quality, he said.

"We need to reward quality but go after waste where we see it," said the NCQA's Ms. O'Kane.

A consultant not connected with the survey or the press conference said there was a certain "irony" in the study's findings.

"This is an assessment of managed care plans. This is a measure of improving quality in managed care at a time when—for better or worse—the country is turning away from managed care. There's an irony there," said Joe Martingale, national leader for health care strategy for Watson Wyatt Worldwide in New York.

"It's also evidence that these things take time. The NCQA with HEDIS measures has been at this for many years now, and this demonstrates that quality improvements don't come easily or quickly," he said.

HEDIS, the Health Plan Employer Data and Information Set, is a registered trademark for a performance tool involving more than 60 different measures. More than 90% of the nation's health plans use it, according to the NCQA.

"The State of Health Care Quality: 2000" is available at www.ncqa.org.

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War risk: Underwriters wary of action against Iraq

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The situation for airlines is not as urgent in the United States because of fast-track federal legislation introduced in Congress last week. S. 2949, which the Senate Commerce, Science and Transportation Committee passed Thursday, would extend and broaden the government's war risk liability indemnification authority.

The measure, the Aviation Security Improvement Act, would extend the government's authority to cover airlines' third-party war risks by 270 days if the U.S. Department of Transportation terminates the existing coverage provided to airlines after the Sept. 11, 2001, terrorist attacks.

In addition, the measure would give Congress authority to offer airlines federal coverage for their passenger, crew and hull war risks. Such coverage previously has been available only through a presidential determination, noted Scott Russell, a Minneapolis-based managing director at Marsh USA Inc. and the head of the brokerage's U.S. airlines practice.

Indemnification would be excess of a $50 million retention.

The legislation also would require the Transportation Department to "evaluate the availability and analyze the economic impact of war risk insurance on aviation entities in an effort to determine alternative possibilities for providing insurance for air carriers." Should this bill be enacted, the Air Transport Assn.'s risk retention group Equitime could become the vehicle to offer the government's coverage, brokers say.

Equitime was formed earlier this year to provide war risk liability coverage for U.S. airlines. The ATA is trying to obtain government reinsurance backing for the facility before it offers coverage.

The European Union and its 15 member state governments, however, are not pushing urgently enough for the approval and formation of two airline mutuals that would write third-party and passenger war risk liability coverage in Europe if the insurance market were to cancel that coverage, the AEA spokesman said. The viability of these mutuals—Eurotime, set up by the AEA, and Globaltime, set up through the International Civil Aviation Office—depend on approval by the European Commission this week and by various other committees of the European Council next month.

Twelve of the European Union's 15 member states began indemnifying their domestic airlines' third-party war risks after the commercial aviation insurance market cancelled the coverage in response to the Sept. 11 terrorist attacks. But several European Union states have threatened to withdraw their coverage programs when they expire at the end of October.

> **An invasion of Iraq 'could lead to seven-day notices of cancellation' of war risk coverage, or cancellations with offers to rewrite the coverage for additional premium.**
>
> *Ralf Oelssner*
> *Lufthansa German Airlines*

Aviation insurers—now heading into the year's busiest renewal season—currently offer only $50 million in limits for third-party war risk liability coverage, though they continue to cover passenger war risk liability up to the limits of an all-risk hull and liability policy.

Other insurers offer up to $1 billion in third-party coverage but charge high premiums.

All of the war risk coverage is subject to cancellation after a seven-to-30-day cancellation notice.

If the E.U. member states allow their indemnification provisions to expire and the European Union does not approve the two mutuals prior to any conflict between the United States and Iraq, then the airlines would have to rely on the expensive coverage offered in the market.

And if those insurers cancel their war risk coverage because of a U.S.-Iraqi conflict, then European airlines "are grounded," the AEA spokesman said.

"There are some underwriters indicating that if there were an outbreak of war in the Middle East, then their capital providers would insist they withdraw from terrorism coverage," said Ken Coombes, senior vp of the aviation division of Marsh Specialty Operations Ltd. in London.

"If the market withdraws and there's no Eurotime or Equitime, we would have to go to the governments for indemnities. And if they didn't give the indemnities (for third-party and passenger war risk liabilities), then the airlines would be grounded," Mr. Coombes said.

An invasion of Iraq "could lead to seven-day notices of cancellation," or cancellations with offers to rewrite the coverage for additional premium, said Ralf Oelssner, director of corporate insurance for Lufthansa German Airlines in Cologne.

Some brokerage executives, however, said they do not expect wholesale cancellations of war risk coverage, especially for airlines with no operations in the Mideast.

Marsh's Mr. Russell said that he expects underwriters, as they did during the 1991 Persian Gulf War, to impose territory restrictions on where their war risk coverage would apply. He did note, however, that the Sept. 11 terrorist attacks have changed the risk profile for airlines.

Wayne Wignes, the Chicago-based president of Aon Aviation, a unit of Aon Corp., said he does not expect insurers to withdraw war risk coverage, but instead write it "at a fairly significant price."

PHOTO:AFP

The threat of war may accelerate the implementation the two mutuals, said Jonathan Palmer Brown, chairman of specialty at Aon Ltd. in London. "My feeling is that this should enormously help (governments) reach the right conclusion."

If European Council transport ministers at the Oct. 2 meeting do not agree to back Eurotime or Globaltime, then they probably would agree to extend the indemnities beyond the Oct. 31 expiration date, Mr. Palmer Brown said. "I'm more optimistic than I was before" that some coverage solution will be achieved, he said.

Meanwhile, the outbreak of war in Iraq could upset plans to reduce the aviation hull war risk surcharge, which is up for renewal on Oct. 1, Lufthansa's Mr. Oelssner said.

Following the Sept. 11 terrorist attacks and the destruction of four Sri Lankan Airlines aircraft by rebel fighters last year, aviation hull war underwriters increased their rates dramatically and imposed an additional hull war risk surcharge of 5 cents per $100 of fleet value. As a result, the hull war risk market's gross premium increased to more than $500 million from October 2001 to July 2002, compared with $46 million during the same period a year earlier (*BI,* Aug. 5).

Broker executives say underwriters plan to reduce the hull war risk surcharge to 3.75 cents or incorporate the surcharge into the overall hull war risk premium.

"It doesn't matter what they do, as long as they reduce the bottom-line cost," said Mr. Oelssner.

Angus Roberts, aviation war risk underwriter for Limit Underwriting Ltd. at Lloyd's of London, agreed that some underwriters appear to be reducing the surcharge and keeping it separate from the original rate.

But, Mr. Roberts said his syndicate would meld the surcharge into the original hull war risk rate. The results will be that "the overall premium will be reduced to the airline," Mr. Roberts said.

But if the U.S. invades Iraq, the number of aviation hull war risk underwriters might decline and the surcharge would not be reduced, said Mr. Oelssner.

Senior Editor Dave Lenckus contributed to this article.

Conference: Market changes to be reviewed

Continued from page 2

sion will be moderated by Martin J. Ross III, vp/publisher of *Business Insurance*, and Steven Beigbeder, Deloitte & Touche L.L.P.'s national practice leader for workers compensation and disability management services.

The interactive spirit of the roundtables is encouraged throughout the conference, as attendees are invited to ask questions and seek advice on specific problems from the moderators and panelists at the end of each session and during social gatherings.

The conference will begin with a keynote speech by Michael Phillipus, vp communications/external affairs for the New York-based Risk & Insurance Management Society Inc. Mr. Phillipus, who is manager-risk management for Pennzoil-Quaker State Co. in Houston, will highlight workers comp-related developments in the areas of legislation, litigation and regulation.

Following his presentation, two panels representing buyers and sellers will discuss the current market. Employers will present their experiences in coping with higher premiums, tighter underwriting scrutiny, weighing the necessity of terrorism insurance and exploring alternative financing mechanisms. In their panel, workers comp insurance industry representatives will discuss factors behind the current tight market conditions and strategies for helping buyers find cost-effective options and alternatives.

> **Several sessions will discuss ways employers can manage workers comp and related disability claims, including coping with catastrophes.**

In addition, several sessions will discuss ways that employers can manage workers compensation and related disability claims, including coping with catastrophes, developing workable ergonomics and return-to-work programs, and reducing liabilities for automotive-related claims.

Other panelists will discuss integrated disability management, especially in light of a changing regulatory environment that is increasingly concerned about protecting an individual's right to privacy.

The conference will close with a luncheon workshop featuring a discussion of innovative technologies designed to help employers prevent and manage workers comp and disability claims.

The conference is presented with assistance from IBF President and Chief Executive Officer Alexandra Scott and IBF Executive Conference Producer Jennifer Fauci.

In addition, conference participants can earn 12 continuing education credits from the California Insurance Board.

Before the Sept. 27 deadline, the discounted conference registration fee is $675 for risk, benefit and safety professionals. The fee is $930 for service providers. Discounts may be available for IBF conference alumni as well as for groups.

The registration fee entitles an attendee to two lunches, two cocktail receptions, two continental breakfasts as well as refreshment breaks throughout the conference.

Conference attendees seeking a discounted rate of $199 for a single/double hotel room should call the hotel at 415-788-1234 by Sept. 27.

For additional details, contact Ms. Fauci at IBF, 516-594-3000, ext. 19; or *jenniferf@ibfconferences.com.*

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For the Record

This roundup of news from the previous week is generated by *BI*'s daily news reporting. To get breaking news as it occurs, log on to *www.businessinsurance.com*, or sign up online for free *BI* Daily News by e-mail.

Class status denied in drug litigation

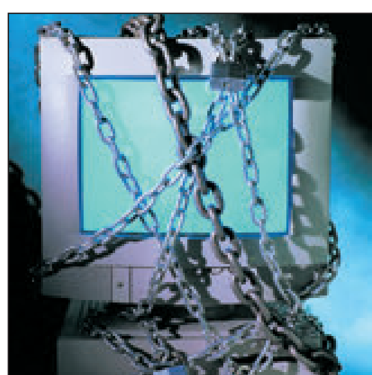
Pfizer Inc. has won its motion seeking to deny class-action status to the multibillion-dollar product liability litigation over the controversial diabetes drug Rezulin. U.S. District Court Judge Lewis A. Kaplan ruled that the individual claims of people who charge they were harmed by the drug were too disparate to be assembled into a class. He noted that plaintiffs' alleged injuries vary, with some claiming heart problems and others claiming liver damage stemming from the use of Rezulin.

Cat reinsurance rates up for third straight year

Although already-rising catastrophe reinsurance rates were accelerated by the Sept. 11, 2001, losses, this year's average cat reinsurance rates on line remain well below their 1993 peak, according to a Guy Carpenter & Co. survey. This year's increases represent the third straight year of rate hikes, following six years of soft market pricing, the report notes. Rates for catastrophe property coverage increased in all regions and for practically all cedents.

Supreme Court refuses to delay asbestos trial

The U.S. Supreme Court has refused to delay a West Virginia asbestos liability trial involving about 8,000 plaintiffs and 250 defendants. The high court rejected without comment requests from Mobil Corp.—now part of ExxonMobil—and Honeywell International Inc. to delay the trial on constitutional grounds. The trial is scheduled to begin Sept. 23 in the Kanawha County Circuit Court.



White House recommends cyber risk management

The availability and utilization of cyber risk coverage for businesses may expand if recommendations in a White House report, "The National Strategy to Secure Cyberspace," are realized. The report urges President Bush's Critical Infrastructure Protection Board to "work with the insurance industry on ways to expand the availability and utilization of insurance for managing cyber risk." It includes an addendum detailing the role that insurance can play in working with businesses and minimizing risks associated with cyber security challenges.

9th Circuit clarifies Jones Act eligibility

A seaman injured aboard a barge that is incapable of navigating the open seas but is routinely towed to different ports would be eligible for benefits under the Jones Act, a 9th U.S. Circuit Court of Appeals panel has ruled. While the ruling overturns a lower court's decision, the 9th Circuit panel did not decide whether the injured plaintiff qualifies as a seaman under the Jones Act. The panel remanded that issue to a lower court. Sailors injured aboard ships are compensated under the terms of the federal Jones Act.

Berkley forms new reinsurance underwriter

W.R. Berkley Corp. has formed an underwriting management group to write casualty facultative reinsurance on a direct basis. BF Re Underwriters L.L.C. will not affect the operations of Facultative ReSources Inc., another W.R. Berkley reinsurance underwriting unit, William R. Berkley, chairman and chief executive officer of the parent company, said in a statement. Facultative ReSources underwrites individual certificate and program facultative reinsurance business.

Diversity training not boosting tolerance: Study

Despite stepped-up diversity training in the workplace following last year's terrorist attacks, there has been little improvement in the tolerance employees display toward colleagues, a survey reveals. The Society for Human Resource Management polled 361 employers in January and 202 employers in April. While employers reported there was no overall improvement in tolerance, SHRM did find that 21% of employees were much less or a little less tolerant of ethnicity, while another 21% were much more or a little more tolerant. Results were similar for race and religion.

New ACE unit offers excess comp coverage

ACE Ltd. has formed a unit to provide excess workers compensation insurance. The stand-alone coverage is written by ACE Risk Management unit ARM Excess Workers Compensation in Philadelphia. The coverage is designed for clients that self-insure predictable losses and want coverage for catastrophic events. Coverage will be written above an attachment point of $250,000 per occurrence up to statutory limits for qualified risks. The minimum premium is $100,000.

Briefly noted

William J. Kelly, who served as president of the Risk & Insurance Management Society Inc. in 1995-1996, is retiring after a 30-year career in insurance and risk management. Mr. Kelly retires as an executive vp and financial institution practice leader for Willis North America Inc. in New York. He previously served for 15 years as a managing director at J.P. Morgan & Co. Inc., with responsibility for risk management....Allianz A.G. Holding will increase the asbestos and environmental reserves of its **Fireman's Fund Insurance Co.** unit by $750 million, the Munich, Germany-based insurer said....**Zurich Financial Services Group** is paying former Chairman and Chief Executive Officer Rolf Hueppi 6.2 million Swiss francs ($4.1 million) in severance compensation, ZFS said. Mr. Hueppi resigned from the Zurich-based insurer in April and was replaced by James Schiro as CEO....A Florida state court judge in Miami on Friday reduced an award against **Philip Morris Cos. Inc.** to $500,000 from $5.5 million. The cigarette maker said it will appeal to seek dismissal of the remainder of the damages in the case, which was brought by a flight attendant who claims her chronic sinusitis was caused by secondhand smoke on airplanes....Metro-Goldwyn-Mayer Inc. and American International Specialty Lines Insurance Co. have agreed to settle their dispute over coverage in a **long-running copyright and trademark infringement case** involving the James Bond character (*BI*, Sept. 16). Los Angeles Superior Court Judge Peter Lichtman has given the parties until Nov. 18 to hammer out details, said MGM attorney William M. Shernoff, a partner with Shernoff Bidart & Darras in Claremont, Calif....Kenneth C. Bollier will retire as president of California's **State Compensation Insurance Fund**, effective Dec. 31.

Online Poll [9/16 - 9/20]

Should the federal Family and Medical Leave Act be expanded so employers are required to offer paid leave to employees?

YES **35.5%**

No **64.5%**

Take part in our weekly poll at *www.businessinsurance.com*

Holocaust claims organizations reach insurance funding accord

By MEG FLETCHER

WASHINGTON—A new agreement between two organizations working to ensure the settlement of Holocaust-era insurance claims ends a yearlong dispute over how claims would be funded.

The agreement, which was signed Wednesday, requires international insurers participating in the International Commission on Holocaust Era Insurance Claims to fully fund their financial commitments to funds administered by Washington-based ICHEIC. The insurers held that previous payments they had made to ICHEIC of $36 million should partially offset other payments owed to a German foundation, whose $275 million in compensation payments will also be administered by ICHEIC.

After a year of "grueling and contentious" negotiations, the insurers "did the right thing," according to Nat Shapo, chair of the National Assn. of Insurance Commissioners Holocaust Commission Task Force and director of the Illinois Insurance Department.

The settlement also calls on for insurers to produce "significant" policyholder lists from their archives, as well as to implement a sophisticated process for matching names to a new list of Jewish residents in Germany during the Nazi era, according to an NAIC statement.

In addition, the current Sept. 30 claims deadline has been extended to March 31, 2003, to give the public adequate time to review the lists.

More information is available from *www.icheic.org*.

BI Stock Index [9/16- 9/20]

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

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

BI Stock Index 1675.29

Dow Jones 7986.02

S&P 500 845.39

Largest gains

Company	Change
Meadowbrook Ins. Group	10.61%
Argonaut Group	8.67%
SCPIE Holdings Inc.	7.64%
Trenwick Group Ltd.	7.55%
Unico American Corp.	5.30%

Largest losses

Company	Change
Gainsco	-33.33%
ING Groep N.V.	-22.85%
SCOR	-22.21%
AXA-UAP Group	-18.93%
Allmerica Financial Co.	-17.35%

Weekly change by market segment

Segment	Change
Brokers	-5.04%
Insurers/Reinsurers	-5.13%
Managed Care Organizations	-4.37%

Source: CNET Investor (investor.cnet.com)

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In 47 days
an accident could happen right here.

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"That's my job – to anticipate when an accident might happen, and make recommendations so that it doesn't. I look at blueprints for hidden hazards. You'd be surprised what I notice – I'll see where an unguarded floor opening might allow workers to fall, or where a flagger might be necessary to avoid traffic dangers. Every layer of blueprints gets my scrutiny. It helps our customers pre-plan, see the potential problems and reduce the chance of accidents before the job even starts. Once construction begins, I can work with site supervision to anticipate additional on-site hazards. If you ask me, it's not construction projects that are dangerous. It's not planning ahead."

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