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PBGC taking over Kemper pension plan / 3

Feds probe AIG unit over Brightpoint deal / 3

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Business Insurance®

October 25, 2004

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HEAT RISING

Industry in crosshairs as states launch probes

By DOUGLAS McLEOD

NEW YORK—The aftershocks of New York Attorney General Eliot Spitzer's fraud and antitrust charges against Marsh & McLennan Cos. Inc. continued to reverberate last week as the world's three largest brokers halted their collection of hundreds of millions of dollars of contingent commissions and as the brokerage industry became the target of regulatory and law enforcement officials in several states.

New York Insurance Superintendent Gregory V. Serio on Friday ordered representatives of MMC, its Marsh Inc. brokerage unit and 11 affiliates to appear at a hearing Nov. 24 to respond to charges that "they used fraudulent, coercive and dishonest practices" in placing client risks.

The order cites Mr. Spitzer's civil complaint against Marsh, which charged the broker with steering clients to insurers paying it the highest contingent commissions and colluding with insurers to produce inflated quotes to channel business to Marsh's favored insurers.

Announcing its action, the New York department noted that

See **BROKERS**/page 46

PHOTO: GETTY IMAGES/STEPHEN CHERNIN

New York Attorney General Eliot Spitzer is widening his probe.

Compensation Crisis

Inside:

Industry's nightmare is its own making
Brokers and insurers must change, Paul Winston writes **page 6**

So what if everybody does it
BI editorial argues for permanent ban to conflicts of interest **page 8**

Marsh, Willis, Aon cave in
Top three halt contingent compensation **page 44**

Resources on *www.businessinsurance.com*
Articles and other links probe broker compensation issues **page 44**

Contingent commissions pervasive
Chart shows vast majority of largest brokers take them **page 45**

Commission deals limited on benefit side
Consultants eschew contingencies, partly due to ERISA **page 46**

Jolt to buyers forcing some to rethink ties

By ROBERTO CENICEROS

Risk managers are skeptical that the alleged fraud and bid-rigging that Marsh Inc. stands accused of is a widespread industry practice.

If the allegations by New York Attorney General Eliot Spitzer are true, the misdeeds would likely have been confined to small pockets within the broking industry, such as Marsh's Global Broking unit, a centralized placement facility that is a focus of Mr. Spitzer's probe, they say. If it were a systemic problem, risk managers reason, simple word of mouth would quickly reveal the problem.

Still, the allegations that Marsh set up bid-rigging schemes and placed business with insurers that would deliver the largest contingent commission payments, has shocked many risk managers and some are already reviewing their current brokerage relationships.

See **BUYERS**/page 44

Late News

First-half P/C profits top $23 billion

The U.S. property/casualty insurance industry's aftertax net income reached a record $23.52 billion during the first six months of this year, according to the Insurance Services Office Inc. and the Property Casualty Insurers Assn. of America. The industry's net income, up more than 60% over the prior-year period, reflected both positive underwriting and improved investment results. Net written premium for the first half of the year grew 4.6%, to $212.12 billion. Insurers experienced an underwriting gain of $9.03 billion during the first half, compared with an underwriting loss of $2.71 billion a year earlier, and their combined ratio after dividends improved to 94.4% from 99.8%.

RR Donnelley settles bias class action

Chicago-based commercial printer RR Donnelley & Sons Co. has agreed to pay $15 million to settle a 1996 class action suit alleging racial discrimination against hundreds of employees. The suit alleged, among other things, that African-American workers were subjected to a racially hostile work environment; kept in temporary positions at length and thereby deprived of health benefits; and wrongfully terminated during a 1994 shutdown of the company's Chicago manufacturing plant. As part of the settlement, RR Donnelley did not admit to any wrongdoing. A spokesman for RR Donnelley declined to comment on how the company will fund the settlement.

Employer of temp worker must pay comp claim

The California Insurance Guarantee Assn. is not liable for workers compensation claims filed by the employee of a temporary staffing company that was insured

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LARGEST REINSURANCE BROKERS

Ranking on page 16

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Feds probe AIG subsidiary

Deal with Brightpoint in 1998 at center of inquiry

By JUDY GREENWALD

NEW YORK—American International Group Inc. is the target of a federal grand jury investigation in connection with an insurance contract for an Indiana company that prosecutors allege did not involve any actual risk transfer.

A Securities and Exchange Commission investigation into the same matter resulted in a $10 million settlement by AIG last September, in which AIG did not admit any wrongdoing (*BI*, Sept. 15, 2003).

New York-based AIG had been charged by the SEC with defrauding investors of Plainfield, Ind.-based Brightpoint Inc., a distributor of mobile phones. According to the SEC's complaint, Brightpoint officials discovered in late 1998 that the company faced $29 million in losses from a division in the United Kingdom, which far exceeded its publicly announced loss estimate of $13 million to $18 million.

AIG unit National Union Fire Insurance Co. of Pittsburgh, Pa., provided $15 million in retroactive coverage that allowed Brightpoint to report an insurance receivable in its financial statements, offsetting the additional losses, the SEC said. As a result, Brightpoint's 1998 net income was overstated by 61%, according to the SEC complaint.

The policy did not represent actual insurance, though, because AIG bore no risk and Brightpoint's $15 million premium simply made a "round trip," deposited with the insurer and repaid to the telecom company, the SEC alleged.

AIG and Brightpoint officials disguised the nature of the transaction by backdating the policy, concealing the large premium and combining the retroactive coverage with standard fidelity coverage, the suit charged.

After being subpoenaed by the SEC in late 2001, Brightpoint restated its financial results to reflect its payment of the full premium in 1998 rather than in installments over three years, as it had earlier claimed. The telecommunications company restated its results again in early 2002 to account for the entire transaction as a deposit rather than insurance.

AIG said the U.S. attorney for the Southern District of Indiana informed it of the grand jury probe. A spokeswoman for the U.S. attorney's office in Indianapolis had no comment on the latest investigation.

Takeover of Kemper plan largest of kind for PBGC

By JERRY GEISEL

WASHINGTON—The Pension Benefit Guaranty Corp. on Thursday took over and terminated Kemper Insurance Cos.' underfunded pension plan, the biggest insurer-sponsored pension plan ever assumed by the PBGC.

Kemper's retirement plan has promised $1.05 billion in benefits to its nearly 12,000 participants—mostly retirees and former employees of operating unit Lumbermens Mutual Casualty Co.—but has just $515 million in assets.

The PBGC estimates it will be liable for about $529 million of the $540 million funding shortfall. That easily eclipses what had been its biggest loss from the takeover of an insurer-sponsored pension plan. In 2002, the PBGC took over failed insurer Reliance Insurance Co.'s pension plan, which was underfunded by about $124 million.

In the case of Kemper, the federal agency stepped in because the company will not be able to pay benefits when due, said PBGC Executive Director Bradley Belt. The financially troubled insurer stopped writing new and renewal business last year amid several ratings downgrades and deteriorating financial results; it now is running off business.

A spokeswoman for Long Grove, Ill.-based Kemper said the PBGC's action should not be interpreted as implying any difficulties with its solvent runoff plan. "We believe the PBGC action will not affect our ability to continue executing our runoff plan," she said.

Kemper has terminated its pension plan.

PHOTO:NY TIMES

Silverstein Properties principal Larry Silverstein is seeking to recover twice the limits of the World Trade Center's property insurance program from a group of insurers.

Silverstein resumes bid for double-limit recovery on WTC

Each side argues over terms

By DOUGLAS McLEOD

NEW YORK—Lawyers for Silverstein Properties Inc. and nine insurers launched the second phase of the World Trade Center property insurance litigation Monday, presenting jurors with starkly different positions on whether the WTC's destruction constituted one occurrence or two.

WTC COVERAGE TRIAL

In opening arguments, Silverstein attorney Bernard Nussbaum noted that the WTC leaseholder's policies insure against "direct physical loss" and that the Sept. 11, 2001, terrorist attack involved two planes striking two buildings 17 minutes apart, causing two fires that led to separate collapses 29 minutes apart.

"On 9/11, we suffered two distinct physical losses...separated by time and separated by space," Mr. Nussbaum told a jury of 10 women and two men, arguing that Silverstein is entitled to two policy limits.

Insurers never expected that the total destruction of the WTC complex could be treated as one occurrence and did not limit their exposure to multiple occurrences, said Mr. Nussbaum, who is with Wachtell, Lipton, Rosen & Katz in New York. He cited

See WTC/page 42

Inside Business Insurance

Trains using video to establish crash fault

Some freight railroads are installing video equipment to help establish liability in rail-crossing accidents. Page 4

Csiszar to continue efforts to develop PCI

New PCI President Ernst N. Csiszar plans to build on the work done by his predecessor. Page 6

Commission practices invite nightmare

It's going to be a long, dark Halloween for the insurance industry, writes Paul Winston. Page 6

Industry must work to regain trust

Brokers and insurers must get rid of contingent commissions to eliminate any appearance of a conflict of interest, an editorial says. Page 8

NSW premier seeks law to open Hardie records

New South Wales Premier Bob Carr has introduced a bill that would give regulators and others access to James Hardie documents. Page 43

Online

- *Business Insurance* has compiled past *BI* articles and other resources on the New York Attorney General's lawsuit against Marsh & McLennan Cos. Inc.
- Searchable directories provide access to all the listings of industry vendors in *BI*'s Market Sourcebook.
- New Opinion Poll for readers: Will New York Attorney General Eliot Spitzer's investigation into the placement of insurance contracts ultimately benefit insurance buyers?

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REPORTING ON CORPORATE RISK AND EMPLOYEE BENEFIT MANAGEMENT NEWS

Business Insurance (ISSN 0007-6864) Vol. 38, No. 43, is published weekly by Crain Communications Inc., 360 N. Michigan Ave., Chicago, Ill. 60601-3806. Periodicals postage is paid at Chicago and at additional mailing offices. POSTMASTER: Send address changes to Business Insurance Circulation Department, 1155 Gratiot Ave. Detroit, Mich. 48207-2912. $5 a copy and $97 a year in the U.S. $130 in Canada and Mexico (includes GST). All other countries, $230 a year (includes expedited air delivery). Canadian Post International Publications Mail Product (Canadian Distribution) Sales Agreement No. 40012850, GST No. 136760444, Canadian return address: 4960-2 Walker Road, Windsor, ON N9A6J3. Printed in U.S.A. Copyright © 2004 by Crain Communications Inc.

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Cameras giving railroads clear picture of crash fault

By MICHAEL BRADFORD

Freight railroads hope that equipping their locomotives with cameras and microphones will provide a clearer defense in grade-crossing accident cases.

High litigation costs from accidents involving vehicles and pedestrians at grade crossings, as well as public safety concerns, are driving the railroads' moves to install recording equipment that can be used to provide a visual account of what happens when trains are involved in accidents.

And while such efforts can raise privacy concerns, train crews generally have accepted that the recording equipment is not being installed to monitor their work but to make their jobs safer and to keep down claims costs.

Grade crossings, which are points where roadways cross railroad tracks at the same level, have long been marked as dangerous intersections. According to the Federal Railroad Administration, 300 to 400 deaths occur each year at the crossings.

"It isn't unusual for grade-crossing cases to go into the millions of dollars, so, obviously, there is a lot at stake here," said a spokesman for Union Pacific Railroad in Omaha, Neb. Earlier this year, the Arkansas Supreme Court upheld a $35.8 million award against Union Pacific in a grade-crossing case, he said.

Union Pacific, like most large railroads, is self-insured, carrying excess coverage above a large retention.

Union Pacific's decision to install cameras was prompted by a July article in the New York Times that pointed out flaws in the railroad's reporting of fatal accidents to federal authorities. Union Pacific, in a statement, acknowledged that it learned during the course of the newspaper's investigation that "some of our reporting and compliance processes were not as thorough as we expect," and corrective actions were taken.

In the same statement, Union Pacific announced that it would install cameras in its locomotives to better document crossing incidents.

The railroad plans to equip around 1,000 of its locomotives with cameras and microphones over the next year and eventually have the equipment in around 6,700 locomotives. The cameras and microphones are being installed inside the cabs and pointed outside to record video and sound.

See TRAINS/page 38

Concerns about safety and liability are prompting some freight railroads to install cameras and other equipment designed to record incidents that occur at rail crossings.

California law mandates periodic manager training on harassment issues

By JUDY GREENWALD

SACRAMENTO, Calif.—California legislation that requires employers to provide two hours of sexual harassment prevention training to supervisors every two years is the most rigorous in the nation, but its benefits could encourage other states to follow suit, say observers.

While some other states have laws that address sexual harassment prevention training for employees in general and supervisors in particular, no other state requires that the training be repeated, according to Brightline Compliance L.L.C., which provides employment training.

But observers say that the training required under A.B. 1825, which was signed into law by Gov. Arnold Schwarzenegger last month, will ultimately pay off for employers in lower litigation costs. It will also give employers guidance for training that had already been called for in federal and state judicial decisions, observers say.

The law's requirements, though, may lead to at least some fine tuning of training programs, even among those Cali-

See HARASSMENT/page 41

RIMS' COO named society's fifth executive director

NEW YORK—Mary Roth has been named executive director of the Risk & Insurance Management Society Inc.

Ms. Roth, the society's chief operating officer, has handled the executive director's duties since John J. Hampton resigned from the position in August to pursue consulting work. She becomes the New York-based society's fifth executive director.

Ms. Roth, who joined RIMS in 1985, has held the position of chief operating officer since July. Before that, she served as the society's deputy executive director.

Mr. Hampton assumed the executive director post in 2000, succeeding Linda Lamel, who served as RIMS' executive director from 1997 to 2000. Eugene Ricci retired in 1997 after holding the position for more than six years. Ron Judd, the society's first executive director, served for 24 years.

—By Michael Bradford

Ms. Roth

Errors & omissions

- Due to a production error, the chart on surplus lines premiums and taxes by state in the Sept. 20 issue incorrectly reported total gross surplus lines premiums written for 2003 as $28,133,870,985. The 2003 total is $28,909,990,379.

23rd Annual Employee Benefits Symposium

Complexity of benefits issues challenges lawmakers, lobbyists

By JOANNE WOJCIK

LAS VEGAS—The adage about the two things you never want to see being made—sausage and legislation—is especially appropriate when it comes to laws governing employee benefits, a congressional lobbyist says.

Congressional lawmakers often are myopic when they vote on benefits-related bills, frequently oblivious to the fact that their views on other legislation or increasing the financial burden on business, according to James A. Klein, president of the American Benefits Council, a Washington-based advocate of employer-sponsored benefit plans.

"Health and pensions are the two largest tax expenditures in the federal budget. It's bigger than the deduction that's given for home mortgage interest, charitable contributions" and state income tax, Mr. Klein told those attending the opening session of the 23rd Annual Employee Benefits Symposium, sponsored by the International Society of Certified Employee Benefits Specialists and held in Las Vegas.

He noted that "$95 billion, $96 billion of federal tax dollars are not collected because the tax code encourages employers to provide health and retirement coverage to their workers and retirees," he said.

See BILLS/page 34

Continued coverage on page 36

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Csiszar takes helm at PCI as group enters next phase

By RODD ZOLKOS

Jack S. Ramirez, retiring president and chief executive officer of the Property Casualty Insurers Assn. of America, likens his departure to a runner in a relay race handing off the baton.

And, having overseen the initial transition following the PCI's birth earlier this year from the merger of the National Assn. of Independent Insurers—which he previously led—and the Alliance of American Insurers, Mr. Ramirez said that now it's time for his successor, Ernst N. Csiszar, to run the race's anchor leg.

"Nothing in any organization is ever completed," Mr. Ramirez said. "But the objective was to have a transition period that would be completed by the time the new CEO came on board."

"We went home Wednesday night Jan. 7 as NAII. And we came back Jan. 8 as PCI," recalled Joseph J. Annotti, PCI vp-public affairs.

The fact that the combined organization was up and running from the start with a functioning board "is a real tribute to Jack's leadership.

Mr. Ramirez

Mr. Csiszar

That is not an easy thing to accomplish," Mr. Annotti said. "The way the entire staff was able to thrust itself into the situation following Jack's lead was really remarkable."

While there remain issues to be resolved, the emphasis was on getting the newly combined Des Plaines, Ill.-based organization "to where it was at least functional," Mr. Ramirez said.

"When the merger agreement was struck, the staffing, the structure, some of the processes were agreed to, and it was indicated that that was more or less an interim situation," he said. "It was not the way you would build an organization from the ground up."

But the transition "really has exceeded everyone's expectations," Mr. Ramirez said. "It's a credit to the staff and the membership. They've responded well to the bigger-picture issues here. But there's plenty of work for Ernie to do."

"I think Ernie is the right person, and the board could not have done a better job of selecting the right person," Mr. Ramirez said.

Mr. Csiszar, who was president of

See PCI/page 38

Paul Winston

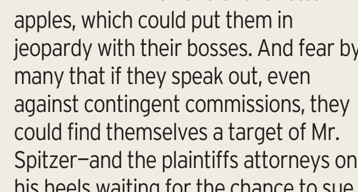
Industry actions invite nightmare

Halloween came early this year for the insurance industry.

Eliot Spitzer is going door to door and definitely doesn't like what he sees. The industry is not going to escape with being pelted by a few rotten eggs; something worse is in store that could haunt it for some time.

Like the homeowner who should know better than to offer rotten treats on Halloween, the industry should have seen this coming. It should have known that its house is not in order and should have taken steps to correct the situation before Mr. Spitzer was on its doorstep. Now, it is too late. Insurers, brokers, buyers and even regulators will face a difficult and painful process of change, as a consequence of Mr. Spitzer's investigations and lawsuits.

Mr. Spitzer's complaint is simple: The insurance industry is using an ethically bankrupt system to compensate brokers, creating a clear conflict of interest that can—and has—resulted in unfair treatment of consumers. Insurance brokers have a duty to represent the interests of their clients, insurance buyers. When they are compensated by the seller, that duty and trust has been fouled.


Paul Winston

Mr. Spitzer claims that Marsh & McLennan Cos. Inc. used its considerable scale and clout to place business with insurers that would give it the best kickbacks in the form of contingent commissions. Mr. Spitzer has named several insurers that were allegedly involved in these arrangements, both in terms of paying these fees to Marsh and in terms of supplying sham bids to support this alleged strategy. And he is looking at other brokers that may have engaged in the same or similar arrangements.

The industry's reaction has been a mix of submission, defensiveness and fear.

Some companies, including brokers and insurers, have publicly announced an end to the compensation agreements, tacitly acknowledging that they should avoid even the appearance of conflict, even if no illegal bid-rigging ensued. That, I believe, is the first step that all insurers and brokers must take to eliminate any whiff of taint from their transactions and restore a clearly level playing field for the competitive business of insurance.

Others have been more defensive, arguing that there is nothing illegal in the compensation arrangements, only in how a few rotten apples took advantage of them for gain. Remove the rotten apples, and the problem is solved. I find that argument feeble.

As we've seen in numerous recent business scandals, just because no law exists to proscribe a questionable activity, that should not be an invitation to engage in it. In this case, the compensation of brokers by the seller clearly creates the potential for controversy, or worse. Rather than avoid this minefield, and demand payment from the customer for valid services, brokers kept quiet in the interest of trying to keep their costs competitive.

When buyers about five years ago first complained about the commissions, a move was made by some brokers to provide greater disclosure of these payments. Risk managers and their representatives seemed to think that was enough, and relatively few even asked about the commissions in the years to follow. Buyers should demand more. Contingent commissions to brokers should be eliminated and replaced with upfront fees and commissions paid by the client for placing coverage.

The other response to Mr. Spitzer has been fear. Fear by insurers and brokers that if they look closely enough at past transactions, they may find some unpleasant realities. Fear by risk managers that they are doing business with one of the rotten apples, which could put them in jeopardy with their bosses. And fear by many that if they speak out, even against contingent commissions, they could find themselves a target of Mr. Spitzer—and the plaintiffs attorneys on his heels waiting for the chance to sue.

This is not a time to hide in fear of change to a better and more open system of doing business. Face it: Mr. Spitzer has shined a light on a problem that won't go away until the rot is cleaned out and repaired. The sooner that hard work is begun, the sooner it will be finished.

Buyers will likely pay more for brokerage services in the future. But the fact is, buyers are paying for it now in the form of higher premiums to cover the commissions to brokers. I say, better to pay it up front and have greater certainty that your coverage is not being improperly placed.

And if a big broker finds that clients aren't willing to pay, and it can't leverage its scale into more lucrative compensation from the client, then competitive forces may bring a painful resizing of the brokerage industry.

Mr. Spitzer clearly does not accept the argument that the industry is competitive enough, and ethically minded enough, to steer clear of conflicts of interest. He's already made some charges, and more are likely.

It's going to be a long, dark Halloween for the industry this year.

Editorial Director Paul Winston's commentary appears fortnightly. He can be reached at pwinston@businessinsurance.com.

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Business Insurance

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ADVERTISING: Boston: 617-292-4856; Chicago: 312-649-5276; Irvine CA: 949-255-5355; New York: 212-210-0133
SUBSCRIPTIONS: Detroit: 888-446-1422

Business Insurance is published by Crain Communications Inc.

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Published weekly at 360 N. Michigan Ave., Chicago, Ill. 60601-3806, Fax: 312-280-3174, biweb@crain.com. Offices: 711 Third Ave., New York, N.Y. 10017-5806, Fax: 212-210-0704; 71121 Minkler St., Abita Springs, La. 70420; Fax: 985-871-4006; Suite 814, National Press Building, Washington, D.C. 20045-1801, Fax: 202-638-3155; 6500 Wilshire Blvd., Suite 2300, Los Angeles, Calif. 90048- 4947, Fax: 323-655-8157; 967 Bermuda Court, Sunnyvale, Calif. 94086-6750, Fax: 408-774-1155; 34 Southwark Bridge Road, London SE1 9EU, Fax: +44-(0)20-7457-1440; 8157 N. Torrey Place, Tucson, Ariz. 85743, Fax: 520-579-3476; 777 E. Speer Blvd., Denver, Colo. 80203-4214; Fax: 303-733-2244; 11133 W. 108th St., Overland Park, Kan. 66210, Fax: 312 280-3174. 77 Franklin St., Suite 809, Boston, Mass. 02110-1510; Fax: 212-210-0704. 4 Executive Circle, Suite 185, Irvine, CA 92614-6791. $5 a copy and $97 a year in the U.S., $130 in Canada and Mexico (includes GST). All other countries, $230 a year (includes expedited air delivery). Rudolf Von Bartesch, circulation manager. Four weeks' notice required for change of address. Send subscription correspondence to Circulation Department, *Business Insurance*, 711 Third Avenue, New York, N.Y. 10017-5806. Microfilm copies available: University Microfilms, 300 Zeeb Road, Ann Arbor, Mich. 48013. Microfiche copies: Bell & Howell, Micro Photo Division, Old Mansfield Road, Wooster, Ohio 44691. Portions of the editorial content of this issue are available for reprint or reproduction in other media. For reprints or reprint permission: Karen Brown Tucker, *Business Insurance*, 360 N. Michigan Ave., Chicago, Ill. 60601-3806, 312-649-5319, Fax: 312-280-3174.

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Editorial

Industry must eliminate contingent commissions

FOLLOWING the allegations raised by New York Attorney General Eliot Spitzer, the stakes for the insurance industry couldn't be higher.

In what may be the biggest scandal ever to hit to the commercial insurance business, Marsh & McLennan Cos. Inc. is accused of rigging premium quotes to maximize its income from compensation agreements with insurers—agreements that are also used by the majority of brokers.

Marsh suspended its so-called market services agreements, but competitors Willis Group Holdings Ltd. on Thursday took an even bolder step—it immediately ceased accepting commissions that are contingent on sales volume or profitability. Aon Corp. followed suit late Friday. As of press time, they were the only brokers to do so. We think that Marsh and all other brokers must take similar action to regain the trust and confidence of their clients. For Marsh, especially, its survival may be at stake.

If Marsh & McLennan's top executives do not do everything in their power to restore the trust of their clients, it is no exaggeration to say the company likely will not survive.

Mr. Spitzer's charge of bid-rigging is deeply disturbing because it would require the collusion of brokers and insurers. If true, insurance buyers are right to wonder who they can trust. If such activity is happening at the world's largest insurance broker and some of the biggest insurance companies, where else is it occurring?

Insurance is a business based on trust. Policyholders rely on their brokers for honest advice and on their insurers' promises to pay claims. The allegations in the Spitzer suit, if true, will shake the industry to its foundation.

It remains to be seen whether the alleged bid-rigging is widespread, but we know for a fact that contingent compensation agreements are commonplace (see chart, page 45).

Many insurance buyers see contingent fees as a conflict of interest, and indeed this was the subject of a debate during the 1998 Risk & Insurance Management Society Inc. annual conference. It led RIMS to negotiate with Marsh an agreement to disclose such compensation in 1999. Why didn't insurance buyers and regulators scream at the top of their lungs in protest when the conflict question was first raised?

Previously, we have questioned the need for contingent commissions. The reason is clear: it is wrong to allow any form of compensation that could alter the broker's allegiance to its client. There is, to be sure, a huge difference between accepting a bonus for meeting a sales or profitability goal and orchestrating false quotes. But we think contingent compensation itself is a slippery slope, as it creates an incentive for fraud and anti-competitive behavior.

Simply put, if a broker knows that its compensation will be increased by a contingent commission, it may be tempted to step away from its duty to clients to obtain what is best for them.

The magnitude of what is involved here cannot be overstated. Marsh is, after all, the world's largest insurance broker, while its Mercer unit is the world's biggest benefit consultant and its Guy Carpenter unit is the second-largest reinsurance broker. Many talented people work at Marsh and other industry companies, providing high-quality service to their customers.

If Marsh's top executives do not do everything in their power to restore the trust of their clients, it is no exaggeration to say the company likely will not survive. That possibility should inspire all industry companies to engage in open and honest communication and, especially, act in the best interests of their clients.

Schillerstrom

Letters to the Editor

Vast majority of brokers do their best for clients

To the editor: As the ramifications of New York Attorney General Eliot Spitzer's allegations of bid-rigging and business-steering by Marsh & McLennan Cos. Inc. and Marsh Inc. reverberate through the commercial insurance marketplace, it is important to remember two things:

The vast majority of insurance brokers are honest individuals who are doing their best to represent the interests of their clients.

The commercial client has an absolute right to know what he or she is paying for.

We at the Council of Insurance Agents & Brokers take the Spitzer complaint very seriously. But as the trade association that represents virtually all the major commercial insurance brokers in this country, we also know it is wrong to presume misconduct on the part of all commercial insurance brokers because of the alleged misdeeds of a few.

According to the latest figures from the Insurance Information Institute, an estimated 2.2 million people work in the commercial insurance business. Some are agents and brokers; others work for carriers and companies involved with life, health and property/casualty insurance.

The vast majority of those 2.2 million people are hard-working, ethical individuals. They earn their clients' trust every day. They are part of a vast and highly regulated industry that provides fuel to the American economy and protects individuals and commercial entities from risk. To suggest that inherent conflicts of interest pervade the industry is absurd.

In considering the Spitzer complaint, it is also necessary to separate the allegations of fraud from the issue of income received through contingent commissions or other commission arrangements.

Allegations of fraud are just that, allegations. If they are proven true, those who are found guilty will pay an appropriate price for breaking faith with their customers. Fraud cannot be tolerated in a business that depends on the trust between the broker and client.

But contingent commissions per se are neither illegal nor improper. They have been a standard feature of the commercial insurance marketplace for many years and are linked to a variety of services provided by the broker.

The Council has been on record since 1998 favoring full disclosure of these commission arrangements to commercial customers. The Council believed then, and believes now, that full disclosure is the best practice brokers have to guard against suggestions of conflict or the appearance of conflict in their business dealings.

This position has been embraced by the Risk & Insurance Management Society, the largest association of commercial insurance buy-

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Reinsurance: Trends & Issues

Spotlight Editor: Judy Greenwald

Reinsurance brokers big and small seek ways to stand out

By SALLY ROBERTS

When it comes to choosing a reinsurance brokerage, ceding companies can select from an array of partners, from the world's largest reinsurance brokerage down to the very smallest boutique firm.

But because virtually all reinsurance intermediaries today have access to the worldwide reinsurance market and most, if not all, offer various catastrophe and financial modeling capabilities, is size the only differentiator?

Some observers think so.

> **Reinsurers generally 'will do business with anyone who is a licensed reinsurance intermediary.'**
> *Andrew Barile Andrew Barile Consulting Corp. Inc.*

With the exception of size in terms of revenues and employees, "there's not much differentiation between the firms," according to Andrew Barile of Andrew Barile Consulting Corp. Inc. in Rancho Santa Fe, Calif. It used to be that the largest reinsurance brokerages had access to all the reinsurance markets and used that as a way to differentiate themselves from the smaller players, he said. But reinsurers in general "will do business with anyone who is a licensed reinsurance intermediary," said Mr. Barile, who provides consulting services to intermediaries and reinsurers.

"Bigger isn't necessarily better, but I think what is characteristic of the marketplace is that the bigger boys will use the bigger brokers and the smaller boys may be relegated to the smaller brokers. But that's not all bad," said Paul Walther, chief executive officer and principal consultant with consulting firm Reinsurance Directions Inc. in Heathrow, Fla.

"As a practical matter, the bigger

See BROKERS/page 25

Gradual market softening expected to continue

Pricing discipline seen as curb to drastic change

By JUDY GREENWALD

The U.S. property/casualty reinsurance market is expected to continue its gentle, if inexorable, slide toward soft conditions.

The four recent hurricanes in the United States, with their estimated $19 billion to $35 billion price tag, are likely to only temporarily slow the onset of the soft market, say most observers.

But the pricing discipline reinsurers have displayed generally is expected to continue, and many observers believe that even when rates do soften further, they will not go into the free fall that has characterized some previous soft markets (see story, page 18).

Overall, the U.S. reinsurance market is going to be "stable to moderate. We don't see it spinning down in any fashion," said Peter Zaffino, managing director for New York-based reinsurance intermediary Guy Carpenter & Co. Inc.

The market's outlook is "very favorable," said James Veghte, president and chief executive officer of Stamford, Conn.-based XL Re America. "The casualty market continues to be very strong. I think as long as we're in a relatively low interest-rate environment, it will remain very strong, because underwriting profits are mandated in an environment like that.

"The property market, without question, was slipping earlier this year, but while we haven't seen conclusive evidence yet, I think the hurricanes, without question, will slow down the decline," Mr. Veghte said.

The disciplined underwriting of the last few years is expected to continue, many observers say.

"The fundamentals continue to look strong in the segment," said John Ward, chairman of the Cincinnati-based Ward Group. "Companies continue to be more

See MARKET/page 12

Arbitration becoming new form of litigation in disputes

By DOUGLAS McLEOD

The opposing parties in a reinsurance arbitration usually don't agree on much, but they can probably get together on one thing: The arbitration process itself increasingly resembles the costly, drawn-out litigation it was designed to avoid.

Intended as a faster, less expensive alternative to the courthouse, arbitrations in the last several years have more frequently featured the kind of procedural battles, broad discovery demands, postponements and legal jockeying that made litigation so unattractive, arbitration experts agree.

> **Reinsurance 'arbitration is becoming like litigation in an inexorable fashion.'**
> *Robert M. Hall*

Arbitration more than a decade ago typically took three to six months from start to finish, with hearings lasting no more than a week, observers say. Today, the process takes at least a year and hearings can last two weeks or more, sometimes stretching over months, said David M. Raim, a partner with Chadbourne & Parke L.L.P. in New York who represents parties in reinsurance arbitrations and has written about the process.

Clifford H. Schoenberg, a partner with Cadwalader, Wickersham & Taft L.L.P. in New York, cited an arbitration process that began in 1996 and dragged through years of repetitive discovery proceedings, multiple hearings, a motion to overturn the final award and appeals, all costing many millions of dollars.

"Arbitration is becoming like litigation in an inexorable fashion," said Robert M. Hall, a former senior vp and general counsel with American Re-Insurance Co. and a certified arbitrator and umpire in Rockport, Maine.

Observers blame a host of factors.

See DISPUTES/page 26

Ranking of world's largest reinsurance intermediaries page 16

Little consolidation seen among reinsurers page 29

Reserving problems remain despite big additions page 32

Market: Underwriting discipline expected to continue

Continued from page 10

willing to give up premium than relax their tight underwriting standards. That's a good sign." Furthermore, "my sense is that the worst is behind us" as far reserve development is concerned, said Mr. Ward (see story, page 32).

Jack Snyder, chief marketing officer for Princeton, N.J.-based American Re-Insurance Co., agreed that underwriting discipline is likely to continue. "The early indications are there is a fairly high degree of resolve to maintain technical pricing and prudent underwriting," in light of many major companies' moderate to flat or even declining premium growth, he said. This "means in some cases, they're basically walking away from business, or not writing as much new business," said Mr. Snyder.

Mark P. Lescault, head of the divisional underwriting office at Swiss Re America Corp. in Armonk, N.Y., said, "Over the past few years, we've gone through a lot of corrections over the entire insurance industry, and I'm optimistic that we're going to maintain the underwriting pricing discipline needed to produce good returns."

Hurricanes Charley, Frances, Ivan and Jeanne "reminded people very graphically that the insurance industry and the reinsurance industry covers a lot of exposure, and we assume a good amount of risks," Mr. Lescault said. "We're in a position to handle that well, but to do that, we need to make sure we price our products adequately."

"We think the industry is reaching a period of stabilization," with the main factor the impact of improved pricing and terms and conditions, said Laline Carvalho, an analyst with ratings agency Standard & Poor's Corp. in New York.

Not everyone is sure that underwriting discipline is here to stay, though.

"All these people are saying, 'This is where the market is going to be at year end,'" said Mike Bungert, president of Chicago-based Aon Re Global. "What nobody has is any idea of what type of underwriting discipline—both on the insurance and reinsurance side—the market's going to maintain," which will drive what happens.

"It's going to be interesting to see, as we go through the next several quarters," whether reinsurers walk away if they cannot get the price they want, he said.

Signs of softening

Many say that the market clearly is softening.

"We think the market has definitely peaked, both in property as well as in casualty," said Ms. Carvalho. "We actually were a little disappointed—we thought casualty had another year to go."

"In theory, you would think that it would stay hard for some time, given the investment environment, but anecdotally, we're hearing that there is a softening" in certain areas, said Yvonne Bernard, managing senior financial analyst at A.M. Best Co. in Oldwick, N.J. "Market psychology doesn't change. People have short memories."

But Adam Klauber, managing director at Cochran Caronia Securities L.L.C. in Chicago, said the market will soften less next year than it has this year. "From a pricing perspective, you'll continue to see a downward trend throughout 2005, with some exceptions. But we think the downward trend will be somewhat less that it was in 2004," he said. This year "was more of a stair step down. Next year "will be more of a gradual bottoming, with the exception of property cat," where pricing is likely to rise because of the Florida hurricanes.

> **'Over the past few years, we've gone through a lot of corrections over the entire insurance industry, and I'm optimistic that we're going to maintain the underwriting pricing discipline needed to produce good returns.'**
>
> *Mark P. Lescault*
> *Swiss Re America Corp.*

"It feels like a transition year, rather than the year in which demand suddenly drops or increases, or a year in which rates suddenly plunge," said Chris Winans, senior property/casualty analyst with Lehman Bros. in New York. Furthermore, "it doesn't feel like there's the same level of competitive behavior as there is in the primary market, and I think that's because the reinsurers, a lot of them, have had to dig out of bigger holes."

Impact of storms

Observers are still evaluating the likely impact of the hurricanes on the market. With such a wide range of estimated hurricane losses, "it's difficult to say precisely what the impact will be," said XL Re's Mr. Veghte. If the ultimate losses are near the high end of the estimated range, "it's heavily into the reinsurance market" and likely to stop the slide in rates in both the primary and catastrophe markets.

But even if rates fall toward the low end, "property cat rates will at least stop sliding as a result of this," Mr. Veghte said.

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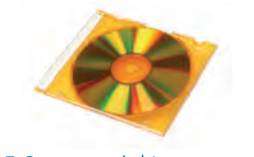
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PHOTO: REUTERS/CHARLES W. LUZIER

Reinsurers are evaluating the impact of this year's hurricanes, which damaged businesses including this Cocoa Beach, Fla., gas station.

Market: Underwriters expected to maintain market discipline

Continued from page 12

Ken Brandt, San Francisco-based president of GE Insurance Solutions' Americas reinsurance business, said the industry has been discovering the hurricane losses are worse than initial estimates.

"I know of more than several examples of significant differences between the reality of the losses coming in" and what models had initially indicated. And, unlike the situation after Hurricane Andrew or the World Trade Center losses, there is no loss of capacity or shift in the supply-and-demand equation, he said.

As a result, "you can almost hear companies thinking, 'Can I afford to go out there and push prices 20%?'" when their competitors may not be thinking the same way.

Steven Bolland, president of reinsurance intermediary Gill & Roeser Inc. in New York, said, "You would think that with losses like this, it would stabilize the market, even put significant pressure on the upside." But the market remains overcapitalized, "and preliminary indications are that some people are still pretty aggressively buying property reinsurance," he said.

In particular, some insurers are seeking third-event covers, which would be triggered when their initial reinsurance coverage and a reinstatement are exhausted, he said. "From what I'm hearing, some people are getting pretty aggressive in pricing those, which would lead you to believe they're going to be pretty aggressive when it comes to pricing renewal business as well. It's not a sign the market is hardening if people are aggressively competing for business now," he said.

> **'I think reinsurers will be looking to use the loss activity of 2004 as an opportunity to stall the decline in property reinsurance rates.'**
>
> *Tim Gardner*
> *Guy Carpenter & Co.*

"The impact of the four hurricanes was large enough that it will have some impact, it just has to," Mr. Ward said. However, he added, the storms will not "take a softening trend and completely turn it around into hardening trend." Florida's catastrophe fund, created after Andrew, "will have a tremendous impact in taking the edge off the impact of the hurricane."

"I think reinsurers will be looking to use the loss activity of 2004 as an opportunity to stall the decline in property reinsurance rates," said Tim Gardner, London-based managing director and head of the global property specialty practice at Guy Carpenter. However, "the market will continue to soften. It may be tempered a little bit by the loss experience, but generally most of the large property reinsurance purchasers have not been affected" by the losses, at least in terms of their reinsurance coverage.

Looking ahead

For now, observers generally expect reinsurers to continue to post strong results.

"It think that profitability will stay near current levels for a while. That's a pretty high level," said Todd Bault, a research analyst at Sanford Bernstein & Co. in New York.

Mark Rouck, a senior director at Fitch Ratings in Chicago, agreed. "Although there's pressure on pricing, it's going to remain technically adequate in such a way that companies should be able to generate decent earnings going forward."

"I'm positive on the segment," said Mr. Ward. "It's come through some tough years, but the last couple of years have been pretty good. I think it will continue to perform relatively well in the years and months ahead."

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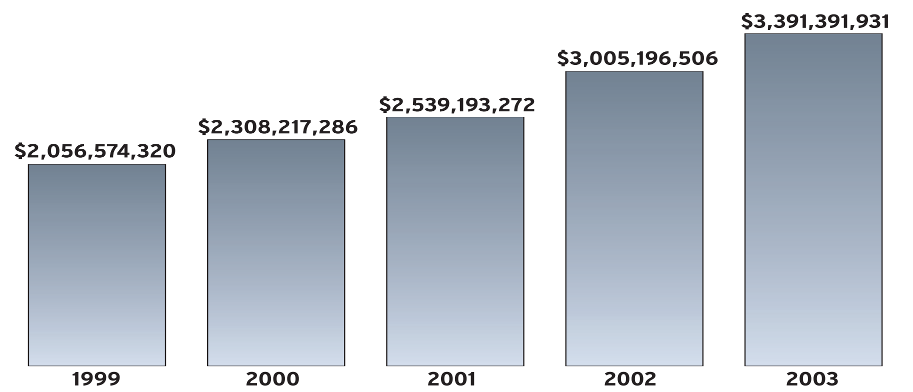
GROWTH IN REINSURANCE BROKERAGE REVENUES

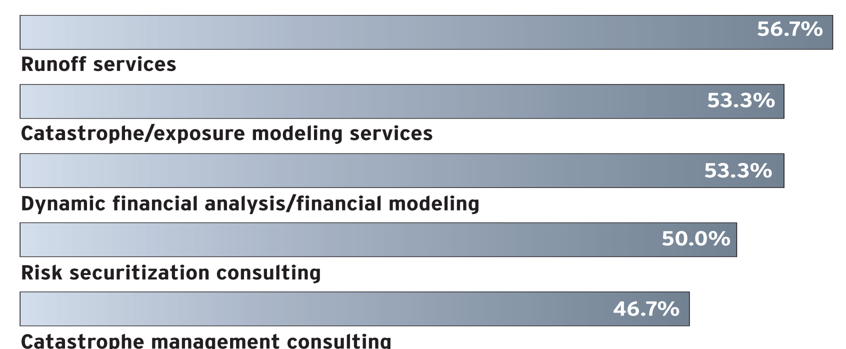
As a group, the world's 10 largest reinsurance brokers had a steady gain in revenues since 1999



Source: *BI* survey

SERVICES PROVIDED

Based on percentage of all listed companies offering services other than reinsurance brokering



Source: *BI* survey

World's largest reinsurance brokers

Ranked by 2003 gross revenues from reinsurance brokerage and related services*

Rank	Company/Address	Phone/Fax/Web site	2003 reinsurance gross revenues	2002 reinsurance gross revenues	% change	2003 employees	Principal officer
1	Aon Re Global Aon Center 200 E. Randolph St. Chicago, Ill. 60601	312-381-3040 Fax: 312-381-3045 *www.aon.com*	$945,000,000 [1]	$833,000,000 [1]	13.4%	3,100	Dennis Mahoney, executive chairman
2	Guy Carpenter & Co. Inc. 1 Madison Ave., Fourth Floor New York, N.Y. 10010-3658	917-937-3000 Fax: 917-937-3500 *www.guycarp.com*	$850,000,000	$740,000,000	14.9%	2,356	Salvatore D. Zaffino, chairman/CEO
3	Willis Re 10 Trinity Square London, EC3P 3AX England	44-207-488-8111 Fax: 44-207-488-8976 *www.willisre.com*	$513,000,000	$462,000,000	11.0%	1,110	John Pelly, chairman
4	Benfield Group Ltd. 55 Bishopsgate London, EC2N 3BD England	44-207-578-7000 Fax: 44-207-578-7001 *www.benfieldgroup.com*	$490,994,759 [2]	$449,635,145 [3]	9.2%	1,700	Grahame Chilton, group chief executive
5	Towers Perrin Reinsurance Mellon Bank Center, 1735 Market St. Philadelphia, Pa. 19103	215-963-7700 Fax: 215-963-7873 *www.towers.com*	$135,000,000	$110,000,000 [4]	22.7%	440	William H. Eyre Jr., managing director/CEO
6	JLT Risk Solutions Ltd. 6 Crutched Friars London, EC3N 2PH England	44-207-528-4000 Fax: 44-207-528 4500 *www.jltgroup.com*	$132,300,004 [2]	$140,175,738 [3]	-5.6%	NA	Dominic Collins, chairman
7	Heath Lambert Group Friary Court, 65 Crutched Friars London, EC3N 2NP England	44-207-560-3000 Fax: 44-207-560-3504 *www.heathlambert.com*	$107,255,788 [2]	$110,657,623 [3,5]	-3.1%	508	Adrian Colosso, group managing director
8	Cooper Gay (Holdings) Ltd. 88 Pine St., 26th Floor New York, N.Y. 10005	212-248-1150 Fax: 212-248-1181 *www.coopergay.com*	$85,000,000 [6]	$70,000,000 [6]	21.4%	450	Tobias C.D. Esser, group chief executive/COO
9	Arthur J. Gallagher & Co. Inc. [7] The Gallagher Center, 2 Pierce Place, Itasca, Ill. 60143-3805	630-285-3805 Fax: 630-285-4025 *www.ajg.com*	$77,710,000	$76,285,000	1.9%	369	David E. McGurn, president-specialty marketing and international division
10	BMS Group Latham House, 16 Minories London, EC3N 1AX England	44-207-480-7288 Fax: 44-207-374-5928 *www.bmsgroup.com*	$51,964,380 [2]	$43,873,000 [3]	18.4%	258	John Spencer, group chief executive

* Includes all reinsurance revenue reported through their holding and/or subsidiary companies. NA=Not Available 1 *BI* estimate. 2 Fiscal year ending 12/31/03 British pound=$1.6341. 3 Fiscal year ending 12/31/02 British pound=$1.5025. 4 2002 numbers are pro forma to include Denis M. Clayton & Co. Ltd. 5 2002 numbers are pro forma from 12/31/01 to 12/31/02. 6 Fiscal year ending 9/30. 7 Includes Arthur J. Gallagher Intermediaries (Bermuda) Ltd., Arthur J. Gallagher Intermediaries, Arthur J. Gallagher (UK) Ltd. and John P. Woods Co. Inc.

Source: *BI* survey

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Cedents to see little to no rate relief from reinsurers

Executives predict some softening, but modeling tools preventing slide in prices

By JUDY GREENWALD

Just how soft will the next soft market be?

Most reinsurers and reinsurance intermediaries believe that while rates will continue to moderate, the drop will not be precipitous. Closer scrutiny by rating agencies and other interested parties, as well as the technical tools now available to reinsurers to evaluate their exposures, will likely prevent rates from dropping as drastically as they did in the previous soft market, they say.

Observers say the ultimate insurance buyer will benefit from a more moderate, less volatile market.

Reinsurance prices likely will drop, but there will not be a rate free-for-all, said Jack Snyder, chief marketing officer for Princeton, N.J.-based American Re-Insurance Co. Reinsurers, he said, are "going to be able to avoid it."

The market will soften, and certain segments of the industry may report poor results, "but a wholesale, free-for-all deterioration in pricing to absolutely unacceptable, anemic levels that sustain themselves for a long period of time? The answer is 'no,'" said Mr. Snyder.

"There's more transparency now in the industry. There's more oversight from many parties, whether it be regulators, investors, analysts, rating agencies. The ability to obfuscate and hide and manage your results to look good—when the underlying dynamics are not—is just too difficult to sustain itself for any period of time," he said.

"We expect the market to soften, and we expect it to have an adverse impact on companies' financial strength, but we don't expect it to be of the same depth and duration of the last soft market," said Mark Rouck, a senior director at Fitch Ratings in Chicago.

Some observers maintain that tools now available to reinsurers will minimize the chances of a free fall in rates.

"We've developed an awful lot of tools that will put a natural brake on the marketplace before we reach the point where we did in the prior soft markets," said James Veghte, president and chief executive officer of Stamford, Conn.-based XL Re America.

The use of models for property business, while still not precise, "has developed significantly over the last 10 years, (which) allows us to know where we are in the market with a lot more clarity," he said. And on the casualty side, the damage sustained in the last soft market from prior-year loss reserves was so severe, "the market is really not going to reach the depth that it did" then, Mr. Veghte said.

> **'The ability to obfuscate and hide and manage your results to look good—when the underlying dynamics are not—is just too difficult to sustain itself for any period of time.'**
>
> *Jack Snyder*
> *American Re-Insurance Co.*

Tim Gardner, London-based managing director and head of the global property specialty practice at reinsurance intermediary Guy Carpenter & Co. Inc. said, "The reality is, reinsurers are much more technical in the way they analyze the business than they were in '92, as rates spiked dramatically and started to fall off just as dramatically."

Now, reinsurers "have tools in place to measure exposure (and are) much less reliant on the market cycle," he said. "We're going to see much less dramatic swings, at least from a property perspective, in the way prices move relative to cycles."

Bill Adamson, chief executive officer of Norwalk, Conn.-based reinsurance intermediary Carvill America Inc., pointed to new corporate governance rules as another factor that will influence the shape of the softened market.

The 2002 Sarbanes Oxley Act, which subjects corporations to numerous new reporting and auditing requirements, "really precludes (companies) from knowingly underreserving," he said. Companies are spending a lot of money to be in compliance with the act, and the "buck stops with the CEO," he said. As a result, Mr. Adamson said, "I'm not sure you're going to see some of the same habits we've seen in the past."

The movement of capital will also be a factor, said Patrick Denzer, president and CEO of reinsurance intermediary John B. Collins Associates in Minneapolis. "Capital flows in and potentially out of the market much more quickly than it has in

See RATES/page 20

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Rates: Major relief unlikely

Continued from page 18

previous cycles, which I think lends itself to a greater level of consistency."

Memory will play a role as well, said Mark P. Lescault, head of the divisional underwriting office at Swiss Re America Corp. in Armonk, N.Y.

"I think people remember the pain of coming out of the soft market, and I think that will help maintain an appropriate level of discipline."

However, William H. Eyre Jr., chief executive officer of Philadelphia-based intermediary Towers Perrin Reinsurance, said while "I don't think it'll get that bad in reinsurance," you cannot really disconnect what happens in the reinsurance market from activity in the primary market. He noted that reinsurers often base their rates on primary insurers' prices.

John Berger, president and CEO of Chubb Re Inc. in Bernardsville, N.J., said it is too early to say whether there will eventually be a pricing free-for-all.

"You just hope people have learned coming out of the '97-2001 market," he said. "People say they are going to be disciplined. You just look at the carnage from those years, so you hope it doesn't go into free fall, but our business periodically does that." Next year, he added, "is the test."

Risk managers will ultimately benefit if the next soft market is moderate, said John Ward, chairman of the Cincinnati-based Ward Group. "It would appear to be bad in the short term, because it might mean that rates are higher. But I think that it's good for the insurance buyer in the long term, because it keeps more discipline in the process, and with discipline comes stability of prices for the long term."

Reinsurer portfolios weighted in bonds

By JUDY GREENWALD

Reinsurers tend to invest more heavily in bonds and less heavily in equities than do their primary insurer counterparts, in part because of the often longer-term nature of the reinsurance business.

According to the Cincinnati-based Ward Group, for the period from 1999-2003, 75.5% of reinsurers' invested assets were in bonds, compared with 65% for the overall industry. And reinsurers had only 12.6% of their assets in stocks, compared with 22.6% for the overall industry. The remaining assets are accounted for by mortgage loans, real estate, cash and cash equivalents and other miscellaneous assets.

Reinsurers "have enough risk on the liability side," said Yvonne Bernard, managing senior financial analyst with Oldwick, N.J.-based A.M. Best Co. "You usually then don't want to take risk on the asset aside, on the investment side," so investments tend to be high quality.

Reinsurers' investment strategy enables the segment "to be more effective at paying their claims," said Ward Group Chairman John Ward. "Stocks are generally perceived as a riskier asset than bonds."

'You try and match the maturity of your investments in line with your payout pattern. It's a balancing act, because you're never quite sure what your payout pattern is going to be.'

Steven Bolland
Gill & Roeser Inc.

In addition, if the underwriting of the bond portfolio is matched to the reinsurer's liabilities, "that should enhance the ability to make claims payments on a timely basis," he said.

"You try and match the maturity of your investments in line with your payout pattern," said Steven Bolland, president of reinsurance intermediary Gill & Roeser Inc. in New York. "It's a balancing act, because you're never quite sure what your payout pattern is going to be."

Princeton, N.J.-based American Re-Insurance Co. has a $13 billion investment portfolio, of which $1 billion is in foreign assets, most of which is to cover liabilities associated with American Re's foreign operations, said Senior Vp Wolfgang Engshuber. Of the remaining $12 billion in assets, $11 billion is in fixed-interest securities, and $1 billion in equities, he said.

American Re's investment strategy "very much depends on the underlying business," said Mr. Engshuber. Because the reinsurer writes a significant amount of casualty business, which has a long tail, it invests accordingly, he said. But "we also obviously look into what our potential short-term liquidity needs" are to ensure that in the event of, for instance, a series of hurricanes, it has sufficient liquidity to pay claims without have to recognize significant investment losses, he said.

"You could argue that we should have a higher percentage in equities, but obviously equities have much more volatility and therefore, for us, surplus protection has kind of put the cap on our equity exposure."

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Reinsurers resisting cedents' push for collateral

But reinsurance buyers' interest in collateralization pacts growing amid security concerns

By JUDY GREENWALD

Many reinsurers are rebuffing cedents' efforts to include collateralization provisions in their reinsurance contracts, and some are even walking away from business over the issue.

While their language varies, these provisions generally call for the reinsurer to provide collateral, such as letters of credit, to cedents if the reinsurer's rating falls below a certain level. Interest in the provisions has grown of late because of the spate of reinsurer rating downgrades seen during the last few years.

Cedents' success in obtaining such arrangements may hinge both on the desirability of their business and the strength of the reinsurer, say observers, who note highly rated reinsurers in particular are generally reluctant to agree to the provisions.

Collateralization is an issue of "who's going to blink first," said Jack Snyder, chief marketing officer for Princeton, N.J.-based American Re-Insurance Co., which refuses to collateralize its business.

Although the pace of rating downgrades is widely expected to slow, more cedents are asking for these provisions.

"I think it's much more common for companies to ask for collateralization," said Patrick Denzer, president and chief executive officer of reinsurance intermediary John B. Collins Associates Inc. in Minneapolis.

"There are a number of ways to approach that, and there doesn't seem to be yet a standard way to do that, but it is certainly something that is much higher on people's radar screen as a potential way to secure their credit risk," said Mr. Denzer.

Some observers, though, contend that the basic premise behind collateralization provisions is flawed.

"We've gone on the record as being not particularly impressed from a credit-rating standpoint with the value of some of the protections that ceding companies are getting with these termination clauses," said Steven J. Dreyer, managing director at rating agency Standard & Poor's Corp. in New York.

There is a "real likelihood" that the provisions "won't provide much benefit when everyone tries to cash in on them at the same time, which typically is the case. So they provide comfort when they are not needed, but when they are needed, they may not be worth very much," Mr. Dreyer said.

"I don't think it's an effective answer" to cedents' concerns about the security of their reinsurance contracts, said Ken Brandt, San Francisco-based president of the GE Insurance Solutions' Americas reinsurance business, which will not agree to include the clauses in its contracts.

> **Putting collateralization provisions into reinsurance contracts 'isn't a great solution...I think people being more careful about whom they're doing business with is a solution.'**
>
> *John Berger*
> *Chubb Re Inc.*

"Some of the more objectionable forms of these clauses create artificial rating cliffs" that could drive a reinsurer out of business if its rating drops below a designated level and the clauses cover a large portion of its portfolio, said Mr. Brandt. In such cases, "you've forced what could be a viable market completely out of the market by having these triggers," he said.

Furthermore, he said, the default rate among reinsurers rated BBB or higher is extremely small. Given those factors, "there are better ways to get a comfort level with the financial security of your reinsurers," Mr. Brandt said.

"It isn't a great solution," said John Berger, president and CEO of Chubb Re Inc. in Bernardsville, N.J. "I think people being more careful about whom they're doing business with is a solution," he said.

"If you don't trust your reinsurer, you should find another reinsurer," said Steven Bolland, president of reinsurance intermediary Gill & Roeser Inc. in New York.

"I just can't see reinsurers willing to (use collateralization) on a huge basis," he said. They are saying, "If you don't trust me, don't use me. End of story."

"It's very much on an individual basis," said Mike Bungert, president of Chicago-based reinsurance intermediary Aon Re Global.

"I don't think you'll find many reinsurers saying they'll do it all the

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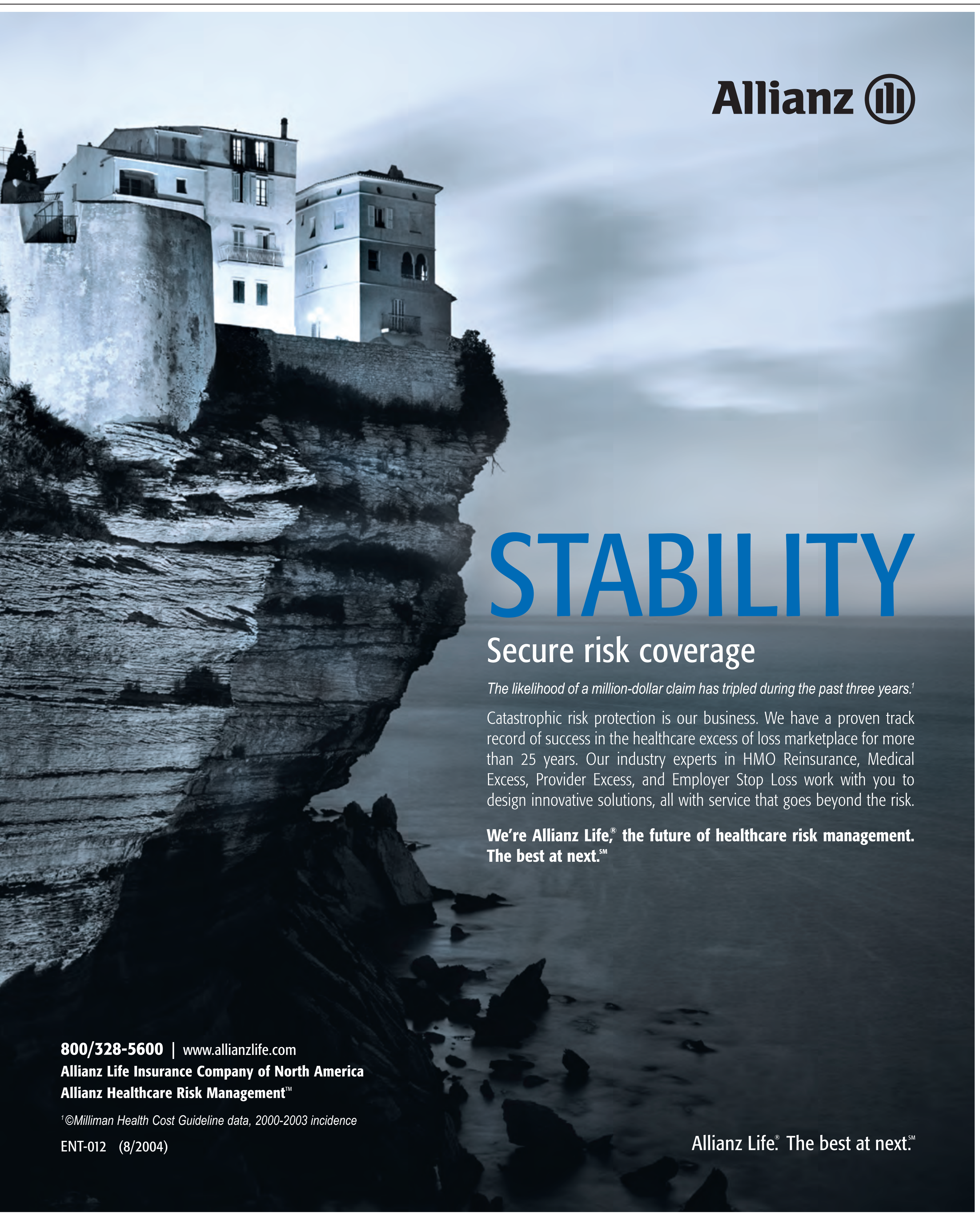

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Collateral: Many reinsurers resisting client demands

Continued from page 22

time, or they won't do it at all. It's going to depend on the relationship," he said.

"You're having some do it, but it's really not turning out to be a major trend," said Adam Klauber, managing director at Cochran Caronia Securities L.L.C. in Chicago. Casualty companies in particular are showing a preference for higher-rated reinsurers, "but they're not making make-or-break decisions" based on whether reinsurers will put up collateral.

"It's probably more prominent with the lower-rated reinsurers," said John Andre, vp-property/casualty division at Oldwick, N.J.-based A.M. Best Co. "Brokers in many regards are pushing (the clauses), or recommending that to their clients."

Reinsurers, for their part, say they are unhappy with collateralizaton provisions.

American Re's Mr. Snyder said: "We basically have a fundamental business posture that we do not think it makes good business sense to collateralize our contracts, and that's because we have a reputation, we have a strong balance sheet, we have strong financial strength ratings.

> **'Brokers in many regards are pushing (collateralization clauses), or recommending that to their clients.'**
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> *John Andre*
> *A.M. Best Co.*

"We feel that is what should be valued and used by our buyers, by our clients, to determine whether they should see collateralizing in their contracts or not," said Mr. Snyder.

When American Re has been asked to use collateralization provisions, "we have declined, and in some cases we have lost some business as a result, but it's been modest," said Mr. Snyder.

Mark P. Lescault, head of the divisional underwriting office at Swiss Re America Corp. in Armonk, N.Y., said, "We don't believe strongly rated reinsurers should be having to provide collateral up front, if you will," and Swiss Re has not done so except in jurisdictions where the collateral is required by law.

The reinsurer has not lost any business because of its policy because "reinsurers with the strong balance sheet are being sought," Mr. Lescault said.

"We resist (collateralization) with all our willpower," said Chubb Re's Mr. Berger.

James Veghte, president and CEO of Stamford, Conn.-based XL Re America, said, "we're responding case by case" to clients' requests.

He added, though, that "companies such as ours, with strong ratings in the spectrum of the ratings scale" have an advantage in the marketplace.

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Collateral: Many reinsurers resisting client demands

Continued from page 22

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Brokers: Does size of firm really matter?

Continued from page 10

you are as a ceding company, the more leverage you have and the better off you might be to take advantage of the worldwide presence of…one of the bigger players. And if you're a smallish company…you're likely to get more attention from the smaller brokers that maybe have five, 10, 12 people in the shop," he explained.

Indeed, Steven Bolland, president of intermediary Gill & Roeser Inc. in New York, said that one of the advantages of dealing with a small independent reinsurance brokerage rather than a larger one is that clients deal with the principals of the firm all the time.

"With the larger brokers, you might see the principal to cut the deal, and then suddenly you've got a bunch of juniors and a team of people who are suddenly your new account handlers and are looking after your business," he said. "When you're a smaller independent, you tend to have access and day-to-day contact with the senior guys."

Patrick Denzer, president and CEO of John B. Collins Associates Inc. in Minneapolis, agrees.

"We try to maintain senior broker involvement with all of our clients, which is really very essential," he said. "At its core, a reinsurance broker really needs to talk about the client's exposures and the client's business and the client's risk management/insurance needs. And the only way to really be able to talk intelligently about the client is to understand the client at a very in-depth level, and you only get that with experience," he said.

Mr. Denzer said Collins' status as a midsize, privately held and independent firm also benefits its clients. "We are not publicly traded, we don't have outside shareholders, so we can really provide advice to our clients without any external pressures, whether they be from the public market or from a parent company," he said.

Reinsurance brokerages say, however, it's not just about the various advantages associated with size—whether small or large—that ceding companies should look at when choosing a broker. Other key distinguishing features include specialized services the companies offer.

Willis Re Inc., for example, will be launching an initiative with its Jan. 1, 2005, reinsurance renewals called "contract certainty," that will set the firm apart from its competitors, according to Peter C. Hearn, president of U.S. operations in Philadelphia.

Under this initiative, the contracts reinsurers sign on Jan. 1 will be the wording used, he said.

"This is an attempt to expedite a process which up to now can take as long as nine months to execute," Mr. Hearn said.

Peter Zaffino, managing director of New York-based Guy Carpenter & Co. Inc., said one of the key differences he sees in the market is the depth of resources brokerages can offer in terms of modeling capabilities.

Two proprietary models that Guy Carpenter recently developed—one for directors and officers liability risks and the other for workers compensation risks—are "total differentiators," he said. Guy Carpenter also will soon be launching a new employment practices liability model that will measure the likelihood of certain types of EPL lawsuits, he said. "We think it's going to be a very important tool for our clients" as well as a way to set Guy Carpenter apart in the marketplace.

But Mr. Barile contends that while having various technological and analytical services may have been a distinguishing feature in the past, it's not so much anymore, he contends. "Everybody is pretty well predicated on the ability to provide that kind of modeling expertise," whether it's outsourced or offered on a proprietary basis.

As many reinsurance brokers point out, when it comes to the various analytical and modeling tools brokerages provide today, the real distinction lies with how each firm uses the information. And that comes down to the true differentiation between the firms—their people.

"The people ultimately differentiate firm to firm. The top four (reinsurance brokerage) firms to a greater or lesser degree have proprietary products, but they are only as good as the people who use them, who can interpret them and then provide a strategy to assist the client or prospect," Mr. Hearn said.

"It really comes down to the ability to bring value to the client through technical and analytical tools and really being able to use them intelligently and actually delivering the product to the client," agreed Mr. Denzer of John B. Collins.

"Oftentimes, some intermediaries are unable to really perform a detailed level of analysis for their clients or a meaningful cross section of their customers. If it becomes just a template analysis that is done, that really provides a very limited amount of value. So we fo-

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Gill & Roeser Inc.

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Brokers: Does size of firm really matter?

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Brokers: Does firm size matter?

Continued from previous page

cus on being able to have enough resources in our analytical services area to provide meaningful and analytical work for all of our clients," he said.

"Our business is all about people," said Rod Fox, CEO of Benfield Group Ltd.'s North American operations in Westport, Conn. "It's the creativity and the energy of our people that ultimately differentiates us. We spend a lot of time focusing on that."

Mr. Fox noted that just as important as the people is the culture in which they work. "It's about building a culture around a central premise and our premise is: Our job is to make our customer more successful. It's not just placing reinsurance and filling orders," he said. "It's, how do you make that customer more successful all the time?"

Guy Carpenter's Mr. Zaffino noted that one of the differentiators of his firm is its ability to have key employees serve as resources for its customers and potential customers.

Around the world, Guy Carpenter has a number of specialty practices set up to support brokers and clients, he explained.

"So we'll have an individual who heads up, say, our workers comp specialty practice, and it is that individual's job to provide creative ideas, solutions, market intelligence, best practices in terms of presentations and interaction with (Guy Carpenter's modeling tools), all in support of the brokers," Mr. Zaffino explained. "So that individual's full-time responsibility is to be a resource, not to manage accounts. And we've put our best people in that space…and it's really differentiated us in our presentations in terms of the depth and breadth of what we bring to our clients."

Disputes: Arbitration losing some appeal

Continued from page 10

Reinsurance disputes have steadily become higher-stakes affairs, involving more money and, in many cases, parties with no ongoing business relationship and greater mutual hostility.

Lawyers, some contend, have also "hijacked" the process, importing litigation tactics such as voluminous deposition and document production requests that slow proceedings and pile on costs.

Arbitrators and umpires, meanwhile, have been reluctant to curb discovery or limit the scope of arguments out of concern that one side or the other might claim denial of due process and try to vacate any eventual award in court.

Some reinsurers have become disenchanted enough with the process that they have removed arbitration clauses from some contracts or limited arbitration only to disputes involving smaller amounts of money, arbitration experts say.

Still, many in the field say that arbitration remains a better "business solution" to reinsurance disputes than litigation and that all parties need to take steps to improve the process.

Those steps include limiting discovery proceedings, encouraging lawyers to narrow their focus to the most relevant issues, streamlining hearing procedures and—in cases where one side pursues meritless claims—awarding attorney fees to the winner, arbitration experts say.

"The process is working, but it needs more active involvement on the part of the panel," said Ronald A. Jacks, a certified arbitrator and umpire and a founding director of ARIAS-U.S., a Mount Vernon, N.Y.-based nonprofit formed to promote arbitration. "Panels need to impose more discipline on the process," he said.

"It's a legitimate criticism to say that some but not all reinsurance arbitrations are turning into litigation by another name," Mr. Jacks said. "But I think that's the exception, not the rule."

A changed approach

Years ago, arbitration was an informal, fast and inexpensive way to resolve routine disagreements between long-term business partners that had an incentive to settle things and move on.

That has changed as the character of the parties' relationships has changed, observers say.

Many arbitrations now involve parties with no ongoing business relationship. Ceding insurers in runoff, for example, have accounted for a growing number of arbitrations. Many bitter disputes have arisen from the huge losses that life insurers suffered writing the accident and health "carve-out" portion of workers compensation programs; those life insurers no longer write carve-out risks and aren't likely to do business again with their arbitration opponents.

"Some of the glue that holds arbitration together is missing," said Ronald S. Gass, an arbitrator and president of The Gass Co. Inc., a Weston, Conn.-based consultant. "It's nice to have parties that are motivated to resolve their dispute because they have an ongoing business relationship."

The disputes themselves are also bigger, involving tens or even hundreds of millions of dollars and enormously complex factual and legal issues, others note.

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Disputes: Alternative to litigation losing some appeal

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The carve-out debacle "is a perfect example of disputes that no one should have expected to be addressed speedily and inexpensively," said James I. Rubin, a partner with Butler, Rubin, Saltarelli & Boyd L.L.P. in Chicago.

Meanwhile, lawyers have increasingly applied the tactics of litigation to arbitrations, and several experts cite lawyers' discovery demands as the biggest obstacle to efficiency.

"The entire reinsurance arbitration process has been hijacked by the lawyers," Mr. Schoenberg said.

Robert M. Huggins, an arbitrator and reinsurance consultant in Basking Ridge, N.J., noted one case in which a party wanted to take 27 depositions.

"If you really need 27 depositions, how well have you thought about your case?" Mr. Huggins asked, saying the panel ultimately allowed 12 depositions to each side.

The extent of the problem can depend on the issues: If a dispute involves business handled by a managing general agent or third-party administrator, for example, "you're off to the races" with demands for audits, document production and other discovery, Mr. Hall said.

E-mail has added to the burden, creating a huge new category of discoverable material that can be expensive and time-consuming to retrieve, Mr. Raim added.

Lawyers can also use massive discovery demands as an offensive tactic, "intended mainly to harass the other side," Mr. Gass pointed out.

Arbitration panels are often reluctant, though, to curtail discovery because lawyers may argue that they were denied due process and use that argument as grounds to overturn an award in court, Mr. Jacks said.

"I've seen so many arbitrations that should last three days and that last three weeks because the panel is reluctant to do anything to risk the lawyers crying about their due process rights," Mr. Schoenberg said.

Arbitrators are similarly loath to grant the equivalent of summary judgment on certain issues before a hearing, a tendency that also prolongs the arbitration process, experts say.

A variety of other factors, meanwhile, has contributed to slow pace and rising expense of arbitrations.

One is the growing difficulty of scheduling hearing dates that busy panel members and lawyers can all agree on. The most sought-after arbitrators are often booked a year or more in advance, observers note.

A related problem is that a relatively small number of arbitrators handles the majority of cases, making scheduling less flexible.

While the ARIAS-U.S. Web site lists scores of ARIAS-certified arbitrators and umpires, many relative newcomers on the list complain that they have trouble winning arbitration assignments, experts agree.

The problem is further compounded by a growing tendency of lawyers to request last-minute postponements—sometimes as a tactic to delay or to force a settlement—that automatically trigger a new round of scheduling difficulties, Mr. Jacks added.

Nevertheless, arbitration experts cite a number of actions participants can take to improve the process.

Panel members, for example, should get tougher about limiting unreasonable discovery requests and focusing lawyers' attention on the issues most germane to the dispute, most agree.

"It is up to the panels to decide what is relevant and not to allow fishing expeditions," Mr. Raim said.

Arbitrators could streamline hearings in other ways, including by taking direct testimony of witnesses in writing beforehand and using hearing time only for cross-examination.

Panels could also discourage lawyers from wasting their time on frivolous arguments by awarding fees and costs to the winning party, a tactic that some panels have already employed, several experts agree.

"There is definitely a feeling among some parties that there needs to be some type of penalty put in to limit disputes (to) a legitimate claim on the one side and a legitimate defense on the other," Mr. Raim observed.

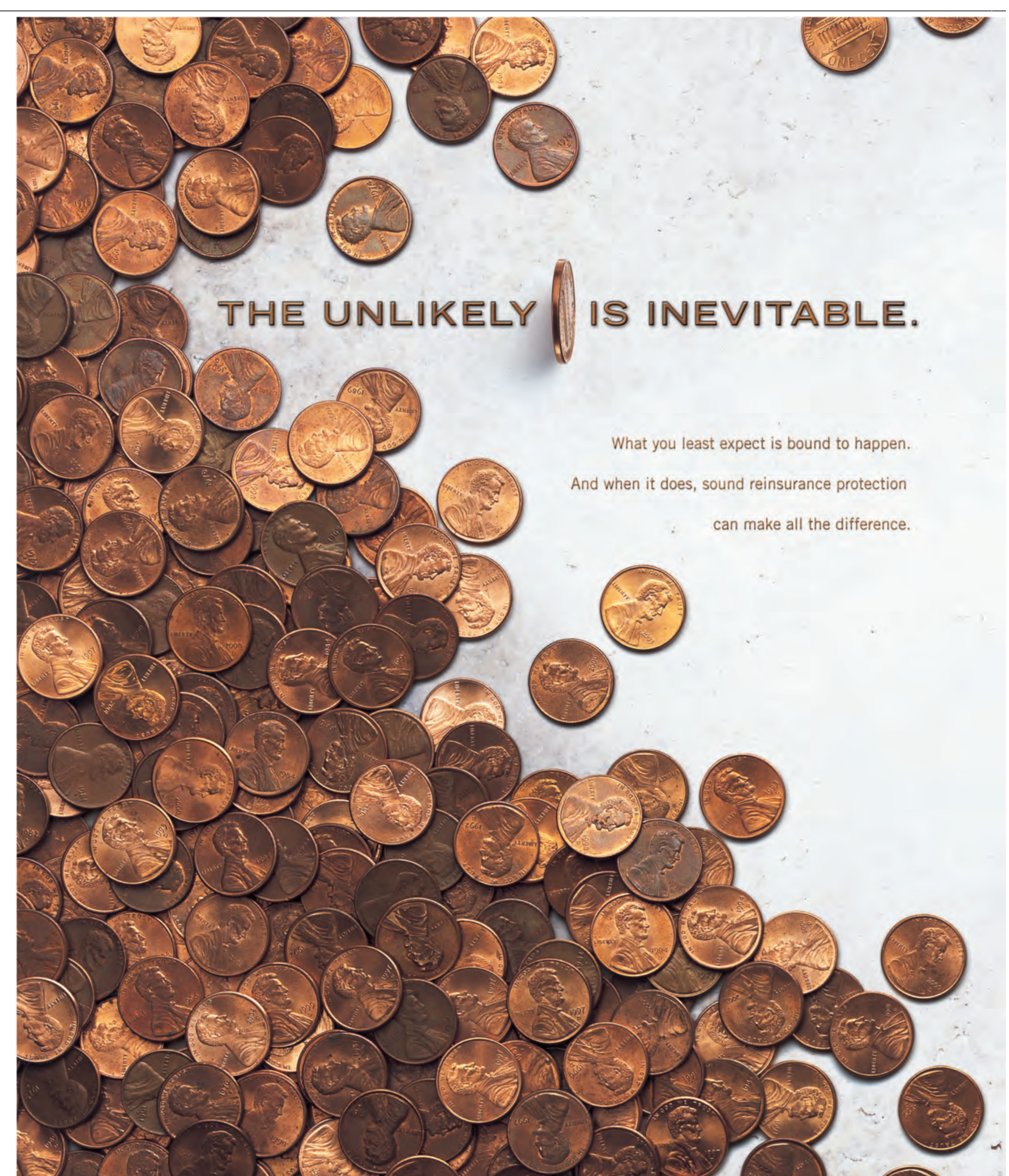
Whether the situation will improve—and arbitrations will move toward their original goal of serving as a smoother, less costly alternative to litigation—remains a matter of debate.

"We are beginning to see panel members much more active from the outset in managing the process," Mr. Rubin said. "That is a trend that I think is a really good one."

Arbitrations retain their original advantage of allowing disputes to be heard by industry experts rather than judges or juries unfamiliar with reinsurance customs, he added.

Others sound less hopeful.

"The inertia is so strong in favor of widespread, unhampered deposition discovery that it's difficult to see it changing," Mr. Schoenberg said.



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Cedents can expect to have choices in reinsurance

By MARK A. HOFMANN

Reinsurers are resisting any urge to merge, and there's no reason to expect that to change in the near future, provided the marketplace remains profitable, market observers say.

Instead of growing bigger through acquiring other entities, other approaches—such as setting up offshore facilities, finding new means of capitalization and simply buying attractive books of business—make more sense, say the market watchers. Through such growth avenues, reinsurers avoid the nagging worries over legacy issues that accompany merger and acquisition deals.

"The legacy issues have been so paramount in the (property/casualty) sector, it's really preventing any significant amount of transactions right now, obviously including the reinsurers," said Peter Roth, head of insurance investment banking for Keefe, Bruyette & Woods Inc., a New York-based investment bank specializing in the financial services sector.

A key reason for the lack of consolidation is that the market is already highly concentrated.

"When you think about the possible buyers, it is important to remember that the reinsurance marketplace is dominated by a handful of elephants," said John A. Wicher, principal of John Wicher & Associates Inc. in San Francisco.

"That was not the case 10 years ago, when there were good, midsize companies that are now gone. The larger reinsurers are already seeing almost every reinsurance placement. Why buy what you already have access to?" said Mr. Wicher, pointing out that large reinsurers already enjoy such advantages as geographical reach and technical expertise.

And the situation isn't likely to change soon, said Robert Hartwig, chief economist for the Insurance Information Institute in New York.

"I think that there will be very little M&A activity among major reinsurers for the next several years," Mr. Hartwig said.

One factor that will curb consolidation, he said, is a "morbid fear over acquiring or assuming 'skeletons in the closet,'" including reserve deficiencies, both known and unknown. Reinsurers also fear that primary insurers are losing underwriting and pricing discipline, increasing the likelihood of burning through primary retentions while, at the same time, diminishing income from ceded premiums, he said. There are also concerns over buying into a softening market and the fact that only weakened companies may offer themselves up for sale.

A change in market direction, however, could accelerate M&A activity, said Bob DeRose, an assistant vp with A.M. Best Co. in Oldwick, N.J.

"As long as (the reinsurance market) remains profitable, I don't think you're going to see a vast increase in M&A activity. If it softens materially, then some of the current investors may look for an exit strategy that may include M&A," he said.

'The legacy issues have been so paramount in the (property/casualty) sector, it's really preventing any significant amount of transactions right now, obviously including the reinsurers.'

Peter Roth
Keefe, Bruyette & Woods Inc.

"We are seeing a number of reinsurers that have gone to their boards asking for the authority to buy shares back, which is one method of returning capital to investors without forcing companies into merger," said Mr. DeRose.

"We believe it is likely that merger activity could pick up as top-line (growth) slows, particularly among the new Bermuda companies," said Bill Yankus, a managing director at Fox-Pitt Kelton Inc. in New York.

However, Mr. Roth said that "there is a lot of discussion about consolidation among the Bermuda companies; I think the jury is still out as to whether that will happen.

"A lot of them really aspire to grow into companies with businesses in the U.S. and Europe," like ACE Ltd. and XL Capital Ltd., he said.

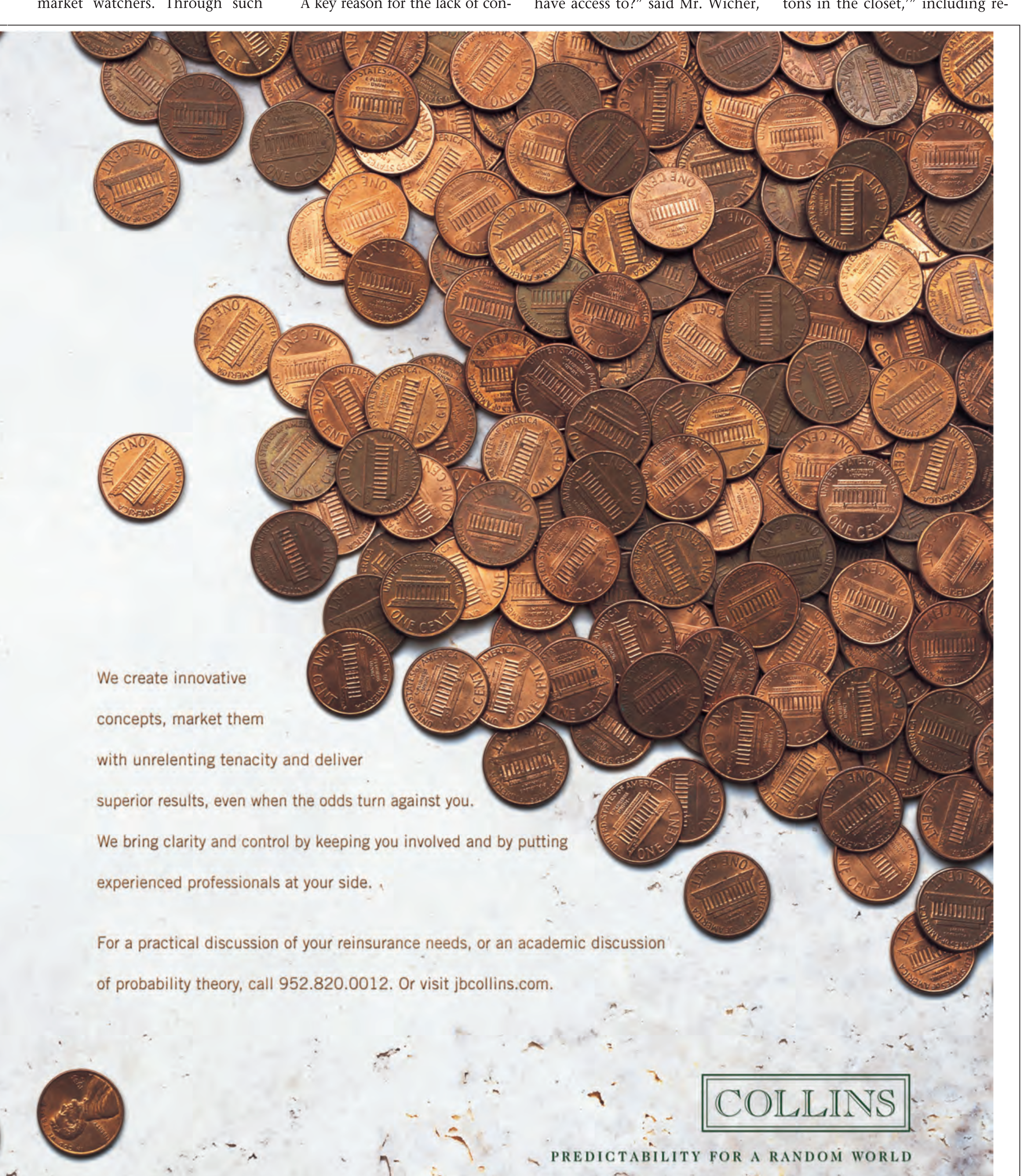
Other growth strategies

Instead of outright M&A, reinsurers will look to different ways to gain strength, said several observers.

"What we do see is capital activity taking place within the segment that may be somewhat below the M&A radar," said John L. Ward, chairman of Ward Group in Cincinnati.

"It would not necessarily mean it's leading to fewer players, but it would be a sign that some of the bigger players...are shoring up their capital commitment so they can recommit to the segment," he said. "It's truly a global market, and

See DEALS/next page



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Deals: Reinsurer consolidation won't limit choices

Continued from previous page
there's been significant fresh capital coming in to the Bermuda reinsurance segment."

Some U.S. companies are also raising capital through secondary capital offers and debt issues. And with interest rates continuing at historically low levels, debt issue is a cost-effective way for reinsurers to boost capital, Mr. Ward said.

Forming new offshore facilities is another alternative to acquiring existing reinsurers, said Mr. Wicher.

"For the best-capitalized new participants, forming fresh offshore facilities is less problematic. As we have seen, these newly capitalized companies can also attract top talent," said Mr. Wicher.

"Given the right environment, with a fresh-start company free of any past sins, why would you deploy your capital on an acquisition here in the (United States) or Europe?" said Mr. Wicher.

Observers disagree on how prevalent buying books of good business will be as an alternative to outright acquisition.

"I believe most of the action will involve picking up select books of business. This mirrors what is happening on the primary side, with insurers buying renewal rights, rather than seeking ownership of the company," said III's Mr. Hartwig. He cautioned, however, that he believes that some of the reinsurers formed in late 2001 and 2002 still might be absorbed into larger companies.

Buying books of business "appears to be the preferred way of augmenting a reinsurer's business position," said Best's Mr. DeRose. Such an approach allows them to diversify quickly and efficiently, he said. In addition, it avoids complications associated with legacy liabilities. "Generally, they just purchase the renewal rights; they don't take any existing liability," he said.

Mr. DeRose cited as examples of this approach Endurance Specialty Holdings Ltd.'s 2002 acquisitions of a catastrophe book of business from LaSalle Re Ltd. and a casualty book of business from HartRe Co. L.L.C. More recently, Endurance acquired a surety book of business from XL Reinsurance America Inc. (*BI*, Oct. 4).

Mr. Ward, though, said he expects reinsurers' growth efforts to involve other approaches.

"I'm not expecting that there would be book of business transactions—I don't see a lot of that on the horizon. The main thing is companies raising new capital through equity and debt issues," he said.

Munich Reinsurance Co., Berkshire Hathaway Inc. and Hannover Reinsurance Co. all have raised capital in recent months through debt issues, said Mr. Ward.

Despite Converium Holding A.G.'s recent decision to close its U.S. operations following reserve boosts and ratings downgrades, observers don't see any signs that others will follow suit, particularly given the size of the U.S. marketplace.

"The U.S. market is large enough and important enough that the major players will continue to hang tough on the U.S. market," said Mr. Ward. The top tier of international reinsurers is particularly unlikely to withdraw, he said.

'I believe most of the action will involve picking up select books of business. This mirrors what is happening on the primary side, with insurers buying renewal rights.'

Robert Hartwig
Insurance Information Institute

"I don't envision anyone else withdrawing from the U.S. unless they're downgraded below A-," said Mr. Roth.

"When you look at the reinsurers that remain in the U.S. marketplace today, they are primarily global reinsurers, and the U.S. is the largest market. If they want to continue to have a global reinsurance franchise, they're going to have to be in the U.S.," said Mr. De Rose.

Recent catastrophe losses, including those from the quartet of hurricanes in the United States, aren't expected to have an impact on consolidation activity, observers note.

"I don't see that series of events driving M&A activity in a big way," said Mr. Ward. "I do see the chain of events having potential impact on the softening trend that was under way. The impact is relatively isolated to several companies. While the insured losses are about $20 billion to $25 billion for the industry, the impact will be softened somewhat by the role of the Florida catastrophe fund, which will probably absorb 20% to 30% of those insured losses—in the $5 billion to $7 billion range."

Looking ahead, Fox-Pitt Kelton's Mr. Yankus said that the impact of legacy issues—currently a major factor hindering consolidation—could fade over time.

"Legacy issues will always hamper consolidation activity, but it will not stop the activity," he said. "The further we get away from legacy years, the profitability of the more current years and future market-share growth are the most important factors the buyers would consider," he said.

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Reinsurers' reserves improve but big hole remains

Large reserve additions, improved techniques help whittle deficiency

By CAROLYN ALDRED

Reinsurers still have massive holes to plug in their casualty reserves, although they may be through the worst of their underreserving problems, industry experts agree.

The large reserve increases by major reinsurers over the past several years have gone some way to alleviating their reserve problems, but the industry as a whole is still underreserved by billions of dollars, according to some estimates.

Still, improved reserving techniques and a general willingness by reinsurers to deal with reserve issues as they arise could help reinsurers address the problem, some observers say.

The past few years have seen several significant reserve boosts among major reinsurers, in some cases resulting in ratings downgrades.

Most recently, Converium Holding A.G. in July said it was bolstering its reserves by $384.7 million, principally because of U.S. casualty business written between 1997 and 2001. The Zug, Switzerland-based reinsurer has since placed its U.S. operations in runoff, following ratings downgrades that took it out of the A range.

In 2002, Munich, Germany-based Munich Reinsurance Co. added around $2 billion to the reserves of its American Re-Insurance Co. unit to address deficiencies in various liability reserves, including those for asbestos claims. In addition, Paris-based SCOR S.A. and Kansas City, Mo.-based Employers Reinsurance Corp. also boosted reserves that year following assessments of their reserving position.

"Reinsurers took significant hits on their reserves in 2002 and 2003, particularly for U.S. casualty business and asbestos," said Chris Waterman, a senior director of Fitch Ratings in London.

"We think that reserve deficiency decreased in 2003 and will reduce again this year. But the industry remains underreserved and has a way to go," he said.

In recent years, as reinsurance rates have increased, reinsurers have managed to strengthen their reserves, but Robert DeRose, an assistant vp with A.M. Best Co. in Oldwick, N.J., estimates that the reinsurance industry still has "a $7 billion hole that needs to be plugged."

"But it is 10 times harder for a reinsurer to assess its reserve situation than for a primary underwriter," said Mr. DeRose, because reinsurers are farther removed from the underlying claims.

"Reserve adjustments are part of the reinsurance game. Underwriters of long-tail business have to make certain assumptions when assessing reserves and those assumptions may end up being too conservative or too aggressive," said Clement Booth, chief executive officer of reinsurance broker Aon Re International in London.

Reinsurers were "suddenly faced with having to make massive reserve adjustments" as a result of falling interest rates and stock markets, rapidly deteriorating claims and a period of poorly priced underwriting in the late 1990s, said Mr. Booth.

A bull market had allowed reinsurers to "significantly underprice" their product for a long time, he said.

But a continued and prolonged period of low investment return will probably result in more reserve adjustments, he predicted.

"We believe the worst is behind them, but it is still likely that reinsurers will have to boost reserves for the older accident years," said Karen Davies, senior credit officer of Moody's Investors Service Inc. in New York.

"Reinsurers had an unrealistic view of underwriting for a long period during the soft market," she said, adding that "some reinsurers went into a lot of market segments that they didn't have a history in."

The underreserving by established reinsurers does give an advantage to new reinsurers established in Bermuda, but they too will have to carefully manage their business to avoid future reserving problems, observers say.

"The new reinsurers have the advantage of clean balance sheets and good returns on pricing. But the challenge for the new players will be as rates soften," noted Dominic Simpson, a London based Moody's analyst.

The companies which have started since 2001 "have had a very benign claims environment. Our concern is how well they will withstand the stress of a more difficult catastrophe year," said Fitch's Mr. Waterman.

It is important to remember that casualty business written today will become legacy business tomorrow, said Mr. Booth.

But in the future, reinsurers may be able to predict more accurately what level of reserves they will require, analysts note.

"Their techniques for reserve assessment continue to be enhanced," said Mr. Waterman.

Large reinsurers have "very significant teams of actuaries to support reserving," he noted.

A lot of reinsurers have tried to improve their reserving process, said Moody's Karen Davies.

"Actuarial science has improved substantially, although the execution of new techniques often is not as far-reaching because of poor data," she said.

Reinsurers also require a much higher level of underwriting detail from cedents, which should increase their ability to more accurately assess reserves now and in the future, said Best's Mr. DeRose.

"Cedents are required to include a claims history. The information required is supposed to be much more robust than it ever has been before. The industry is no longer relying on handshakes," said Mr. DeRose.

"Reinsurers need to be on top of reserves on a daily basis. There is nothing more important than keeping on top of reserves, after charging the right price," said Mr. Booth.

Reinsurers no longer are able to wait a year to suddenly boost their reserves. If they need topping up, companies will tend to wait no more than a quarter, he said.

"More and more, we are seeing companies adjust their reserves on a quarterly rather than an annual basis," agreed Mr. DeRose.

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Bills: Legislative challenges

Continued from page 4

That is one reason why Congress is always "fiddling around" with laws governing employee benefit plans, according to Mr. Klein.

Lawmakers are partial to benefit mandates because they view such laws as a cost-free way to achieve political gain, unlike legislation supporting infrastructure improvements, for which they must appropriate federal funds, he explained.

"They don't have to spend any money...they don't even have to apply the same provisions to the health and retirement plans that the federal government sponsors for its own employees," he pointed out.

For the most part, members of Congress are unaware of the cumulative cost of the proposals that become law, according to Mr. Klein.

"They'll look at the (Health Insurance Portability and Accountability Act) requirements, mental health parity, the patients' bill of rights, and maybe they'll look at the cost implications to plan sponsors and participants of each one of those items, but they don't necessarily fully appreciate (the total costs of) one of these on top of the other," he said.

"There's also, I'm sorry to say, very little concern for being logically consistent in terms of what they're legislating," Mr. Klein continued. "So, for example, the same member of Congress might be a strong advocate of the patients' bill of rights, which would expand liability, and at the same time they are advocating medical malpractice reform, which shrinks that liability."

'The same member of Congress might be a strong advocate of the patients' bill of rights, which would expand liability, and at the same time they are advocating medical malpractice reform, which shrinks that liability.'

James A. Klein
American Benefits Council

"They might consider new restrictions on the ability to sponsor a hybrid pension plan at the same time they are supportive of the bipartisan effort to simplify the administration of pension plans. There's that disconnect sometimes," he said.

Finally, Congress is largely unaware of the impact of health care costs on retirement security.

"Members of Congress hear a lot about health care costs, but they don't necessarily fully appreciate that what's happening with health care costs is crowding out plan sponsors' ability to save adequately for traditional kinds of retirement security opportunities," he said.

The problem is that lawmakers are asked to make decisions on many issues on which they are not experts, according to Mr. Klein.

"I have a great deal of appreciation for the fact that they have an extraordinarily difficult job. I mean, on any given day, a member of Congress is asked to attend a hearing on the NASA program, to vote on some resolution relative to environmental policy, to meet with some constituents about a housing project that's in their district," he said.

"They can't all be experts on the things that we all spend time being experts on in terms of employee benefits policy. So, the fact that they view these things in separate silos and don't make the connection between the trenches is sort of part of what makes my job as a lobbyist interesting and challenging and your job as somebody actually in the trenches implementing this stuff often very frustrating," Mr. Klein said.

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23rd Annual Employee Benefits Symposium

Managing depression benefits employers, workers

By JOANNE WOJCIK

LAS VEGAS—With depression costing employers more than $80 billion a year in medical expenses, absenteeism and lost productivity, it makes sense to institute a program that detects the disease early, responds quickly and, in some cases, may even help prevent it, a mental health expert says.

"One out of 10 employees suffers from depression, resulting in over 200 million lost days per year," said David Campbell, vp of quality management at ComPsych Corp., an employee assistance plan vendor based in Chicago. Mr. Campbell said employees who perform rapid, competitive work, such as those in manufacturing and at call centers, have the highest incidence of depression.

One reason depression is so costly to employers is that "people with depression have two times more physician visits than the normal population. Depression, which people perceive sometimes as something people have and it goes away, is also considered a chronic disability. It's as disabling as diabetes and heart disease," Mr. Campbell told those attending the 23rd Annual Employee Benefits Symposium, sponsored by the International Society of Certified Employee Benefits Specialists and held recently in Las Vegas.

Yet while many employers have disease management programs for diabetes and heart disease, few have them for depression. As a result, most employees suffering from depression usually seek treatment only from their primary care physicians, who are often ill equipped to treat this disease, according to Mr. Campbell.

"Eighty-seven percent of medication and outpatient services are provided by primary care physicians through the medical plan, which raises the medical cost and lowers the quality of care," he said.

The American Psychiatric Assn. has treatment guidelines "which establish that talk therapy and medication have the best outcomes for depression," Mr. Campbell said. But treatment by a primary care physician alone will not ensure that outcome, he said.

Moreover, Mr. Campbell said, those who are not adequately treated for depression have medical costs that are, on average, two to two-and-a-half times those of non-depressed individuals.

> **'One out of 10 employees suffers from depression, resulting in over 200 million lost days per year.'**
>
> *David Campbell*
> *ComPsych Corp.*

But employers can begin to stem these costs through early identification and intervention, according to Mr. Campbell.

Having training and awareness programs, incorporating the symptoms of depression into health risk assessments and providing access to online depression screening tools all will help educate employees about the condition, promoting early detection, he said.

"Sixty percent of those diagnosed with depression never seek out any form of treatment," he said, yet "studies have shown that people who have education and awareness of depression have a better chance of seeking out treatment."

Managers and supervisors also should be trained to identify the symptoms of depression and urge those employees exhibiting symptoms to seek treatment, he suggested.

And treatment need not always be covered by the health plan, he said. There are numerous community resources that can be accessed for little or no cost, Mr. Campbell noted. "Having these resources and phone numbers and contacts allows supervisors to direct the employees," he said.

Work/life programs that provide ways for employees to address stressful situations, such as obtaining child or elder care, can prevent depression from occurring in some cases, according to Mr. Campbell.

But for any of these programs to be successful in detecting and treating depression early, "they have to be communicated," he stressed. "And the communication has to be frequent."

Too often, employers communicate the availability of such programs only at initial hiring or during open enrollment, rather than at the time an employee may need them, he said.

Employees also need to feel that their employer really cares and wants them to get better, he said.

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23rd Annual Employee Benefits Symposium

Over 700 attend CEBS conference

LAS VEGAS—More than 700 benefits experts attended the 23rd Annual Employee Benefits Symposium, sponsored by the International Society of Certified Employee Benefits Specialists and held Oct. 3-6 in Las Vegas.

Also during the conference, 168 graduates of the society's professional development programs received their CEBS designation at this year's conferment ceremony.

In addition, three people were named to join the ISCEBS governing council, and the organization selected new officers for 2005.

ISCEBS' new president will be David V. Repko, who is the current secretary/treasurer of ISCEBS and a principal at Towers Perrin in Cleveland. The new vp and secretary/treasurer will be Linda Mackey, national director, retirement savings at MetLife Inc. in Schaumburg, Ill.; and Rick A. Storms, vp at Marsh Inc. in Minneapolis, respectively.

Picked to serve three-year terms on the CEBS governing council beginning in January 2005 are: Mary Ann Blackburn, vp-corporate human resources for SouthTrust Corp. in Birmingham, Ala.; Leanne Fosbre, manager-group insurance administration at Wyeth in Rockaway, N.J.; and Keith Rauschenbach, vp of TIAA-CREF in New York.

The annual symposium is open to CEBS graduates and holders of the Compensation Management Specialist, Group Benefits Associate or Retirement Plans Associate designations. In addition, members of the International Foundation of Employee Benefit Plans' corporate sector are eligible to attend.

Next year's conference will be held Sept. 25-28 in New Orleans.

For more information, visit the organization's Web site at *www.iscebs.org*.

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Trains: Cameras aid defense in crossing accidents

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Burlington Northern & Santa Fe Railway Co. has installed cameras and microphones on six of its locomotives and is considering installing the equipment throughout most of its fleet of around 4,700 locomotives, according to a spokesman for the Fort Worth, Texas-based company.

The recording equipment will be mounted in a fashion similar to that on Union Pacific trains and will provide information on crossing conditions and record accidents, the spokesman confirmed.

A video of an accident that is in dispute could be a real boon to a railroad's defense, said Charles Culver, owner of Charles Culver & Associates, a Houston-based railroad consultant and expert witness who has testified for the train companies as well as for plaintiffs in cases against railroads.

"You hear people say they didn't hear the horn until impact," Mr. Culver said. But a recording that shows that the train's engineer followed the rules on sounding the train's horn well ahead of an intersection and followed all other safety procedures "can sure save the day" for a railroad in court, he explained.

Such recordings have helped Norfolk Southern Railway in court, even though that was not the primary reason for using cameras, a spokesman for the Norfolk, Va.-based railroad said.

"Our motivation was primarily for public safety," the spokesman said of the railroad's decision to equip around 2,500 of its locomotives with recording equipment. Norfolk Southern has installed the equipment on about one-third of those trains.

> **'In our litigious society, when there is a grade-crossing accident, if someone is hurt or killed, there is always a lawsuit. This is something we hope can help in situations like that.'**
>
> *Spokesman*
> *Brotherhood of Locomotive Engineers & Trainmen*

Footage from the camera gives the railroad a view of dangerous crossings so that "we didn't have to rely on anecdotal" information about limited visibility or other conditions at the intersections, he said.

But "as far as litigation is concerned, that is an important element as well," the spokesman noted. He confirmed that video has helped Norfolk Southern avoid potential damage awards by confirming the railroad's account of accidents.

Train crews have expressed some concerns about cameras in the workplace, but loss of privacy has not been a big issue.

"We're careful to say that the cameras are pointed outside the cab and the microphone records the train horn, not voices," said the Union Pacific spokesman.

Train crews have made little fuss about the installations.

"It's their railroad, and they can film whatever they want," said Nate Krig, a locomotive engineer and Alexandria, La.-based chairman of the Local 915 chapter of the Brotherhood of Locomotive Engineers & Trainmen.

"The only time the tapes will be reviewed," Mr. Krig said, will be after an accident. And, he added, crews doing their jobs properly have nothing to worry about. "It's supposed to be all business out there anyway."

There have been some concerns raised over privacy issues, said a spokesman for the national office of the Brotherhood of Locomotive Engineers & Trainmen in Cleveland. But, he added: "In our litigious society, when there is a grade-crossing accident, if someone is hurt or killed, there is always a lawsuit. This is something we hope can help in situations like that."

Letters to the Editor

Continued from page 8

ers, which as recently as last August restated its call for full transparency.

The New York Department of Insurance also reviewed the practice in 1998 and issued a rule—contained in New York Department of Insurance Circular Letter No. 22—addressing contingency commissions. That rule did not suggest the practice is impermissible in any way, but instead dictated that brokers who receive contingent commission income should disclose the nature of that income to their clients.

Most commercial insurance brokers are doing the best they can to cement a bond of trust with their customers through hard work and ethical behavior. Insurance is an industry fraught with changing dynamics and practices, but at the end of the day, commercial brokers are good people who work hard for their clients.

Insurance brokers are, fundamentally, service providers, and their clients should expect—indeed, demand—the best possible service in exchange for their business. If commercial clients are uncertain about any aspect of their business as a result of the Spitzer charges, those individuals need to talk to their brokers.

A bond of trust between broker and customer is the foundation upon which the commercial insurance industry rests; honest and open communication between broker and client is the best way to make sure that bond is not frayed or broken.

Ken A. Crerar
President
The Council of Insurance Agents & Brokers
Washington

An accurate forecast of industry trouble

To the editor: On June 16, 2003, *Business Insurance* published my commentary article titled "Industry Needs to Clean its Dirty Laundry." In that article, I had indicated that the insurance industry could face the same ethical problems and probes into fraudulent and improper conduct that were recently experienced by the accounting industry.

Given the widening probe into antitrust and improper conduct by Attorney General Eliot Spitzer of New York, I think that my article turned out to be an accurate forecast of what was to come. *BI* deserves a lot of credit for shining the light on a topic that was too often ignored or not dealt with in the industry.

In recent weeks, much attention has been given to the outlandish compensation packages given to leaders of major health insurance organizations. Given the health care crisis in our country, it is no wonder that such blatant greed would receive critical review.

Now, the regulatory spotlight has rightfully shined upon what many of us industry veterans have always known were unfair antitrust-type practices within the commercial insurance arena between dominating brokers, insurers, TPAs and their select partners. Much like what occurred within the accounting industry, it appears that the insurance industry will face some adjustments of its own.

These recent probes have an interesting parallel to the current presidential elections. The Bush campaign has taken the easy and simple path in blaming lawyers for our country's rising insurance costs and our inability to deliver a long overdue health care plan for all our citizens. They have enabled large and dominating companies to outsource jobs and to manipulate the marketplace to their advantage. Meanwhile, small businesses and middle-class workers have suffered.

Clearly, an open and very competitive marketplace is the best cure for the industry's problems. When large companies control who plays in the marketplace and who doesn't, it creates bad options for consumers and it leads to deserved antitrust speculation and probes. I applaud Eliot Spitzer and other challengers of the status quo for ensuring that our American free enterprise system is kept in check.

Corby Pelto
President and
Chief Executive Officer
Pelto Group Inc.
Minneapolis

PCI: Csiszar to continue efforts

Continued from page 6

the National Assn. of Insurance Commissioners and South Carolina's director of insurance before taking his PCI post, said he's inheriting an organization that is very strong in shaping public policy and public opinion.

In continuing the work "to make these two organizations one," Mr. Csiszar said its no secret that there's going to be some streamlining, "but I think in such a way that we're not losing any of the talent that we have."

"But then we'll quickly turn to what we're all about—the issues," he said.

Mr. Ramirez said he thinks the decision to combine the NAII and the Alliance paid almost immediate dividends in terms of making the case for members on those industry issues.

"One of the things that was noticed almost immediately (was) there was almost an immediate impact with the industry, with the regulators, and it wasn't just a function of being bigger," he said.

"I do think these two organizations represented a certain segment of the market," the retiring president and CEO said. "They represented what I call 'the core of the heart of the industry.'" Among the PCI's members are companies of all sizes—both mutual and stock—doing business in every line and every region of the country.

The combination has "been very helpful in dealing with people who are not directly related to the industry, policymakers in Congress and so on," Mr. Ramirez said.

Mr. Ramirez said he thinks there is considerable value in the notion of the industry addressing its various concerns through a single organization.

"If you have a formalized way of resolving your disputes and reaching consensus, if you can have a permanent structure where people can build relationships with one another, if you can eliminate the competition and inefficiency, then the industry would have a much better chance to reach consensus," he said.

Mr. Csiszar agrees. "Having come from the regulatory side, when you have that multiplicity of voices, the old divide and rule kicks in," he said.

As a regulator, Mr. Csiszar said he would find himself sympathetic to certain positions, but if there weren't consistency from the industry surrounding a given position, he would find it difficult to make it a high priority. "You pick the ones that seem to have the greatest strength behind them," he said.

Reflecting on his accomplishments at the PCI and the NAII before it, Mr. Ramirez is quick to give credit to the associations' managers and staff.

"Looking back, one of the things I'm very proud of is the work we did collaboratively with the staff in creating the strategic plan when I first arrived," he said. Mr. Ramirez joined the NAII in 1993 and was executive vp and chief operating officer before replacing Lowell R. Beck as president and CEO after Mr. Beck retired in 1996.

"It's a plan that served us well," Mr. Ramirez said. "One thing the strategic plan helped us do was change from an organization that monitored and reported on events to one that influenced the outcome. That's something I know Ernie wants to continue."

And help came not only from the staff. "One of the beauties of dealing with an organization at this level is you've got the impact of some CEOs of great companies," said Mr. Ramirez.

"And, they're not shy about sharing their opinions," added Mr. Csiszar.

As he takes over the PCI's president and CEO position, Mr. Csiszar said he expects to benefit from his experience as a regulator. "I think the experience with being, so to speak, on the other side certainly will help," he said. "You certainly see the thinking that was done both privately as well as publicly."

"I think the industry sometimes is kind of naïve about some of the political realities of the regulators," he said. "That's not to say you can't develop that (understanding) over the years. But I've had the opportunity to sit at the table with those people, and you develop that quickly."

The first challenge he'll face is completing the task of "coming up with the right mix" on the PCI's organizational side. "But that's a short-term challenge," Mr. Csiszar said. "Really, the industry faces the challenges and, as a result, they are our challenges."

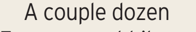
Commentary

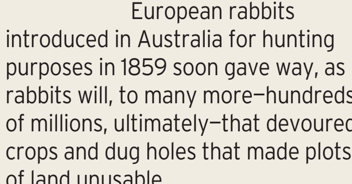
Snakeheads catch Lakes unaware

It's been quite some time since I've done any trick or treating, and I'm rarely moved these days to get into costume on Halloween. But if I was looking for a way to scare the wits out of the little ones coming to the door this year, I think I'd be inclined to go as a northern snakehead.

Actually, the costume would probably do little to distract the kids from job one: shoveling the contents of the candy bowl into their lootsacks. But it probably would cause a few palpitations in some of their parents, the anglers or naturalists among them at least.

For those not familiar with this aquatic menace, the snakehead is an Asian fish that's popped up in various U.S. waters in recent years. A long, thin fish with razor-sharp teeth and known for its voracious appetite, the snakehead is considered a serious threat to existing species in the waterways in which it appears.





Rodd Zolkos

The fish apparently made their way to this country as food—it's considered by some to be a delicacy with medicinal benefits—or as exotic pets described as the "pit bull of fish," so aggressive they can shatter an aquarium with their thrashing.

A couple of years ago, a fisherman pulled one out of a pond in Maryland. Since then, what are believed to be reproducing populations have been found in the Potomac River in Virginia, a pond in South Philadelphia that feeds into the Delaware River and in Massachusetts.

Earlier this month, an angler pulled one out of Lake Michigan's Burnham Harbor in downtown Chicago. It was the snakehead's first confirmed appearance in the Great Lakes.

Biologists' positive ID of the snakehead prompted immediate concern about the well-being of the world's largest freshwater ecosystem and the possible threat posed to the Great Lakes area's sport and commercial fishing industries.

The hope was that the discovery was an isolated incident, and that the snakehead the fisherman landed on Chicago's lakefront was swimming solo and not part of a breeding population. Some good news came last week when traps biologists set in Burnham Harbor failed to produce any additional snakeheads.

I guess it's possible that the snakeheads weren't interested in the raw chicken the biologists used as bait, but that doesn't seem to fit with the description of their hearty appetites.

The snakehead is a creature natural resources types take very seriously. Maryland officials had been sufficiently concerned with the creature called "Frankenfish" that they poisoned an entire pond, not an option for those concerned about the Great Lakes fishery. Federal officials ban bringing 28 species of snakeheads or their eggs into the country and prohibit releasing them into waterways; and a number of states, Maryland and Illinois among them, also prohibit their possession.

Speculation is that the snakeheads that have been popping up around the country came here as pets whose owners released them into ponds or streams after they grew too large or became too expensive to feed.

Tales of ecological disaster associated with species introduction, whether intentional or inadvertent, are myriad, often sounding like something out of a 1950s B horror movie but with very real economic implications.

A couple dozen European rabbits introduced in Australia for hunting purposes in 1859 soon gave way, as rabbits will, to many more—hundreds of millions, ultimately—that devoured crops and dug holes that made plots of land unusable.

Brown tree snakes, thought to have been introduced accidentally to Guam through cargo shipments during World War II, proceeded to kill off the local forest bird population. Today, the lack of birds is responsible for various bug problems on the island, while the snake, which likes to slither along electrical power lines, has been blamed for more than 1,200 power outages since 1978.

In the snakehead's case, its particular form of havoc is wreaked by seriously disrupting the existing food chain wherever the fish is introduced by devouring the various smaller creatures that make up the diets of established larger fish in the habitats they invade.

With the snakeheads' ability to breathe air, survive for extended periods out of water and even move about a bit on land—not to mention the fact that the northern version has learned to slow its metabolism to survive winter—they clearly represent a serious cause for concern. If they start figuring out bus routes and develop a taste for deep-dish pizza and hot dogs, we're doomed.

Senior Editor Rodd Zolkos can be reached at rzolkos@businessinsurance.com.

Comings & Goings

Ms. Hollenbeck

Mr. Wallace

Steven Odell

Robert Odell

Mr. Dickler

Brokers:

Michael K. O'Connell has joined Aon Risk Services as managing director of the company's U.S. financial institutions practice in New York. Previously, Mr. O'Connell was a managing director for Marsh Inc.'s financial institutions practice.

Patti Hollenbeck has been named senior vp/account executive in the risk management unit of Denver-based Lockton Cos. of Colorado Inc. Previously, Ms. Hollenbeck was senior vp with Aon Risk Services.

Palmer & Cay Inc. has named **Steve Conger** as senior vp in the Washington office, where he will have responsibility for developing new client relationships in the mid-Atlantic region. Previously, Mr. Conger was a vp with Marsh USA.

Willis Group Holdings Ltd. has made two senior-level appointments in its New York-based operation.

Lou Daniels has been named executive vp, North America middle market leader. Previously, Mr. Daniels was a corporate vp and national business development leader for Wells Fargo & Co.

Scott Shader, who has been named executive vp, North America small commercial leader, formerly was corporate vp and field operations officer-select accounts for the St. Paul Travelers Cos. Inc.

London-based Heath Lambert Group Ltd. has named **Bob Wallace** as executive director of its construction division. Before joining Heath Lambert, Mr. Wallace was a director for Aon Corp.

Steven Odell has been named president and chief executive officer of the new Radnor, Pa., office of the Lyons Cos., an Assurex Global partner. Previously, Mr. Odell was a senior vp of Clair Odell Group.

Also at Lyons, **Robert Odell** has been named executive vp and chief operating officer of the Radnor office. Previously, he was a senior vp of Clair Odell.

Insurers:

Endurance Specialty Holdings Ltd. has named **Michael Fujii** to head the development of its insurance business in the United States. He previously was president and CEO of Great American Custom Insurance Services.

Richmond, Va.-based Essex Insurance Co. has named **W. Bradley Dickler** as president and COO. Previously, he was vp of the Markel Corp. unit.

Hamilton, Bermuda-based Aspen Insurance Holdings Ltd. has named **James Few** as chief underwriting officer of Aspen Insurance Ltd. Previously, Mr. Few headed Aspen's property reinsurance unit.

New York Life Insurance Co. has named **Gregory Deavens** as senior vp. Before joining the New York-based insurer, Mr. Deavens led the investor relations department of CIGNA Corp.

Gary Kaplan has been named chief underwriting officer of Zurich North America Commercial and head of its technical center. Previously, Mr. Kaplan was senior vp and program executive with the strategic initiatives group of the Schaumburg, Ill.-based insurer.

Keith F. Anderson has been named senior vp-corporate marketing and communications with Alea Group Holdings (Bermuda) Ltd. Previously, Mr. Anderson, who will be based in Rocky Hill, Conn., was chief communications officer for Travelers Property Casualty Corp.

Other providers:

Jody Porrazzo has been named director of econometric risk strategy at Princeton, N.J.-based NiiS/APEX Group Holdings, a division of Gallagher Benefits Services Inc. Before joining NiiS/APEX, Ms. Porrazzo was a consultant.

Minneapolis-based Fiserv Inc. has made two senior-level appointments.

Jay M. Anliker has been named president and CEO for Wausau Benefits of Wausau, Wis. Previously, Mr. Anliker was COO of the company.

John D. Weymer has been named president and CEO of Avidyn Health. Previously, Mr. Weymer was COO of the Dallas-based company.

Christopher McKenna will head a new office of law firm Smith Mazure Director Wilkins Young & Yagerman P.C. in Somerville, N.J. The office will focus on insurance defense. Mr. McKenna formerly was an attorney with Kulick Brennan & Krochta P.A.

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Harassment: Other states may follow California's lead

Continued from page 4
fornia employers with established programs, say observers.

"I think actually it isn't such a bad idea," said Carolyn Humphreys, vp of human resources at Salinas, Calif.-based River Ranch Fresh Foods L.L.C., a food processor.

Supervisors "should be well trained and well versed, and if it means we have an even more effective harassment training program, I think that's a good thing," she said. "It just keeps us on our toes and it provides a benefit to the employee population as a whole."

Under the legislation, employers with 50 or more employees must provide two hours of training and education to all supervisory employees by Jan. 1, 2006, and once every two years thereafter. The training must include information and practical guidance on federal and state statutory provisions concerning sexual harassment, and practical examples aimed at preventing harassment.

'I think you should look at (sexual harassment training) from the point of view of payoff. One lawsuit can really bring a company down, especially a smaller one.'

Joe Gibbons
FutureWork Institute

Training must be conducted by trainers and educators with knowledge and expertise in this area. The legislation states that not providing this training will not result in the liability of any employer charged with sexual harassment, and neither will compliance insulate the employer from liability. The state Fair Employment and Housing Commission can issue orders requiring employers to comply.

Complying with the law may help California employers avoid punitive damages claims, say attorneys. Although "there's not a lot of teeth" in the law, "it will be the first thing plaintiffs point out in a lawsuit if people do not have a formal training program," said Wendy Lazerson, an employer attorney with Holland & Knight in San Francisco.

Attorneys say the issue of employee training has already been raised in federal and state court decisions. Employers "shouldn't be surprised by (the law) because they've long had the same obligations to provide training" under court decisions, including those issued by the U.S. Supreme Court, said Michael W. Johnson, managing director of Washington-based Brightline.

While several other states have laws in this area, the one that most resembles California's is Connecticut's. The Connecticut law, which went into effect in 1993, calls for an initial two hours of training, but does not require that it be repeated, although employers are encouraged by the Connecticut Human Rights Commission to provide updates every three years.

Other states may follow California's lead, say some observers. "I don't imagine it's going to be a big stretch" for other states to do so, said D. Gregory Valenza, an employer attorney with Jackson Lewis in San Francisco.

"I certainly think that it makes a lot of sense for states to legislate this, since, in effect, they'd be legislating judicial-made law anyway, and it's a very good employment practice," said William J. Anthony, an attorney with Jackson Lewis in Hartford, Conn., who said the Connecticut law has not caused problems for Connecticut employers.

Many, but by no means all, California employers already offer some sort of training, say observers. "I think there will be more training done than is being done now," said Ms. Lazerson. In addition, now that training is a statutory requirement, "people will take it more seriously," she said.

The law will also change how training is conducted. Patricia C. Perez, president of La Mesa, Calif.-based Puente International Consulting Inc., said while "we haven't gotten a ton of guidance" as to what the curriculum should be, it is "pretty clear that it must be conducted in an interactive, classroom style, not sitting behind a computer," she said.

Mr. Valenza said while initially there will be a ramping up time as employers put a system in place, it will not pose a major problem for employers.

Ms. Humphreys said the legislation means doubling the session time River Ranch now spends training supervisors on sexual harassment prevention.

In addition, "when you're training something to pretty much the same people every two years, you're going to have to be creative about how you keep their attention the next time," she said. "You certainly don't want to put them to sleep the second time around. We want to make sure people are taking away things they can actually apply in their everyday work life."

Willie Washington, human resources director for the Sacramento-based California Manufacturers and Technology Assn., which opposed the legislation, said the law means an additional two hours of lost productivity time per employee. "It's an additional cost being added on to employers' product cost and we don't know of any way to offset that," he said.

However, Jacqueline McManus, an attorney with Monterey, Calif.-based Fenton & Keller, said clients she has talked to "don't seem to be viewing this as a negative or huge obstacle."

And the training is effective, said Mr. Valenza. "We found that training and prevention tools like this really do cut down on potential claims."

"I think you should look at it from the point of view of payoff," said Joe Gibbons, research director for the Brooklyn, N.Y.-based FutureWork Institute. "One lawsuit can really bring a company down, especially a smaller company."

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WTC: Jury hears opening arguments in coverage trial

Continued from page 3

provisions in the various policies at issue, including a 72-hour clause in some policies that specifically aggregates losses for certain events such as hurricanes but does not mention terrorism. The policies also contain aggregate sublimits for earthquake and flood, but not for terrorism, and exclude war risks without excluding terrorist acts, he noted.

"These insurance companies could have drafted an hours clause to include airplane crashes, fires and terrorist acts," Mr. Nussbaum contended. "Prior to 9/11, not one of them did so."

The insurers, meanwhile, countered that the loss was a single occurrence arising from a coordinated Al Qaeda plot to destroy the complex.

"The World Trade Center was not destroyed because two planes happened to hit two buildings.... The World Trade Center was destroyed because of an obscene, conscious decision to take planes and use them as guided missiles," argued Harvey Kurzweil, a lawyer with Dewey Ballantine in New York, representing units of St. Paul Travelers Cos. Inc.

"The parties did not intend for the amount of insurance to depend on the number of weapons chosen by the terrorists," Mr. Kurzweil said.

Silverstein, its broker Willis Group Holdings Ltd. and the insurers all intended the WTC program to have the kind of broad, aggregating definition of "occurrence" that is customary in the insurance industry and that was included in a Willis property form, known as Wilprop, that the broker circulated with its underwriting submissions, Mr. Kurzweil said.

> **'These insurance companies could have drafted an hours clause to include airplane crashes, fires and terrorist acts. Prior to 9/11, not one of them did so.'**
>
> *Bernard Nussbaum*
> *Wachtell, Lipton, Rosen & Katz*

Willis officials failed to note a Travelers Indemnity Co. policy form's lack of an occurrence definition when they compared the form with Wilprop in 2001 and found 76 other differences, he noted. The reason the occurrence issue wasn't raised, Mr. Kurzweil said, is that Willis assumed Travelers would treat the term "occurrence" in the same way Wilprop does.

Silverstein principal Larry Silverstein, "now that he has suffered a loss, is trying to get more than he bargained for," Mr. Kurzweil charged.

In previous court proceedings and settlements, 15 insurers representing more than two-thirds of the WTC's $3.55 billion limit were found to be bound on the Wilprop form and liable for only one policy limit.

The current phase of the litigation involves the nine remaining insurers, which bound coverage on a variety of other forms and represent $1.13 billion of the program's limit.

Silverstein will continue presenting its case to the jury this week.

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Front, from left: **John W. Stinnett**, Tampa, FL; **Tony Tuggle**, Louisville, KY; **David Valenzano**, Pinellas Park, FL. *Back, from left:* **Frank Rainer**, Tallahassee, FL; **Nick Thilges**, Bloomington, MN; **Marty Maroney**, Tampa, FL

Front, from left: **Brenda J. Bonney**, Fort Lauderdale, FL; **Jena L. Kennedy**, Atlanta, GA. *Back, from left:* **David A. Skup**, Fort Wayne, IN; **Fitzroy A. Smith**, Arlington, VA

Not Pictured: **Stephen Papuchis**, Clarksville, TN; **Mitch Rohde**, Lakeland, FL; **Diana Cook**, Iowa City, IA; **John T. Haas**, Chicago, IL; **Paul Leftwich**, Pinellas Park, FL; **Heather Maxwell**, Fort Lauderdale, FL; **Ruth Murray**, Las Vegas, NV; **Larry Patrick**, Seffner, FL; **Christopher Ridge**, Charleston, SC

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REQUEST FOR PROPOSALS

NEW YORK CITY HOUSING AUTHORITY

REQUEST FOR PROPOSALS (RFP) FOR THIRD PARTY WORKERS' COMPENSATION CLAIMS AND ADMINISTRATIVE SERVICES

The New York City Housing Authority ("NYCHA") requests proposals from Third Party Administrators to provide workers' compensation claims and administration services to NYCHA.

Proposals must be made in the format outlined in the RFP packet containing instructions, specifications and detailed submission requirements. Packets may be obtained beginning October 29, 2004 from **NYCHA's Coordinator for this RFP: Augusto Montan, Assistant Director,** New York City Housing Authority, Risk Finance Division, 90 Church Street, 6th Floor, New York, NY 10007 and **telephone (212) 306-6681. Completed proposals must be received by 4:00 P.M. Monday, December 13, 2004.**

A Proposers' conference will be held on November 5, 2004 @ 2:30 PM in the 5th Floor Ceremonial Room at NYCHA's offices, located at 90 Church Street, New York, NY 10007. All inquires for additional information regarding the RFP are to be directed to **Augusto Montan, Risk Finance Division** at the above address and telephone number.

Michael R. Bloomberg, Mayor, New York City — **Tino Hernandez**, Chairman, NYCHA

REQUEST FOR PROPOSALS

NEW YORK CITY HOUSING AUTHORITY

REQUEST FOR PROPOSALS (RFP) FOR INSURANCE BROKERS - EQUIPMENT MAINTENANCE MANAGEMENT PROGRAM PILOT

The New York City Housing Authority ("NYCHA") requests Proposals from qualified **INSURANCE BROKERS** for placing insurance through qualified carriers to assume the risk associated with preventative maintenance and repair on specified equipment through insurance. Brokers must be licensed by the N.Y.S. Insurance Department and meet minimum qualifications identified in the RFP. Insurance carriers utilized must possess an "A.M. Best" rating of at least **"B+", "VI"**.

Proposals must be made in the format included in the Request for Proposal (RFP) package containing instructions, specifications and detailed submission requirements. Packets may be obtained and requested beginning October 29, 2004 from **NYCHA's Coordinator for this RFP: Augusto Montan**, Assistant Director, New York City Housing Authority, Risk Finance Division, 90 Church Street, 6th Floor, New York, NY 10007-2919 and telephone (212) 306-6681. Completed **proposals must be received by 3:00 P.M. Monday, December 13, 2004**

A Proposers' conference will be held on November 12, 2004 @ 2:30 PM in the 5th Floor Ceremonial Room at NYCHA's offices, located at 90 Church Street, New York, NY 10007-2919. All inquiries for additional information regarding the RFP are to be directed to Augusto Montan, Risk Finance Division at the above address and telephone number.

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U.K. plan sponsors urged to get creative

Efforts to boost participation, manage liability spur look at hybrid plans

By SARAH VEYSEY

LONDON—Employers should consider more innovative benefit designs—and improve benefits communication—to boost pension plan participation, a panel says.

In the wake of a recent report that estimates that 9 million Britons are failing to save enough for their retirement, John Sunderland, president of the Confederation of British Industry, said the CBI hopes to "kick start the debate" as to how employers, individuals and the government can boost retirement saving. The report was published earlier this month by the Pensions Commission, an independent commission set up by the U.K. government to examine pension issues (*BI*, Oct. 18).

Speaking at conference last week in London, CBI Director Digby Jones urged employers to consider alternative pension plan designs, such as hybrid plans, which have elements of both defined benefit and defined contribution plans. Such changes could encourage more employees to participate in company pension plans, Mr. Jones said at the conference, which was sponsored by the CBI and Mercer Human Resource Consulting.

Employers in recent years have moved away from offering defined benefit plans because the risks and costs associated with such plans can leave them faced with an "open-ended liability," Mr. Jones said.

But he added that employers using a switch away from a defined benefit plan to a defined contribution plan as an "excuse to put less in" to their fund is "unacceptable."

Mr. Jones said that employers should be more innovative in designing pension plans. "It is not just a choice between defined benefit and defined contribution," he said.

Adair Turner, chairman of the Pensions Commission and a former CBI director general, told delegates that an important issue employers must consider when setting up or making changes to pension plans is, "who bears the risk?" That risk can be both an investment risk and a longevity risk, he noted.

A move from defined benefit plans to defined contribution plans has resulted in "an extraordinary shift of risk at the moment from employers to individuals," he said.

He said that employers should consider whether there are "intermediate" ways to share risk between the "classic" defined benefit plan structure—in which employers bear the investment risk—and defined contribution plans, where that risk is borne by employees.

"This is a key area that we'd like employers to think about…creative thinking about intermediate solutions of risk," Mr. Turner said.

Aside from hybrid plans, Mr. Turner said, employers could also consider average-salary plans, in which benefits are based on the average salary employees earn during their years of employment. Under traditional defined benefit plans, benefits are based on employees' salary during their last or final years.

Mark Hyde Harrison, pension fund investment director at Barclays Bank P.L.C. in London, told delegates that last year the company decided to change its pension offering to a hybrid plan rather than a purely defined contribution plan.

One reason for this, he explained, was that the company believed some employees were showing a "lack of engagement" with the defined contribution plan, such as not matching employer contributions. In addition, the company was concerned that, in a volatile financial market, pension plan members may not have been equipped to "handle the risk of their pension pots," he said.

"So we decided we were willing to share the risk—there are risks that we can take as a sponsoring employer that would significantly improve the pensions our employees would receive," he said.

But, Mr. Hyde Harrison noted, the bank decided that in order to receive reasonable pension payouts, participating employees should be required to contribute to the plan and to take on some of the responsibility.

Barclays' new pension plan, which was introduced in July 2003 and to which all existing pension plan members were shifted to Jan. 1, 2004, is made up of two parts, he explained. One part of the plan is a credit account that guarantees a certain sum at retirement, based on employees' years of service, he explained. The second part of the plan is an investment account that works very much like a traditional defined contribution arrangement, he explained.

Employees joining the plan must contribute 3% of salary annually to be a member of the plan, he noted.

Because the company requires employees to contribute to the plan, a good communications program that made clear the benefits of the new plan was vital, Mr. Hyde Harrison said.

Since the plan was set up, employee participation has increased 70%, with 58% of staff now paying into the plan, he said. And average employee contributions have increased to 5% from 3.5% of salary, he added.

Other speakers at the conference were Alan Johnson, the secretary of state for Work and Pensions; Peter Thompson, worldwide partner at Mercer; David Smith, economics editor of The Sunday Times; Michael Glasgow, director of pensions at Diageo P.L.C.; and Brendan Barber, general secretary of the Trades Union Congress.

Bill would open up James Hardie records

By ELIZABETH FRY

SYDNEY, Australia—New South Wales Premier Bob Carr has introduced legislation that would give Australian securities regulators investigating James Hardie Industries N.V. full access to the records examined in the recent government investigation the company.

PHOTO: AP/WIDE WORLD

New South Wales Premier Bob Carr

In addition, the legislation, which would override any legal professional privilege or confidentiality protections regarding the James Hardie records, would make the documents available to parties such as the U.S. Securities and Exchange Commission and the Medical Research & Compensation Foundation, the asbestos trust that is at the center of the James Hardie probes, Mr. Carr said.

As part of its 2001 redomestication to Amsterdam, Netherlands, building supplier James Hardie set up the MRCF, funding it with $293 million Australian ($154 million) to pay all claims related to its former asbestos-producing subsidiaries. Although the Sydney-based company attested to the Australian Stock Exchange that the fund was adequate to meet its liabilities, subsequent actuarial assessments determined that it is underfunded by around $2 billion Australian ($1.44 billion) (*BI*, Aug. 16).

Public concern over the fund's adequacy led to a New South Wales government investigation, which last month concluded that James Hardie Chief Executive Officer Peter Macdonald and Chief Financial Officer Peter Shafron had withheld critical data from the actuaries advising James Hardie on the likely cost of future claims, and that Mr. Macdonald had misled the Australian Stock Exchange about the adequacy of the MRCF. In the wake of the government commission's report, Messrs. Macdonald and Shafron resigned their positions, and the Australian Securities and Investments Commission launched its own investigation.

In introducing the legislation, Mr. Carr said: "The government recognizes that legal professional privilege is an important common law right. But when abhorrent corporate conduct on this scale is uncovered, the offenders should not be able to avoid prosecution or other proceedings by hiding behind spurious claims for legal professional privilege."

"The special commissioner's report found that James Hardie's records were littered with claims for legal professional privilege that would be very difficult to justify," he said.

Mr. Carr said the bill would allow ASIC to share the records with other relevant parties, such as the SEC.

"I want the SEC to consider whether James Hardie has breached any United States companies and securities legislation," Mr. Carr told the New South Wales Parliament.

In addition, the bill would give the MRCF access to materials, where approved by the NSW attorney general, for use in civil litigation against James Hardie.

The MRCF welcomed the introduction of the legislation, noting that it is considering legal action against James Hardie if current negotiations with the company over additional funding fail to achieve a satisfactory resolution.

World Updates

ZFS storm claims put at $525 million

Zurich Financial Services Group Inc. expects to pay $525 million in claims arising from the four hurricanes that hit the United States between August and September. After tax and reinsurance recoveries, the Zurich, Switzerland-based insurer will face third-quarter charges of $400 million related to the hurricane losses. The four hurricanes that made landfall—Charley, Frances, Ivan and Jeanne—are estimated to have caused more than $20 billion in total insured losses.

Half in U.K. support mandatory contributions

Half of U.K. adults polled favor making pension contributions compulsory for both employers and employees, according to a survey. Of the 1,002 adults polled, 50% said they would vote "yes" if a referendum were held on whether pension contributions should be made compulsory for both workers and their employers. The study was carried out by market research firm TNS on behalf of AXA, the U.K. arm of Paris-based insurer AXA S.A. Twenty-two percent of respondents said they would vote against such a move, while 21% said they would not vote because they did not feel adequately informed about the issue. Seven percent of respondents said they did not know which way they would vote.

AXA, subsidiary scrap buy-out

AXA S.A. has withdrawn a bid to acquire the remaining 48.3% share it does not own in AXA Asia Pacific Holdings Ltd. The deal was called off last week after AXA and a subcommittee of independent directors at Melbourne, Australia-based AXA APH failed to agree on a price.

Briefly noted

Zurich Financial Services Group has named Dieter Wemmer chief executive officer of Europe general insurance. Mr. Wemmer, currently chief operating officer of the unit, succeeds Axel Lehmann, who was appointed CEO of Zurich North America Commercial earlier this year....Inga Beale has been appointed president and chairman of the board of management at Munich, Germany-based **GE Frankona Re**, a unit of GE Insurance Solutions. Ms. Beale, currently head of GE Insurance Solutions' Continental European operations in Paris, will replace Ken Brandt, who has returned to the United States to head the company's North America and Asia Re business.

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Three largest brokers cave in on contingent income

By SALLY ROBERTS

Although the three largest insurance brokers have stopped or suspended contingent commission arrangements with insurers, it remains unclear whether the controversial form of compensation will vanish from the insurance industry's practices.

Aon Corp., the world's second-largest brokerage, late last week said that it would stop accepting contingent commissions, saying it "cannot permit even the slightest impression of a conflict between acceptance of these commissions and our paramount obligations to our clients."

Approximately $200 million, or about 2.9%, of Aon's $6.8 billion in 2003 commission and fee income is attributable to what Aon calls "compensation for services to underwriters," or CSUs.

Earlier in the week, Willis Group Holdings Ltd., the world's third-largest brokerage, said that in response to customer concerns it would no longer accept extra commissions from insurers based on the volume or profitability of business it places. Willis estimates that such commissions would amount to about $80 million, or about 4% of its projected 2004 gross revenues.

Aon's and Willis' moves came one week after New York Attorney General Eliot Spitzer sued Marsh & McLennan Cos. Inc., charging it with fraudulent self-dealing and bid-rigging in its placement of clients' business (*BI*, Oct. 18). Among other things, Mr. Spitzer charges that brokerage unit Marsh Inc. improperly steered business to insurers that paid it the highest contingent commissions.

Compensation Crisis

While many observers acknowledge that insurers rewarding brokers based on the volume of business produced creates a potential conflict of interest, some argue that profit-sharing arrangements can, in fact, benefit buyers by encouraging brokers to help clients keep losses down.

Following Mr. Spitzer's charges, Marsh "suspended" its practice of collecting the controversial commissions through what it calls "market service agreements." Those extra commissions amounted to $845 million in 2003, or about 12% of Marsh's $6.9 billion in revenues, MMC said last week.

Whether other agents and brokers will discontinue collecting contingent commissions remains to be seen.

Brokerages contacted by *Business Insurance* last week did not return phone calls, declined to comment about their contingent commission arrangements or said they were studying the issue. Most of the top 100 brokers of U.S. business report some revenues from contingent commissions, according to a *Business Insurance* survey (see chart, next page).

Other industry insiders, though, contend that contingent commissions, which are at the heart of Mr. Spitzer's investigation, are being painted as improper with too broad a brush.

While some of the extra commission brokerages receive from insurers—namely volume-based commissions—may create potential conflicts of interest, most arrangements involve profit sharing and, ultimately, may benefit insurance buyers, they say.

Volume-based commissions are more common among the world's largest brokers, while smaller brokers tend to enter into profit-shar-

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Compensation Crisis

***Business Insurance* last week conducted an informal straw poll of a small number of senior risk management professionals to gauge their opinions on the allegations raised in the Spitzer lawsuit. Here are the findings:**

Do compensation agreements between brokers and insurance companies represent a conflict of interest?

Yes 81.8%
No 9.1%
Don't know 9.1%

Have you ever asked your broker to provide information on its contingent commissions or other compensation agreements with insurers?

Yes 72.7%
No 18.2%

Is nondisclosure of contingent commissions an industrywide problem?

Yes 81.8%
No 9.1%
Don't know 9.1%

Should brokers and insurers stop the practice of additional compensation for insurance placements?

Yes 72.7%
No 18.2%
Don't know 9.1%

Would you be willing to pay your broker more if the insurance industry abolishes contingent commissions?

Yes 72.7%
No 18.2%
Don't know 9.1%

Do you believe that bid-rigging on insurance placements, as alleged in the New York attorney general's recent lawsuit, is widespread?

Yes 18.2%
No 27.3%
Don't know 54.5%

Buyers: Some mull severing broker ties

Continued from page 1

At least one risk manager says she has instructed Marsh to cease using its New York-based Global Broking unit to place her account.

The Texas-based risk manager, who did not want to be identified, said that while she'll continue to use her local Marsh office, she has instructed Marsh to stop using the Global Broking unit to place the excess liability portion of her coverage. Like many other large accounts, the risk manager's excess liability exposure was routed by Marsh through its Global Broking center, she said.

Remarking on the allegations made against Marsh and its Global Broking unit, the risk manager said: "In my opinion that is where what I would call the excesses occurred because this relatively small group of people had control." She added, "I'm not saying it hasn't happened at other brokerage firms that don't have centralized marketing, but it certainly set themselves up for these kinds of excesses."

Marsh has agreed to the risk manager's request that its Global Broking unit not handle the account, she said.

Marsh did not respond to questions about the centralized handling of excess liability insurance accounts through its Global Broking unit.

Generally, though, risk managers say that the allegations of bid-rigging, whereby the broker allegedly secured fake high bids from one insurer to ensure that another insurer secured an account, are unlikely to be widespread practices in the placement of commercial insurance.

"I haven't seen any evidence that would cause me to believe there is a systemic problem with bid-rigging," said Susan Meltzer, president of the International Federation of Risk & Insurance Management Assns. Inc. "Given my position in the community, I would have heard whispers. I just don't see it," she said.

A risk manager for a personal lines insurer, who asked not to be identified, said he would have heard of bid-rigging if it regularly occurred in the placement of commercial accounts.

Too many account executives in too many offices would have known about the practice if it were widespread, he said. And given frequent career moves by risk managers into insurance and broking and vice versa, details of the schemes would have leaked out to buyers had the practice been widespread, he said.

The risk manager said he was aware that Marsh handles many of its large excess casualty accounts through its New York office. "So you have few people who could do it," the risk manager said. "But the vast majority of placements have no opportunity," he said. "I can't imagine that the bid-rigging would have been widespread. You would know about it."

And, while the abuse of contingent commissions is unlikely to be widespread, the very use of these compensation arrangements is a bad business practice, although not illegal, contends Ms. Meltzer.

The payment of contingent commissions by insurers to brokers can create an environment "where individuals can do rogue, corrupt things," she said.

According to Mr. Spitzer's complaint, Marsh brokers placed commercial business with insurers that paid it the highest contingent commissions rather than with insurers that provided the best coverage at the lowest price. Contingent commissions take several forms, but are payments made by insurers to brokers based on the volume or profitability of business place by the brokers.

Ms. Meltzer was vp of the New York-based Risk & Insurance Management Society Inc. in 1999, when the organization negotiated an agreement concerning contingent commissions with J&H Marsh & McLennan Inc., a predecessor of Marsh. The broker agreed to inform clients about contingent commission revenue upon their request (*BI*, Feb. 1, 1999).

RIMS made a significant effort to educate risk managers that they should manage a potential conflict of interest stemming from contingent commissions, Ms. Meltzer said. But, she added, risk managers mostly ignored the advice.

The allegations against Marsh, however, should convince more risk managers that the arrangements present a potential conflict of interest, said Mark DeLillo, North American risk manager for developer Taylor Woodrow Inc. in Bradenton, Fla.

"When you start having disclosures of fraudulent transactions and guilty pleas, it raises that question all over again of a conflict of interest," Mr. DeLillo said. "So I would think that there would be a higher level of interest today than there was in the risk management community" in the late 1990s.

But contingent commissions are "not a Marsh issue," Mr. DeLillo added. "Marsh happens to be the focus. But it's a brokerage industry issue."

The fraud allegations made against Marsh do raise concerns for risk managers but it may be a problem that is not confined to Marsh, said Ken Dolan, director of risk management for MDU Resources Group Inc. in Bismarck, N.D., who is a Marsh client.

"If you are going to leave, who are you going to go to?" Mr. Dolan said. "Lord only knows who the next targets are going to be."

Additionally, dealing directly with insurers is not an option, because of the leverage and resources brokers can provide clients, Mr. Dolan said.

However, the recent allegations could spur more risk managers to hold direct talks with their insurers to help guard against any abuse of contingent commission payments, said Daniel H. Kugler, assistant treasurer-corporate risk management for Pleasant Prairie, Wis.-based Snap-on Inc.

Chuck Magazine, risk manager for the City of Boynton Beach, Fla., said he has a system in place that could prevent conflict of interest issues over contingent commissions. Mr. Magazine said he asks several brokers to submit a list of insurers with which they are capable of placing his business. He then studies the lists and assigns to the brokers the insurers they can obtain quotes from.

It is a lot of work, but "I control their access to insurance companies," Mr. Magazine said.

In response to an informal straw poll of a small group of senior risk managers conducted last week by *Business Insurance,* risk managers overwhelmingly say that nondisclosure of contingent commissions is an industrywide problem (see related graphic).

Nearly 73% of the respondents said brokers and insurers should stop the practice of additional compensation for insurance placements while 18% said no and 9% said they don't know.

Only 18%, however, said they believe that bid-rigging on insurance placements, as alleged by Mr. Spitzer, is widespread.

Compensation Crisis Online

The controversy over contingent commissions is not new but is drawing greater attention in the wake of allegations that they contributed to fraud by brokers and insurers. To help subscribers stay informed, and to review the developments that led to Eliot Spitzer's investigation, *Business Insurance* has compiled an online archive of all articles it has written on the contingent commissions debate in recent years. In addition to links to articles going back to 1998, the online resource features links to Mr. Spitzer's announcement of his lawsuit, Securities and Exchange Commission filings and other material. To view the Compensation Crisis archive, visit *www.businessinsurance.com/cgi-bin/page.pl?pageId=194*

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CONTINGENT COMMISSIONS AMONG THE 100 LARGEST BROKERS OF U.S. BUSINESS

Percentage of total gross revenues from contingent commissions

Rank	Company	2003 total gross revenues	% from contingent commissions
1	Marsh & McLennan Cos. Inc.	$11,612,000,000	7.3%
2	Aon Corp.	9,752,000,000	2.0
3	Arthur J. Gallagher & Co.	1,304,500,000	3.0
4	Willis Group Holdings Ltd.	2,075,000,000	4.0 *
5	Wells Fargo & Co.	902,225,000	3.4
6	BB&T Insurance Services Inc.	626,023,000	NA
7	Hilb Rogal & Hobbs Co.	563,647,023	NA
8	Brown & Brown Inc.	551,040,513	6.0
9	USI Holdings Corp.	354,802,000	5.0
10	Lockton Cos. Inc.	301,000,000	4.0
11	Wachovia Insurance Services Inc.	191,656,510	7.2
12	Hub International Ltd.	286,359,000	6.0
13	Jardine Lloyd Thompson Group P.L.C.	728,808,600	NA
14	Alliant Resources Group Inc.	158,461,000	5.7
15	Palmer & Cay Inc. [1]	151,446,530	6.2
16	CBIZ Benefits & Insurance Services Inc.	168,061,161	4.0
17	ABD Insurance & Financial Services	120,662,000	3.0
18	Heath Lambert Group Ltd.	532,389,780	NA
19	Talbot Financial Corp. [2]	99,100,000	8.4
20	Frank Crystal & Co. Inc.	92,978,000	NA
21	Keenan & Associates	93,212,862	NA
22	Meadowbrook Insurance Group Inc.	87,400,000	1.0
23	John L. Wortham & Son L.P. [1]	83,174,000	3.0
24	Commerce Insurance Services Inc.	82,377,000	NA
25	Citizens Financial Group Inc.	80,725,000	4.1
26	Hylant Group	77,014,930	6.5
27	The Leavitt Group	77,650,000	4.7
28	The NIA Group L.L.C. [1]	73,560,000	6.0
29	Fleet Insurance Services	71,200,000	4.0
30	Bollinger Inc.	70,970,458	7.5
31	Brokerage Concepts Inc.	68,100,000	0.0
32	J. Smith Lanier & Co. [2]	63,657,553	7.0
33	Holmes Murphy & Associates Inc.	62,647,897	4.0
34	Summit Global Partners Inc.	70,135,307	8.1
35	UBOC Insurance Inc.	$63,250,000	7.0 %
36	Synaxis Group Inc.	59,359,000	3.6
37	Rebsamen Insurance Inc. [2]	57,930,889	2.0
38	Allied North America	56,900,000	NA
39	Mesirow Insurance Services Inc. [2]	54,236,000	10.0
40	Compass Insurance	53,200,000	4.9
41	The IMA Financial Group Inc. [1]	52,974,583	6.4
42	Guaranty Insurance Services Inc.	53,176,542	5.0
43	Tanenbaum-Harber Co. Inc.	50,874,000	4.6
44	Frenkel & Co. Inc. [1]	50,797,087	9.0
45	The Hays Group Inc. dba Hays Cos.	48,800,000	NA
46	Banknorth Insurance Group	47,256,000	11.0
47	Brooke Franchise Corp.	65,967,040	3.1
48	Heffernan Group	44,408,000	6.0
49	InterWest Insurance Services Inc.	42,558,418	8.0
50	Neace Lukens [1]	41,474,108	5.0
51	Insurance Office of America Inc.	41,170,241	7.0
52	Van Gilder Insurance Corp. [1]	41,309,000	12.0
53	Marshall & Sterling Enterprises Inc.	40,155,052	8.0
54	BancorpSouth Insurance Services Inc.	40,195,048	6.0
55	The Graham Co.	38,063,000	2.4
56	SullivanCurtisMonroe Insurance Brokers [2]	38,253,000	5.0
57	Woodruff-Sawyer & Co. [1]	39,250,000	7.0
58	The Rutherfoord Cos. [1]	38,515,295	NA
59	The Treiber Group	36,039,546	6.0
60	Barney & Barney L.L.C. [1]	35,350,000	NA
61	Jenkins Athens Insurance Services	35,590,000	3.6
62	Horton Insurance Agency Inc.	34,633,061	4.0
63	Cottingham & Butler Inc. [1]	34,114,500	2.5
64	Hibernia Insurance Agency L.L.C.	34,032,000	1.0
65	The James B. Oswald Co. [1]	34,179,000	5.8
66	William Gallagher Associates Insurance Brokers Inc.	34,771,967	10.0
67	The Mahoney Group [1]	34,263,407	5.1
68	Andreini & Co.	$32,000,000	4.2 %
69	McQueary Henry Bowles Troy L.L.P.	31,500,000	7.0
70	Van Beurden Insurance Services Inc.	39,205,000	1.0
71	Capacity Group of Cos.	30,079,114	NA
72	BWD Group L.L.C.	29,748,000	NA
73	Trion	30,500,000	NA
74	Frank F. Haack & Associates Inc. [1]	29,700,000	7.0
75	Riggs, Counselman, Michaels & Downes Inc. [1]	28,700,000	8.0
76	The Loomis Co.	28,940,000	1.0
77	Eastern Insurance Group L.L.C.	27,729,288	10.0
78	Bratrud Middleton Insurance Brokers Inc.	27,900,000	11.0
79	Lawley Services Inc.	27,421,402	8.3
80	R.C. Knox & Co. Inc.	27,147,000	NA
81	Bowen, Miclette & Britt Inc.	36,446,000	6.5
82	Roger Bouchard Insurance Inc.	27,343,800	3.5
83	The Daniel & Henry Co. [1]	25,182,000	6.1
84	Payne Financial Group Inc. [1]	25,089,804	9.0
85	Fringe Benefits Management Co.	24,260,738	NA
86	Higginbotham & Associates Inc.	24,561,035	5.4
87	Charles L. Crane Agency Co.	23,938,000	NA
88	Associated Financial Group L.L.C. dba CFG Insurance Services [2]	23,892,361	6.1
89	Seitlin [1]	24,200,216	6.0
90	Barlocker Insurance Services Inc.	23,896,000	11.0
91	Sterling & Sterling Inc. [2]	23,000,000	NA
92	Lovitt & Touche Inc.	23,078,690	NA
93	JMB Insurance Agency Inc.	23,300,000	4.5
94	Dawson Insurance Inc. [2]	24,082,228	5.5
95	Haylor, Freyer & Coon Inc.	25,000,000	8.4
96	T.J. Adams Group L.L.C. [1]	21,200,000	10.0
97	Parker, Smith & Feek Inc. [1]	21,371,200	6.3
98	Scott Insurance	21,350,000	4.8
99	North American Insurance Agency Inc. dba North American Group [1]	21,680,964	5.1
100	Fred A. Moreton & Co. [1]	21,110,000	4.7

Source: *BI* survey, company reports * Willis estimate for 2004 N/A - not available or did not report data 1 An Assurex Global Partner 2 A RiskProNet Partner

Commissions: End of controversial compensation?

Continued from previous page

ing arrangements with their insurance partners.

In detailing its projected 2004 contingent commission revenues last week, for example, Willis said that $73 million of its estimated $80 million in contingent commissions comes from volume contingencies, while only $7 million come from profit contingencies.

On the other hand, Brown & Brown Inc. estimates that 90% of its $30.2 million in contingent commissions so far in 2004 are profit driven, according to Cory Walker, chief financial officer of the Daytona Beach, Fla.-based brokerage.

"I think it's unfortunate that Spitzer has painted the entire insurance agency system with this broad brush," Mr. Walker said of contingent commissions.

"They've characterized this thing as some contra-consumer interest," Mr. Walker said. Profit-based "contingencies do help align the interests of the insured and the insurance company in getting the broker to help out in that relationship. If everybody can keep their losses a little lower, then there is a reduction in overall insurance premiums. But you've got to have everybody helping out," he said.

"Where everything goes from here, I don't know, but this is not something that I believe has been detrimental to clients," Mr. Walker said of profit-based contingent commissions.

Other market observers agree.

While volume-based contingencies "in theory are neutral, but in practice could be abused," profit-sharing agreements are a "pretty benign form of extra commission that actually serves a good purpose, which is aligning the objective of the broker with that of the insurance company," said Donald Light, a San Francisco-based senior analyst with research and consulting firm Celent Communications. "And I think it has little potential for harm for the corporate buyer of insurance."

"I think carriers are motivated to reward brokers for writing profitable business," said John Wicher, principal of San Francisco-based insurance investment bank John Wicher & Associates. "A healthy insurance industry requires underwriting profit, and that requires brokers placing business at proper rates. Placing poor business and moving that from market to market with the objective of achieving price rather than adequate price…isn't a formula for a healthy industry," he said. "So I think rewarding brokers for consistently placed business at proper rates with proper markets resulting in underwriting profits is healthy."

'Our clients don't like contingency agreements. We've listened to our clients. We've heard them loud and clear. They want contingencies to end, and we intend to respond to that. It's over.'

Joe Plumeri
Willis Group Holdings Ltd.

"There are many, many contingent commission agreements where all the arrows are pointing in the same direction," said John Ward, chairman of Cincinnati-based Ward Group. "It works to the benefit of the system—the producer, the company and the customer," he said. "And I think clearly the intent of most companies that have these is to develop an incentive compensation arrangements that is a win, win, win for everybody involved," he said.

Bobby Reagan, president and CEO of Reagan Consulting Inc. in Atlanta, for one, said that the agency consulting firm is "not suggesting to our clients that they suspend contingent income, because it is a legal practice and, if handled properly, does not compromise the interest of any insured. But we are advising our clients that there will most likely be disruptions in this source of income," he said.

But as Ken A. Crerar, president of the Washington-based Council of Insurance Agents & Brokers, points out, even though these practices have been longstanding and are legal, "at the end of the day, the most important relationship for a broker is the relationship between the client and the broker. And if there's a perceived problem from the client, it's clear that the broker needs to do what it's supposed to do, which is to stand up for the client," he said.

Aon and Willis cited such considerations in announcing their decisions to end contingent commission arrangements.

"Our clients don't like contingency agreements. We've listened to our clients. We've heard them loud and clear," Willis Chairman and CEO Joe Plumeri said in a conference call with analysts. "They want contingencies to end, and we intend to respond to that. It's over."

He said Willis has ended the use of contingent commission arrangements with insurers in North America and will wind up the practice elsewhere around the world as soon as it is practicable. Willis said it also would restructure its compensation arrangements for other market services provided to insurers.

He also noted that Willis has discovered no evidence of bid-rigging within the brokerage.

In a statement announcing Aon's decision to stop accepting contingent commissions, Patrick G. Ryan, chairman and CEO of Aon said the broker would establish an alternative system for payment of services.

"We will work closely with insurance carriers, regulators and other constituencies to establish a new business model that ensures appropriate linkage of compensation to specific, measurable services in a way that is transparent, accepted and understood by our clients. We provide important services on behalf of underwriters; however, certain current compensation models must change," he said. Aon previously announced that, to the best of its knowledge, its employees have not participated in bid-rigging.

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Brokers: Industry in crosshairs

Continued from page 1

it has the authority to suspend or revoke Marsh's licenses, order restitution to clients and impose fines. An insurance department spokesman said it is too early to say what penalties might be imposed if the charges are proven, but legal sources discount the possibility that Marsh's licenses are in danger.

Speculation continued late in the week about Marsh's top management, with reports that the company's independent directors were pressing Chairman Jeffrey W. Greenberg to step down and clear the way for settlement talks with Mr. Spitzer.

At a press conference announcing his lawsuit, Mr. Spitzer had suggested that he would not negotiate with Mr. Greenberg and advised MMC's board to "look long and hard" at its top management.

Marsh officials could not be reached for comment Friday. Soon after the suit was filed, Marsh Inc. Chairman and Chief Executive Officer Ray J. Groves resigned and was replaced by Michael G. Cherkasky, formerly CEO of the company's Marsh Kroll risk consulting unit.

Meanwhile, Aon Corp. announced late Friday that it would stop taking contingent commissions, following a similar announcement by Willis Group Holdings Ltd. on Thursday and news from Marsh on Monday that it would suspend its use of such commissions. Marsh collected $845 million in contingent commissions last year, and Aon collected about $200 million, while Willis expected to collect $80 million this year, the companies said (see story, page 44).

Mr. Spitzer's probe of insurance industry compensation practices also widened as his office subpoenaed information and documents from health insurers (see story, page 46) and reinsurance brokers.

A number of the reinsurance subpoenas specifically target the reinsurance operations of Aon, Marsh and Willis.

Subpoenas issued to several competing reinsurance intermediaries in the last two weeks ask for information about contingency fee agreements and for any evidence that Aon, Marsh or Willis demanded insurance companies' reinsurance brokerage business as a condition of placing insurance risks with them.

Mr. Spitzer is asking intermediaries whether they've lost clients to the top three brokers as a result of their "tie-in" of insurance and reinsurance placements, a copy of a subpoena obtained by *Business Insurance* shows.

The subpoenas also ask the intermediaries to provide details of any contingent commission arrangements they have with reinsurers.

An Aon spokesman declined to comment on the subpoenas and said only that Aon is cooperating with Mr. Spitzer's investigation.

A Willis spokesman also declined to comment, though Joe Plumeri, Willis' chairman and chief executive officer, said last week in a conference call with analysts that the brokerage has found no evidence of tie-ins in its treaty reinsurance placements.

A Marsh spokeswoman did not respond to a call seeking comment.

For brokers with enough business to provide the necessary leverage, tie-ins have been a longstanding practice, some intermediaries say.

"It has gone on, and it has been overt in some instances and less overt in other instances," one broker observed.

Contingent commission agreements, several brokers add, have not been a common reinsurance industry practice, though one intermediary who requested anonymity said he knows of at least one case in which a rival broker collected volume-based commissions.

Disclosing that it had been subpoenaed, Benfield Group Ltd. said that it has acquired brokers that had a "limited number" of contingent commission agreements and that Benfield has terminated the agreements.

New York-based Holborn Corp., which was also subpoenaed, sent a letter to its clients and reinsurers last week saying it has never accepted contingent commissions because they "present an actual conflict of interest or the appearance of one."

Several brokers, meanwhile, questioned whether Mr. Spitzer's investigation will extend to possible retrocessional tie-ins, in which brokers similarly pressure reinsurers for their retrocessional business in exchange for reinsurance placements.

A spokesman for Mr. Spitzer refused to comment on the subpoenas or the scope of the investigation, saying only that it is "broad and deep."

Fast-developing situation

The reinsurance inquiry came amid a rush of other developments in the Spitzer probe.

Marsh—which collected $1.27 billion in contingent commissions over 18 months in 2003 and 2004—saw its debt rating downgraded and was forced to renegotiate credit facilities with lenders. Marsh also became the target of several shareholder class action lawsuits and suits filed on behalf of participants in Marsh retirements plans who suffered huge losses with the decline in the broker's stock price.

The turmoil followed Mr. Spitzer's filing of a lawsuit on Oct. 14 charging Marsh with fraud and antitrust violations for allegedly steering business to insurers that paid it the highest contingent commissions and rigging bids to protect favored insurers.

Under contingent commission agreements—also known as placement service agreements and market services agreements—insurers pay brokers a commission based on the volume or profitability of business they produce. The agreements, Mr. Spitzer charges, create a conflict of interest and subvert brokers' duty to serve only their clients' best interests.

In addition to the steering charges, Mr. Spitzer's suit alleges that Marsh Global Broking employees directed insurers to submit artificially inflated quotes—known within Marsh as "B quotes"—to create the appearance of competition while Marsh channeled business to insurers it chose. Insurers provided B quotes knowing that they would be similarly protected on other placements, the suit charges.

Insurers cited in bid-rigging allegations—but not named as defendants—are AIG, units of ACE Ltd. and Hartford Financial Services Group Inc. and the Munich-American RiskPartners division of American Re-Insurance Co.

As the civil complaint was filed, three insurance company employees also pleaded guilty to criminal charges of participating in the alleged bid-rigging and agreed to cooperate with Mr. Spitzer's investigation. They are: Jean-Baptiste Tateossian and Karen Radke, both executives with an excess casualty unit of AIG's American Home Assurance Co.; and Patricia Abrams, an ACE assistant vp.

Early last week, meanwhile, a Marsh spokeswoman confirmed that the broker had suspended five employees in the wake of the charges, including four Global Broking employees.

While the spokeswoman declined to name those suspended, four Marsh employees are identified in the criminal complaints against Mr. Tateossian, Ms. Radke and Ms. Abrams. The complaints allege that William Gilman, a managing director in Global Broking, and Edward McNenny, another Marsh official, instructed AIG to submit phony quotes to rig placements in favor of incumbent insurers. They also charge that Gregory Doherty, a Global Broking senior vp, directed ACE to submit similar fake quotes, and that Samantha Gilman, another Marsh official, received confirmations of phony quotes from AIG.

Mr. Gilman, Mr. McNenny, Mr. Doherty and Ms. Gilman did not respond to requests for comment.

In announcing the civil suit and criminal charges, Mr. Spitzer said his investigation of the industry will be wide-ranging, covering brokerage practices in "virtually every line" of property/casualty and life/health insurance.

Other troubles

Troubles piled up for Marsh and other brokers last week in the wake of the probe.

California Insurance Commissioner John Garamendi proposed new rules that would require brokers to disclose all compensation they receive on insurance placements and punish them for failing to provide the best available quotes to clients.

Officials in several other states are launching similar probes. They include Minnesota, Florida, Georgia, Illinois, Massachusetts, Connecticut and New Jersey.

Credit rating agencies, meanwhile, reacted negatively to the investigation and the announcements by brokerages that they would halt collecting contingent commissions. For Marsh, the commissions amounted to 7% of the parent company's total revenues in 2003 and the first half of 2004.

Standard & Poor's Corp. downgraded Marsh's credit rating to BBB+ from A+, citing its loss of contingent commission income and diminished ability to rapidly retire $1.9 billion in short-term debt from its acquisition of Kroll earlier this year.

In addition, prior to Aon's announcement that it would end the use of contingent commissions, S&P downgraded its rating to BBB+ from A-, citing the potential loss of commissions. Aon is estimated to have taken in $200 million in contingent commissions last year.

Other rating agencies have placed ratings of Marsh, Aon and Willis under review.

Meanwhile, brokers and insurers became the targets of several class action lawsuits triggered by the Spitzer probe.

Opticare Health Systems Inc., a Waterbury, Conn., eye care services company, has filed a racketeering lawsuit in federal court in New York, citing Mr. Spitzer's charges and naming Marsh, Aon, Willis, eight other brokers and several units of AIG, ACE, Hartford and Munich Reinsurance Co. The suit seeks class action status on behalf of all of the brokers' clients and insurers' policyholders since August 1994.

Marsh has also been named in a number of shareholder class action suits, as well as separate lawsuits filed on behalf of employees and retirees who participated in the company's 401(k) and other retirement plans and held Marsh stock.

Marsh stock closed at $26.79 on Friday, down 42% from its close Oct. 13, the day before the Spitzer lawsuit was announced.

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Contingent fees limited on benefits side

By GLORIA GONZALEZ

New York Attorney General Eliot Spitzer will likely find less evidence of contingent commission arrangements as he expands his investigation into the practice to include health and disability insurers.

Structural differences between the property/casualty insurance industry and the health insurance industry as well as the existence of stringent federal requirements regarding the placement of health insurance have limited the spread of contingent commissions on health insurance placements, market observers say.

However, several health insurers have received subpoenas seeking information on contingent commissions from Mr. Spitzer, and at least one broker has indicated that it has received some form of contingent commissions from health insurers.

Compensation Crisis

While the focus of Mr. Spitzer's investigation has largely been on the placement of commercial property/casualty insurance contracts, in particular those placed by Marsh Inc., he has indicated his investigation will include life and health insurance, disability insurance and personal lines coverage.

Several health and disability insurers last week confirmed they had received second subpoenas from Mr. Spitzer. The insurers include Aetna Inc., in Hartford, Conn.; Philadelphia-based CIGNA Corp.; Chattanooga, Tenn.-based disability insurer UnumProvident Corp. and New York-based MetLife Inc.

Connecticut Attorney General Richard Blumenthal has also launched an investigation into whether health insurers are participating in contingent commission arrangements, a source familiar with the investigation said.

And a lawsuit filed last week in California accuses several health, life and disability insurers of conspiring with San Diego-based insurance broker Universal Life Resources to steer Universal's clients to the insurers in exchange for undisclosed fees and kickbacks. The lawsuit was filed by an employee of Intel Inc. who purchased insurance policies through the company's em-

See BENEFITS/next page

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Late News

Continued from page 1
by now-insolvent Reliance National Indemnity Co., a state appeals court ruled. Instead, the insurer for the employer that contracted for the temporary worker must pay the claim, California's 2nd District Court of Appeals in Los Angeles found Thursday. Aliso Viejo, Calif.-based RemedyTemp Inc. said that it would appeal the decision. The court said its decision is to be applied prospectively. .

NAIC examining industry practices

The National Assn. of Insurance Commissioners said it is taking steps to better protect corporate consumers in the wake of New York Attorney General Eliot Spitzer's lawsuit alleging bid-rigging and other improper conduct involving brokers and insurance companies. The NAIC plans to "coordinate directly with law enforcement officials in identifying and terminating" any illegal activities, "as well as developing new regulations as needed to better monitor all sales activities," NAIC President Diane Koken, the Pennsylvania insurance commissioner, said in a statement. In addition, insurance regulators have "pursued the formation of a commissioner-level entity whose sole focus will be to prevent future abuses and protect consumers at all levels," the NAIC statement notes.

Rise in formations boosts RRGs' premiums

Amid a sharp increase in new formations of the vehicles, premium volume generated by risk retention groups grew significantly last year, according to a recent survey. Risk retention groups produced a total of $1.74 billion in premiums in 2003, up 37% from $1.27 billion in the prior year, according to the Risk Retention Reporter, a Pasadena, Calif.-based publication that covers the risk retention group industry, which analyzed premium data obtained from the National Assn. of Insurance Commissioners. In 2003, a record 58 risk retention groups were formed, bringing the total number of risk retention groups at year end to 141.

Briefly noted

A twin-engine turboprop aircraft operated by Corporate Airlines that crashed near the airport in Kirksville, Mo. on Oct. 19, killing 13 of the 15 passengers and crew, had an insured value of $1.67 million, according to market sources. The coverage is led by Global Aerospace Underwriting Managers Ltd. A liability reserve has not yet been set, market sources reported.

Check out BusinessInsurance.com

Items in the Late News column originally appeared in *BI*'s Daily News feature on *www.businessinsurance.com.*

Benefits: Contingent fee deals limited

Continued from previous page
ployee benefit program, which was brokered by Universal.

In a statement, Doug Cox, president and chief executive officer of Universal, denied the allegations in the suit and said Universal "maintains proper relationships with its clients and their insurance carriers."

Although Mr. Spitzer's lawsuit has already had serious repercussions for the property/casualty insurance industry, few expect a similarly severe impact on the benefits side, because contingent commission arrangements are not prevalent in the benefits area.

"My sense is that it's not nearly as widespread on the employee benefits side as on the P/C side," said John Ward, chairman of Cincinnati-based Ward Group. "All things being equal, the employee benefits side would be less of a target or less of an issue than the other lines of business on the P/C side."

Unlike property/casualty insurers, most health insurers do not pay commissions linked to the volume of placements by intermediaries, said Bradley Ellis, director of Fitch Ratings in Chicago. "Selling health care does not lend itself to these types of contingent commissions."

Contingent commission arrangements are uncommon in the employee benefits area partly because consultants, rather than brokers, place most large benefit programs, analysts say. Consultants generally work on a fee basis rather than on a commission basis, and the fees are paid by employers. When commissions are paid as part of a consultant's remuneration, the commission is offset by a reduction in consulting fee paid by the client so the consultant does not receive extra compensation by working on commission.

Consultants say they purposely do not accept any contingent commissions to avoid any potential conflicts of interest.

"We feel as an organization we have to maintain our independence as well as our objectivity," said Richard Sinni, managing director of the Northeast health and welfare practice of PricewaterhouseCoopers L.L.P. in New York.

Another reason contingent commission arrangements are not widespread in the health care field is benefit placements often have to abide by federal laws that make use of such arrangements difficult.

Most benefit plans are governed by the Employee Retirement Income Security Act and must follow Department of Labor rules governing compensation arrangements.

The rules mandate that broker compensation arrangements be fully disclosed to the plan's fiduciary, said Sheldon Emmer, a partner with Los Angeles-based law firm Emmer & Graeber who specializes in ERISA law. If the broker fails to disclose all compensation arrangements, the Labor Department can penalize the broker for ERISA violations, he said.

"Without disclosing, you can't take compensation because it would be a prohibited transaction," he said.

When a broker discloses its compensation arrangements, the plan fiduciary must decide if the compensation is reasonable and if the cost of the plan is higher than it would have been had the coverage been placed by another broker or directly with the insurer, Mr. Emmer said. Fiduciaries who allow brokers to be overcompensated can be charged with a breach of duty and may face penalties, he said. "The fiduciary shouldn't allow them to be more than reasonably compensated," he said.

Although contingent commissions are probably more common in property/casualty placements because of these rules, they might exist in the benefits arena because some people may be ignorant of ERISA or may choose to flout the law, Mr. Emmer said.

"When people are pressured to make financial goals…they try to rationalize why this is OK," he said.

In addition, ERISA's ambiguity regarding certain types of contingent commissions impacts how much of a barrier they are to these arrangements, he noted. The ERISA rules are clearly prohibitive on the issue of steering clients to particular insurers in exchange for higher commissions, but the rules are ambiguous on volume or override commissions, which are based on meeting certain thresholds rather than for specific clients, he said.

"This override concept is much more nebulous," Mr. Emmer said. "I don't want to say overrides are illegal or improper. That's the big question."

Mr. Ellis of Fitch Ratings said his company's view is that contingent commissions would be problematic if based on one client, but not if based on achieving overall goals.

Some brokers avoid participating in either type of contingent arrangements for fear of running afoul of ERISA.

Brokerage Concepts Inc. does not participate in any commission arrangements based on profitability or volume of business or bonuses based on directing business to a certain insurer, because the company believes the Department of Labor rules clearly prohibit these arrangements, said Arnold Katz, president of the King of Prussia, Pa.-based brokerage specializing in benefits. "We refuse to participate in these things," he said.

In a statement on its Web site, Chicago-based Aon Corp. said it has compensation arrangements with several health insurers, including CIGNA and Aetna, that are not client specific. The company did not return calls for comment on the nature of its compensation agreements with the health insurers.

London-based Willis Group Holdings Ltd. declined to comment on its compensation arrangements, but the broker announced last week that it would immediately end the use of contingent commission arrangements with insurers in North America and would do so elsewhere as soon as it is practicable.

Other benefit brokers did not return calls for comment.

While most of the major health insurers either declined to comment or did not return phone calls, New York-based WellChoice Inc. released a statement saying it does not engage in any of the practices filed in Mr. Spitzer's complaint against Marsh.

Online Poll

[10/18 - 10/22]

Do you expect your 2005 group health care premium increase to be lower than the 2004 increase?

Response	%
Yes	30.4%
No	46.1%
Do not know	23.5%

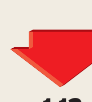
BI Stock Index

[10/18 - 10/22]

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

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

Index	Value	Change
BI Stock Index	2038.41	-3.41
Dow Jones	9757.81	-1.77
S&P 500	1095.74	-1.12



Largest gains

Company	Change
Arthur J. Gallagher & Co.	10.61%
Willis Group Holdings	7.78%
ACE Ltd.	5.09%
SCPIE Holdings Inc.	3.79%
USI Holdings Corp.	3.68%

Largest losses

Company	Change
ESG Re Ltd.	-16.67%
Aetna Inc.	-14.61%
CIGNA Corp.	-12.27%
Sierra Health Services	-9.93%
Aon Corp.	-8.92%

Weekly change by market segment

Segment	Change
Brokers	0.31%
Insurers/Reinsurers	-1.57%
Managed Care Organizations	-6.77%

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