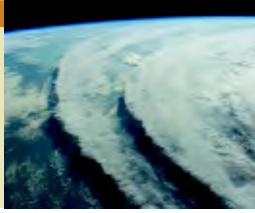


ABOVE-AVERAGE HURRICANE ACTIVITY PREDICTED / PAGE 3



ZURICH TO PAY \$25 MILLION TO SETTLE SEC CHARGES OVER FINITE DEALS / PAGE 3

RULES ON TOXINS IN THE WORKPLACE MAY CHANGE / PAGE 4



In Brief

Daschle nominated to health reform post

President-elect Barack Obama has nominated former Senate Majority Leader Tom Daschle to be director of a new White House office for health reform and will nominate him to be secretary of the Department of Health and Human Services. Mr. Daschle said reforming the nation's health care system is "our biggest domestic policy challenge." Ultimately, reforming the system through expanding coverage and bringing costs under control will benefit not only the uninsured but also will help businesses by making them more competitive, he said.

Senator seeks comment on offshore tax proposal

Senate Finance Committee Chairman Max Baucus, D-Mont., is seeking comments on draft

See **IN BRIEF** page 26



Kevin Kelley (left), the longtime chief of American International Group Inc. surplus lines unit Lexington Insurance Co., last week joined Bermuda-based Ironshore Inc. Shaun Kelly, COO of Lexington, also went to Ironshore.

Lexington regroups as execs jump ship

Ironshore swoops in to pick up big names from key AIG unit

By **DOUGLAS McLEOD**

BOSTON—American International Group Inc. suffered a severe blow with the departure last week of the two top executives at its Lexington Insurance Co. unit—departures that underscore the difficulties AIG faces in retaining key employees, industry sources say.

Kevin H. Kelley, longtime chairman and chief executive officer of the nation's largest surplus lines insurer, resigned to become CEO of Bermuda-based Ironshore Inc. last week. He was joined by Shaun Kelly, who resigned as Lexington's president and chief operating officer to become CEO of Ironshore's U.S. operations.

Mr. Kelley, a widely respected executive, spent 33 years at Lexington, including 21 as CEO and 11 as

chairman. He oversaw the insurer's growth from a few hundred million dollars in nonadmitted direct premiums to \$6.3 billion last year.

"This is a big deal, to lose Kevin's leadership inside the Lexington," said Tom Curtin, CEO of Birmingham, Ala.-based CRC Insurance Services Inc., the largest U.S. wholesale broker. "He was the architect of that business."

The two departures also show the impact of AIG's collapsed stock price on its ability to hold on to top executives, observers say.

For many years, high-ranking AIG officials have received long-term compensation in the form of restricted AIG stock units, and some built holdings they expected to be worth millions or even tens of millions of dollars. As AIG's huge mortgage-related losses emerged and its shares plummeted from more than \$50 earlier this year to less than \$2, those officials saw their holdings wiped out.

See **LEXINGTON** page 25

XL move ignites buzz over possible sell-off

Hard-hit insurer seeks bank's advice, estimates losses

By **JUDY GREENWALD**

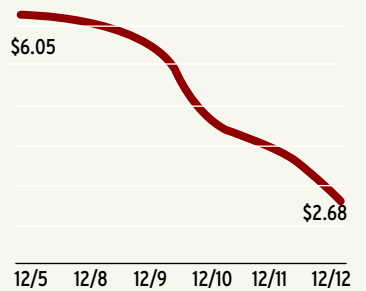
HAMILTON, Bermuda—If embattled Bermuda giant XL Capital Ltd. embarks on a sale of some or all of its operations, the company is likely to encounter a difficult sales environment amid the ongoing economic turmoil, analysts say.

XL said last week that it has hired New York investment banking firm Goldman Sachs & Co. to assist in its exploration of "value-enhancing opportunities." Some observers interpret this to mean all or parts of XL are up for sale. An XL spokeswoman had no additional comment beyond what was in the statement.

The stock market reacted negatively to the news, with XL's shares

XL DROPS

Sell-off talk sends shares lower



Source: www.financialcontent.com

closing at \$2.68 on Friday, down from \$6.05 the previous week.

Hamilton-based XL also said in its statement the company expects the estimated mark-to-market decline on its investment portfolio—which is made up of changes in unrealized losses other than temporary impairments and realized

See **XL** page 25

SPOTLIGHT YEAR IN REVIEW: RISK MANAGEMENT

Business Insurance takes a look back at the AIG bailout, the impact of the economic crisis and other top stories that affected risk managers last year.



Key newsmakers for the year are profiled, and a timeline details the most important events that occurred in 2008. **PAGE 11**

Congress OKs modest pension funding relief

By **JERRY GEISEL**

WASHINGTON—Business groups welcome the last-minute passage of legislation that will reduce the amount of money employers will have to contribute to shore up pension plans badly depleted by the plunge in the equities markets, but they say Congress needs to provide much more relief next year.

Only a year ago, most pension plans—buoyed by several consecutive years of stellar investment returns—were overfunded. But now, after a dramatic and rapid fall in the stock market since September, many pension plans are badly underfunded, with assets in many cases only 75% to 85% of liabilities, actuaries say.

That fall in funding levels—

unprecedented in its speed—means employers are facing a "doubling and even a tripling of cash contributions" to their plans, said Rick Jones, chief actuary with Hewitt Associates Inc. in Lincolnshire, Ill.

With the economy moving into a deep recession and the credit markets extraordinarily tight, this huge demand for cash to shore up plans couldn't come at a worse time for business. The prospect of having to funnel a huge amount of money to their plans when they can least afford it led hundreds of individual employers and many trade groups to seek a temporary easing of funding rules.

Last week, Congress responded to that plea—if only modestly, to soft-

See **PENSIONS** page 24

92%

FUNDED: The target pension plan funding level for employers in 2008 under current law.

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Zurich settles finite fraud charges with SEC

Insurer accused of inflating financial performance of reinsurance unit prior to share offering

By SALLY ROBERTS

NEW YORK—Zurich Financial Services Group will pay \$25 million in civil penalties to settle fraud charges brought last week by the U.S. Securities and Exchange Commission in connection with three finite reinsurance transactions that authorities said inflated the financial performance of its former reinsurance operation, Converium Holding A.G.

The SEC also settled similar civil securities fraud charges against Converium, which was acquired by SCOR Holding A.G. in 2007, in a separate cease-and-desist order.

The SEC alleged that beginning in 1999, management of Zurich's reinsurance group, which operated at that time under the name Zurich

\$2 billion

THE AMOUNT raised when Converium Holding sold 40 million shares to the public in 2001, the largest reinsurance initial public offering in history.

Re, developed three finite reinsurance transactions that it improperly accounted for as reinsurance when, in fact, no risk was transferred outside of Zurich-owned entities.

In two of the transactions, Zurich Re ceded risk to Bermuda-based Inter-Ocean Reinsurance Co. Ltd., but then retroceded the risks to

another Zurich entity. In the third transaction, Zurich Re ceded the risk to a third-party reinsurer but simultaneously entered into an undisclosed side agreement with the reinsurer in which Zurich Re agreed to hold the reinsurer harmless for any losses realized under the reinsurance contracts.

In 2001, Zurich spun off Zurich Re into the newly created Converium and sold 40 million shares to the public in the largest reinsurance initial public offering in history, court papers say. Zurich raised nearly \$2 billion in the IPO.

As a result of the improper accounting treatment of the three finite deals, however, the historical financial statements included in Converium's IPO documents were

materially misleading.

Among other things, the SEC said Converium understated its reported pretax loss by approximately \$100 million in 2000 and by approximately \$3 million in 2001 as a result of the improper accounting. And, for certain periods, the transactions also artificially decreased Converium's loss ratios in certain segments.

Those misstatements, the SEC said, were material to investors who purchased shares in the IPO and caused Zurich to raise significantly more than it would have raised had it correctly reported Converium's financial performance.

Following the IPO, Converium continued the fraudulent scheme,

See **ZURICH** page 25

Hurricane forecasters see active 2009 season

Colorado State team predicts 14 named storms

By MARK A. HOFMANN

The 2009 Atlantic hurricane season looks like it will have above-average activity, two forecasters predicted last week in separate reports.

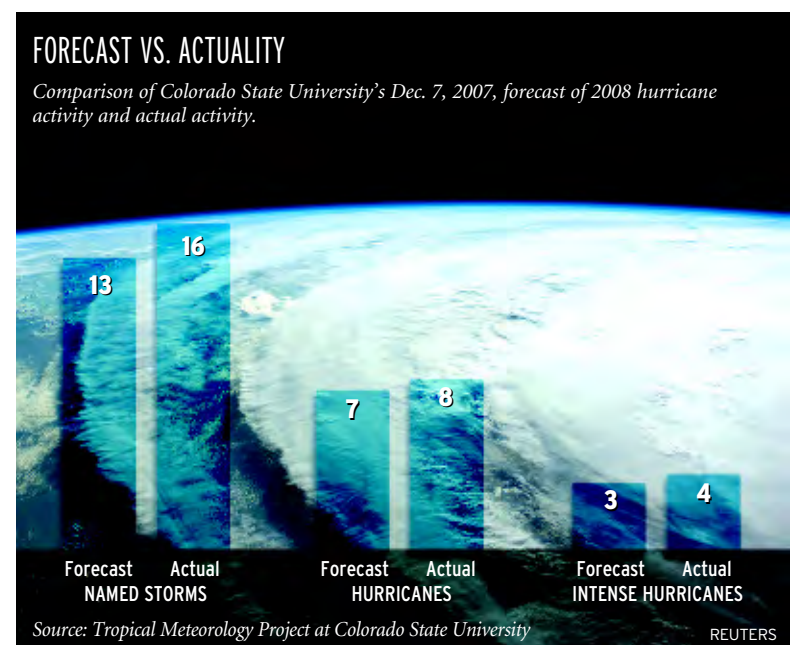
Fourteen named storms are forecast to form during next year's hurricane season that runs from June 1 through Nov. 30, 2009, according to the Tropical Meteorology Project at Colorado State University in Fort Collins.

Seven of those storms are forecast to grow into hurricanes, with three of those strengthening into "intense" hurricanes packing sustained winds of at least 111 mph, the CSU team said.

By contrast, during the period 1950 to 2000 that the CSU team uses as a benchmark, an average of 9.6 named storms formed each year, with an average of 5.9 gaining enough strength to become hurricanes.

Meanwhile, Tropical Storm Risk, a consortium of experts on insurance, risk management and seasonal climate forecasting led by the Aon Benfield UCL Hazard Research Centre at University College in London, also projected above-average hurricane activity next year.

"Based on current and projected climate signals, Atlantic basin and U.S. landfalling tropical cyclone activity are forecast to be 35% above



the 1950-2008 norm in 2009," TSR said in its analysis.

There is a "fairly high" likelihood that the "activity will be in the top one-third of years historically," TSR said.

The London-based consortium said key factors behind its forecast for 2009 "are the anticipated moderate enhancing effect of warmer-than-normal sea-surface temperatures and weaker-than-normal trade winds."

NAIC OKs lower collateral for non-U.S. reinsurers

By MEG FLETCHER

GRAPEVINE, Texas—The National Assn. of Insurance Commissioners must craft details and implementation plans of a recently adopted reinsurance regulatory regime that would relax requirements on non-U.S. reinsurers.

The NAIC voted last week to adopt the measure that may take years to implement. The proposal establishes a framework to allow a single qualified state to be the sole U.S. regulator of a reinsurer writing assumed business in the United States.

Current plans call for establishing a new NAIC Reinsurance Supervision Review Department that would assess the qualifications of non-U.S. jurisdictions as well as states that want to qualify to be the sole U.S. regulator of a reinsurer writing

COLLATERAL PLAN AT A GLANCE

The National Assn of Insurance Commissioners' plan to relax collateral rules for highly rated non-U.S. reinsurance companies would:

- Establish the NAIC Reinsurance Supervision Review Department.
- Seek authorization from Congress to allow adoption of the standard nationwide, although each state would decide whether to participate.
- Organizations in favor of the plan include the International Underwriting Assn., Lloyd's of London, the Reinsurance Assn. of America and the Risk & Insurance Management Society Inc.

Source: NAIC

assumed business in the United States.

All reinsurers would have an option under the new system. They could apply through the new NAIC office for a sliding scale of relaxed collateral for highly rated compa-

nies, or they could operate under the current system that requires non-U.S. reinsurers to post 100% collateral for their U.S. claims liabilities.

The NAIC also plans to seek congressional authority "so the option-

al structure could be adopted uniformly nationwide," although each state legislature would decide whether its insurance regulator will participate, said Steven Goldman, chair of the Reinsurance Task Force and the insurance commissioner of New Jersey.

Helping to build support for the measure at the Dec. 5-8 meeting in Grapevine, Texas, was an amendment by Vermont that established principles for the new department including transparency of operations and participation by small states, observers said.

The measure passed on a voice vote with only a handful of dissenters from Indiana, Kentucky, Ohio, Utah and Wisconsin, who shared the concerns of most U.S. ceding insurers about the proposal's

See **NAIC** page 24

Business Insurance®

REPORTING ON CORPORATE RISK AND EMPLOYEE BENEFIT MANAGEMENT NEWS

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Canadian court rules insurer must cover machine failure

Design exclusion doesn't bar coverage for tunnel borer loss

By KRISTIN GUNDERSON HUNT

OTTAWA—A Supreme Court of Canada ruling favoring policyholders likely will result in insurers rewriting language commonly used in exclusion clauses of policies covering specialized equipment for engineering and building projects, attorneys say.

Canada's highest court resolved a 14-year dispute between Canadian National Railway Co. and six insurers that included Royal Sun Alliance Insurance Group P.L.C.

In a 4-3 decision last month, the

court ordered insurers to pay \$30.8 million Canadian (\$24 million) for costs associated with the 1994 failure of a tunnel-boring machine during a tunneling project under a river.

Montreal-based Canadian National insured the tunnel-boring project between Sarnia, Ontario, and Port Huron, Mich., under a builders' risk policy that covered "all risk of direct physical loss or damage to all real and personal property of every kind and quality including but not limited to the tunnel-boring machine, plus any consequent economic loss occasioned by delay in the opening of the tunnel," according to the decision.

Failure of the custom-made machine caused a 229-day delay,

greatly increasing costs, according to the decision. Insurers denied coverage, though, citing the "faulty or improper design" exclusion in the policy, saying the innovative machine was unfit for the project in the first place and they should not be liable.



Kirk Stevens, who represented the insurers and a partner with Lerner L.L.P. in Toronto, said the case was more of a machine warranty issue, not a coverage issue.

"We said, 'If the machine fails to meet expected and ordinary conditions because the design doesn't work, then the exclusion applies,'"

Mr. Stevens said.

Olivier Chouc, assistant vp-legal affairs for Canadian National, said the company never looked at this as a warranty issue, but as an insured loss. As a result, it sued.

A trial judge held the insurers liable, saying the design accommodated all foreseeable risks and was not faulty according to the state-of-the-art standard when the design was finalized. The Ontario Court of Appeal reversed that decision, finding the machine's design was faulty within the exclusion's meaning and did not withstand all foreseeable risks that the standard required.

The Supreme Court, however, determined that the insurers should be liable.

"The CNR was entitled to insure against the possibility that the

design might fail even though not faulty or improper according to the state of the art," the ruling said. "The design failed, but, because it exhausted the state of the art, insurers did not meet the onus of bringing the loss within the exclusion."

Mr. Stevens said the ruling greatly affects insurers because they now essentially must prove whether a machine's design is state of the art, not just faulty or improper. He said proving a nearly one-of-a-kind machine is not state of the art, and therefore faulty and excluded, is difficult because there is little to compare it with and few experts on the subject.

Ultimately, he said insurers will have to redesign the policy language

See **INNOVATION** page 24



The U.S. Chamber of Commerce supports a proposal it says would better protect workers who are exposed to toxic substances or hazardous chemicals in the workplace.

Democrats, unions fault risk assessment rules

Work safety changes pushed through too quickly, critics say

By ROBERTO CENICEROS

WASHINGTON—Democrats and labor unions charge that the Department of Labor is rushing to implement a new occupational health risk assessment rule before President Bush leaves office in January.

But the U.S. Chamber of Commerce counters that the Department of Labor has allowed public input into developing the rule that would mandate how the U.S. Occupational Safety and Health Administration and the U.S. Mine Safety and Health Administration conduct risk assessments of toxic substances or haz-

ardous chemicals in the workplace.

The Department of Labor could have proceeded without soliciting any public input, but allowed a 30-day comment period to promote transparency in developing its proposed rule, said Marc Freedman, director of labor law policy for the Washington-based chamber.

The chamber supports the proposal, saying it would improve safety regulation by standardizing analysis of issues such as the amount of risk posed by certain levels of toxins, the likelihood of exposure and what measures are warranted to limit worker exposure.

But the Risk & Insurance Management Society Inc. would have liked greater transparency, said Terry Fleming, director of the Montgomery County division of risk management

See **TOXIC** page 26

Increasing number of bankruptcies trouble workers comp self-insurers

As failures mount, claims could strain state guaranty funds

By ROBERTO CENICEROS

As economic conditions deteriorate and bankruptcies rise, managers of self-insured workers compensation guaranty funds across the United States say they fear they will have to take over more employers' claims payments.

Operations of self-insured guaranty funds vary widely from state to state, but often they assess participants to have sufficient money before any of those employers default on paying their workers comp claims.

Should too many large companies default within a short time, the potential drawdown of the guaranty fund balances is a risk that managers increasingly attempt to mitigate, several said.

"Obviously, it's an unprecedented time as far as economic turmoil and default risk, not just for self-insurers but for businesses in general," said Brian D. Gee, executive director of the Florida Self-Insurers Guaranty Assn. Inc. based in Tallahassee. "I think it would be fair to say we are on heightened alert, but (our increased vigilance is) similar work to that we do even in good times to try and identify the risk."

So far in the U.S. recession, Mr. Gee and several other fund managers said they have not seen more companies fail to pay their workers

comp obligations. Defaults won't come until the end of the recession or even after economic conditions improve for companies that have struggled for some period, they said.

But the rising potential for company failures is driving the guaranty fund managers to increase their vigilance over fund participants' fiscal health by monitoring credit reports, signs of financial distress and bankruptcies, several managers said.

In 2007, 71 publicly traded companies with nearly \$64 billion in assets filed for bankruptcy protection or bankruptcy nationwide, according to Boston-based New Generation Research Inc. This year, however, 118 companies with more than \$1.1 trillion in assets had filed

See **COMPENSATION** page 24

Key risks spur changes in approach

But improvements face many obstacles: Survey

By MIKE TSIKOUKAKIS

Nearly 83% of risk managers and chief financial officers say they have revised internal programs to control and prevent losses in five major areas of risk, according to a *Business Insurance* survey.

In addition, slightly more than half of the group said they had changed their business plans or operations and set up study groups to address risks to their reputation, interruption of their business operations, supply chain breakdowns, third-party liabilities and the general market environment, concluded the survey conducted by Syosset, N.Y.-based research firm Erdos & Morgan Inc.

The October survey of 135 risk

managers and CFOs across the United States found that at least 75% of the respondents felt they were somewhat or very prepared to handle such risks.

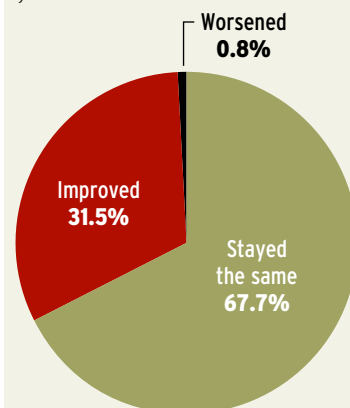
While there was general agreement on preparedness, the opinions of risk managers and CFOs varied greatly when it came to obstacles to improving organizational preparedness. Money, the company's business plan, time and circumstances beyond their control topped a host of risk management concerns. The volatile U.S. economy lagged other factors, according to the survey.

However, Glenn Baker, director of risk management at Highland Park, Ill.-based Solo Cup Co., said

See **SURVEY** page 22

PERFORMANCE

How risk managers and chief financial officers rated risk adviser/broker speed of response to five major risks in the past year.



Source: Business Insurance survey

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that appealed to both the company and its landlord. The existing system was replaced with one designed for high-pile storage and the building was outfitted with new heaters to prevent the pipes from freezing. In addition to protecting its inventory, the company saved almost \$30,000 a year in premiums. It's all part of Wausau TotalValueSM and our commitment to lowering our customers' total cost of risk. A commitment backed by the financial strength of the Liberty Mutual Group. To learn **PRICE ≠ COST.** more, visit wausau.com or contact your Wausau representative.

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Commentary

Will gangster talk hit da 'Govfather'?

Let's pause to remember the glory days of Illinois Gov. Rod Blagojevich.

It was only five years ago that he led the fight to allow reimportation of prescription drugs from Canada, an idea a lot of employers loved. Then he proposed ambitious health care legislation to cover the uninsured, partly by imposing fees on Illinois businesses. This was not as popular.

In the end, neither effort went anywhere, but at least you can say that Gov. Blagojevich never gave those of us who didn't know him personally any reason to doubt his sanity.

How quickly things change.

As everyone now knows, the governor has vaulted Illinois back into the lead for the title "Louisiana of the North." In the past couple of decades, Louisiana has sent one governor (Edwin Edwards) and several successive insurance commissioners to jail on corruption charges. With the 2006 conviction of former Illinois Gov. George Ryan, Gov. Blagojevich stands to make it a consecutive two-for-two for Illinois.

If convicted, Gov. Blagojevich may set the gold standard for statewide public corruption, though, given unusually disturbing aspects of the case.

For one thing, there's the breadth of the charges: Federal prosecutors allege that, almost from the time he took office in 2002, the governor looked for ways to squeeze campaign money from people who did business with the state. This culminated in his alleged attempts to sell Barack Obama's U.S. Senate seat and to get members of the Chicago Tribune editorial board fired in exchange for the state's help to the Tribune Co. in selling the Chicago Cubs.

Another thing is the gangster-movie quality of the governor's conversations, as recorded by the FBI. Many of us let a curse fly once in a while, and anyone familiar with Richard Nixon's White House tapes knows that that kind of talk isn't unprecedented for public officials.

Mr. Blagojevich sounds like he walked out of a "Sopranos" script, though. Who was his campaign chairman, Paulie Walnuts?

"I've got this thing, and it's (expletive) golden," he said of his power to appoint Mr. Obama's Senate successor, according to prosecutors. "I'm just not giving it up for (expletive) nothing."

During a call on the Tribune situation, the governor's wife, Patti Blagojevich, can be heard in the background saying, "hold up that (expletive) Cubs (expletive)...(Expletive) them," accord-



DOUGLAS
McLEOD

Senior Editor Douglas McLeod
can be reached at:
dmcleod@businessinsurance.com

ing to the charges.

Carmela Soprano never sounded like that.

The most disturbing thing about the case, though, is Gov. Blagojevich's weird belief in his own power and bright prospects—prospects he saw as including a run for president in 2016, prosecutors said.

Meanwhile, he huddled with advisers last month about trading the Senate seat for an appointment as secretary of Health and Human Services in the Obama

If convicted, Gov. Blagojevich may set the gold standard for statewide public corruption.

administration, the criminal complaint alleges.

In a three-way call with the governor and an unidentified Washington adviser, John Harris—Gov. Blagojevich's chief of staff, also arrested last week—said they did not want the trade to "look like some sort of selfish grab for a quid pro quo," but needed to consider Gov. Blagojevich's "financial security" and desire to remain "politically viable," prosecutors alleged.

You can imagine what might go on with Mr. Blagojevich as HHS secretary, in charge of billions of dollars of grants and contracts. Jackpot!

What's striking about the prosecution's recap of alleged corruption, though, is the governor's uncanny self-confidence.

This is a man, after all, who openly discussed selling a Senate seat and squeezing the Tribune despite knowing that he was the target of a federal investigation.

In his early days, Gov. Blagojevich seemed serious about health care. If prosecutors are right, it's scary to think he was taken seriously by anyone but the FBI.

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Business Insurance OPINIONS

Daschle pick will help health reform efforts

IT IS SAID that a journey of a thousand miles begins with a single step. President-elect Barack Obama last week made a good first step in selecting Tom Daschle to lead the White House's health care reform drive.

As a former Senate majority leader, few are more knowledgeable and understanding than Mr. Daschle in what it takes to get enactment of legislation as comprehensive, complex and controversial as health reform.

In fact, President-elect Obama alluded to Mr. Daschle's political skills, describing him as someone who knows how to reach across the political aisle and to find an acceptable middle ground.

Mr. Daschle, who President-elect Obama also selected to be secretary of the Department of Health and Human Services, affirmed that the development of health reform legislation should be an "open and inclusive process."

He's right. When it comes to developing and passing health reform legislation, no one person, no special interest group and no one political party has all the right answers.

No one person has all the right answers.

That is a lesson Hillary Clinton, the last person to lead a national reform effort, learned the hard way when the reform plan she developed went down in flames. Given that the plan was developed in secrecy and that no effort was made to bring Republicans in to help draft the plan, its fate was no surprise.

Fortunately, that's a path down which Mr. Daschle shows no sign of starting. That said, crafting and winning passage of health care reform legislation, even under the best of circumstances, would be hugely difficult.

With the economy in tatters and federal dollars drying up, the challenge to find revenues to help subsidize health insurance coverage for the low-income uninsured—an obvious integral part of any serious reform measure—seems an almost insurmountable one.

But nothing is forever—not even a bad economy—and there is no reason why the search for the right health care reform ingredients should not begin now.

Bailout shouldn't create winners and losers

EXTRAORDINARY TIMES can require extraordinary measures, and these are extraordinary times as the federal government directly or indirectly gains an ever-larger share of a shrinking economy.

But even in extraordinary times, common sense can't be ignored. If federal funds are going to be spent to save private institutions, every dollar dispersed must be adequately accounted for. Yet, a Government Accountability Office report released last week said such oversight appears lacking in administering the Troubled Assets Relief Program.

GAO said the Treasury Department "has yet to address a number of critical issues," including assuring that recipients of federal funds are complying with limits on executive compensation, dividends and stock repurchases. That needs to be remedied very quickly.

After all, the purpose of the bailout is to help financial services institutions in trouble, not to give them a competitive advantage over financially healthier counterparts. The government should not be in the position of choosing winners and losers, even inadvertently.

The hundreds of billions of dollars involved are not some abstraction—they are provided by commercial and individual taxpayers. Those taxpayers must be assured that their money is indeed being spent as intended, and only enhanced oversight can provide that assurance.



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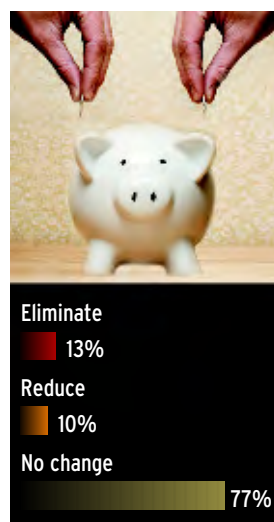
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Top 10 risk management stories of 2008

1. Federal government bails out AIG.
2. Financial crisis hammers insurers.
3. Former executives of Gen Re and AIG convicted of fraud.
4. Rates for most insurance coverage lines continue to slide.
5. Internal Revenue Service drops rule that would have stripped tax breaks from captives.
6. Brokerage market consolidation continues; Willis acquires HRH, and Aon buys Benfield in big deals.
7. Hurricanes Ike and Gustav wallop Texas and Louisiana.
8. Treasury Department endorses an optional federal charter for insurers.
9. Former Marsh executives convicted in bid-rigging trial.
10. Eliot Spitzer resigns as New York governor amid call girl scandal.

Economic turmoil, AIG crisis command buyers' attention

Financial meltdown prompts risk managers to examine relationships with insurers, raises concerns about security

By **DAVE LENCKUS**

The economic crisis and American International Group Inc.'s financial meltdown defined 2008 for many risk managers.

Other developments—including the presidential election, this summer's hurricanes and the federal government's modified stance on assisting public entities after national disasters—also ranked among the events risk managers said most affected them this year.

But the tough economy, which has

led to tighter insurance market conditions, and AIG's financial woes clearly outpaced all other news stories in 2008.

"I can't remember a thing that happened other than AIG and Wall Street," said John Phelps, director-business risk solutions for Blue Cross & Blue Shield of Florida Inc. in Jacksonville.

"That just defined the year, if not the decade," he said.

"Risk managers are going to be far more circumspect about whom they do business with in the future" and

not rely on rating agencies exclusively, Mr. Phelps asserted. Risk managers will have to seek greater analysis from brokers and benchmark with other risk managers, he said.

Meanwhile, AIG's insurance subsidiaries may find problems retaining policyholders, even though the companies remain well capitalized, he said.

"It's very difficult (for some risk managers) to sell that to the board of directors and senior management when all they read about is the problem the mother ship is

having," he said.

For risk managers, the brain drain from AIG's insurance units is troubling, even though AIG has a strong bullpen of talent to step into vacated positions, said Lance Ewing, vp-risk management at Harrah's Entertainment Inc. in Cordova, Tenn. "It's a relationship business," Mr. Ewing said. "I, as a customer, don't have that comfort level yet" with the AIG personnel who have filled open positions.

See **YEAR** page 12

Year: AIG crisis, economic meltdown command buyers' attention

CONTINUED FROM PAGE 11

The balance sheets of other insurers also have suffered as the rest of the economy has weakened and government bonds have begun trading at big discounts, said James D. Hinton, vp-risk and insurance at Nashville, Tenn.-based HCA Inc. "That raises solvency issues."

As a result, "insurers are trying to raise prices or hold them," he said.

Mr. Ewing agreed. Especially with property insurance, the hardening market "came down like a guillotine at the end of the year," he said.

Risk managers also are concerned

now about the strength of all insurers covering group health and pension benefits, said Ron Hayes, the incoming president of the Public Risk Management Assn. in Alexandria, Va.

Mr. Hayes, risk manager for the Calcasieu Parish School Board in Lake Charles, La., said the tough economy also highlights the problem government entities face in complying with accounting rule GASB 45, which mandates that public entities account for their future retiree benefits.

Meanwhile, increasingly frugal public entities are cutting back

funding of ongoing professional education for risk managers, and those cutbacks could continue in 2009, Mr. Hayes said.

President-elect Barack Obama's election has raised questions for risk managers as well as the rest of the country over what health care will look like in the future. For many risk managers, President-elect Obama's victory creates health care cost uncertainties. For other risk managers, such as HCA's Mr. Hinton and Blue Cross & Blue Shield's Mr. Phelps, the election raises questions about their organizations' future business models.

President-elect Obama's election also means financial markets are certain to face greater regulation, which could be good or bad news, risk managers said.

In addition, optional federal charters for insurers likely will be seriously considered, said Wayne Salen, director of risk management at Labor Finders International Inc. of Palm Beach Gardens, Fla.

And the federal government also likely will pay greater attention to issues that will directly affect employees and, therefore, employers, Mr. Salen said. Those issues include immigration policy and

workplace safety, he said.

Two summer hurricanes, Gustav and the more destructive Ike, "had a major impact on the Gulf Coast area," which still is trying to recover from the devastating hurricane season, Mr. Hinton said.

The hurricanes underscored the top news story for public entity risk managers, said PRIMA's Mr. Hayes.

In a May announcement that risk managers did not begin to understand until three months later, the Federal Emergency Management Agency announced it would provide much less federal aid to public entities that sustain damage in multiple disasters of the same nature.

Risk managers pointed out other significant developments this year.

For example, Mr. Salen noted that the federal Centers for Medicare and Medicaid Services announced last summer that next year it will begin reviewing settlements of all casualty cases for their impact on the two programs. CMS currently reviews only workers compensation settlements.

Mr. Salen predicted that the new approach by CMS will drive up costs and create difficulties in resolving litigation involving, for example, auto liability and premises liability claims.

Mr. Salen also noted the new rules, issued by the Securities and Exchange Commission, designed to eliminate conflicts of interest by agencies that rate insurers' financial strength.

And there was at least one piece of good news, Mr. Ewing noted. The Internal Revenue Service reversed course and abandoned a proposed rule that would have stripped away tax breaks from hundreds of captives.

Several risk managers also noted that former New York Gov. Eliot Spitzer's political downfall last spring after he was linked to a prostitution ring was a news story of great human interest, even though it had no impact on risk management. Mr. Spitzer was elected governor on the strength of his investigations as New York's attorney general, including his probe into insurance industry bid rigging.

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Business Insurance

AIG gets government bailout, begins asset sale to repay loan

The federal government's bailout of American International Group Inc. happened in the fall, but the implications of the bailout are likely to continue indefinitely.

In September, as AIG faced the prospect of collapse because of its disastrous involvement in the credit swap default market, government officials decided the insurer was too

1

big to fail.

AIG signed a definitive agreement with the Federal Reserve Bank for a two-year, \$85 billion revolving credit facility in return for the government taking a 79.9% ownership of the insurer.

But as it turned out, the initial loan was not enough and a new, \$37.8 billion credit agreement was announced in October. This took AIG's total available bailout funding to \$122.8 billion.

Then in November a revised bailout plan was announced. The terms included a revised \$60 billion credit facility, purchase of AIG preferred shares and warrants and establishment of two special-purpose entities.

Still unknown is whether the federal government will retain its ownership of AIG, and the implications if it does.

Meanwhile, the company formally announced plans to slim

down as an insurer, stating it planned to focus largely on its core property/casualty business.

Chairman and Chief Executive Officer Edward M. Liddy, named by the Federal Reserve Board to replace Robert B. Willumstad, said the company intends to sell off everything but its core commercial property/casualty insurance and foreign general insurance businesses, while retaining a "continuing ownership interest" in its foreign life insurance operations.

"Everything else that doesn't fit under that definition we are considering for sale," Mr. Liddy

said during a webcast with analysts.

Questions remain, though, about how easily its earmarked assets would be sold. Assets sold so far include its Swiss-based private bank, AIG Private Bank Ltd., to an Abu Dhabi investment company, and the sale of AIG's interest in Omaha, Neb.-based Tenaska Inc. back to the energy producer.

Meanwhile, AIG reportedly has been aggressively pricing coverage in an effort to retain business, though AIG disputes that claim.

In addition, many of its senior

underwriting executives have left the company for competitors. Last week, for instance, longtime AIG executive Kevin Kelley, formerly chairman and chief executive of AIG's Lexington Insurance Co., was named CEO of Hamilton, Bermuda-based Ironshore Inc.

At the same time, the insurer has continued to face criticism on various fronts, including concerns about the more than \$400,000 it spent for an event at a luxury resort shortly after its initial government bailout was announced.

At a congressional hearing in October, former AIG chief execu-

tives Martin Sullivan and Mr. Willumstad came under repeated fire for the company's practices regarding executive compensation and the decision to keep the former head of AIG Financial Products—whom many blame for AIG's near collapse—on a previous \$1 million monthly retainer.

New York Attorney General Andrew Cuomo also criticized the insurer for its "unwarranted and outrageous" expenditures.

The beleaguered insurer reported a \$34.06 billion loss for the nine months ended Sept. 30.

—Judy Greenwald

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Insurers' investments take a hit as financial crisis worsens

American International Group Inc. was not the only insurer to suffer significant financial damage as a result of the economic downturn.

2 **AIG**, of course, went to the brink of bankruptcy before being rescued by the federal government. But by the end of the year, other insurers took steps to tap federal resources as well.

In fact, Hartford Financial Services Group Inc. bought a Florida savings bank to qualify for up to \$3.4 billion in federal bailout funds. Hartford reported a \$2.63 billion third-quarter loss.

A dozen major U.S. commercial property/casualty insurers reported a \$34.06 billion loss for the nine months that ended Sept. 30, according to a *Business Insurance* survey.

Even excluding AIG's \$37.63 billion loss, the remaining insurers reported a 73.2% drop in net income, to \$3.57 billion, compared

with the year-earlier period. Two other insurers also reported losses while the remaining nine reported double-digit declines in net income.

Elsewhere, Europe's three largest reinsurers saw their third-quarter earnings plummet due to poor investment returns and heavy catastrophe claims.

Munich Reinsurance Co., the world's largest reinsurer, saw its profit for the three months ending Sept. 30 plummet by 99% to €12 million (\$16.9 million), while rival Swiss Reinsurance Co. posted a

304 million Swiss franc (\$277.2 million) loss for the three-month period. Hannover Reinsurance Group slid to a loss of €142.8 million (\$201.4 million) for the period.

Despite the losses, property/casualty insurers tended to fare better than other financial institutions, including life insurers. Except for AIG, most property/casualty insurers weren't greatly affected by the subprime mortgage meltdown. But insurers tend to invest in fixed-income securities, such as corporate

and municipal bonds, both of which have dropped in value as the financial crisis worsened.

Property/casualty insurers in general remained leery of participating in federal bailout plans. Although some life insurers attempted to qualify for federal backup, the property/casualty industry's major trade associations remained steadfastly opposed to having property/casualty insurers seek the federal aid available to other financial institutions as the year drew to a close.

—Mark A. Hofmann

Former execs of Gen Re, AIG convicted over bogus finite deal

It was a trial involving astonishing charges filed against top executives working at two of the best-known companies in the insurance industry.

3 **Four** former executives of General Re Corp. and

one of American International Group Inc. stood accused in U.S. District Court in Hartford, Conn., of violating federal law in connection with what prosecutors called bogus reinsurance transactions in which no risk was transferred.

The accused were former Gen Re Chief Executive Officer Ronald Ferguson; former Gen Re Chief Finan-

cial Officer Elizabeth A. Monrad; Christopher P. Garand, former Gen Re senior vp in charge of U.S. finite underwriting; Robert D. Graham, Gen Re's former senior vp and legal counsel; and Christian M. Milton, a former AIG vp for reinsurance. The five faced charges of conspiracy, securities and mail fraud and making false statements to the Securities

and Exchange Commission.

The trial began in early January, and testimony lasted more than five weeks. Prosecutors alleged that the defendants engineered a bogus loss portfolio deal that was intended to help AIG inflate its loss reserves by \$500 million in 2000 and 2001 to counter stock analyst concerns about AIG's reserve levels. While the deal appeared to transfer risk, the defendants had an unwritten side agreement that AIG would not be billed for losses and that AIG would refund Gen Re's \$10 million premium and pay it a \$5 million fee, the government charged.

The defense attempted to discredit the testimony of the government's star witnesses—former Gen Re Senior Vp Richard Napier and John Houldsworth, former chief executive officer of Gen Re's Cologne Re Dublin unit, both of whom already had pleaded guilty to conspiracy. But in late February, the

jury returned verdicts of guilty on all counts against all the defendants.

In considering what sentences to impose, U.S. District Judge Christopher Droney—who had presided over the trial—found that drops in AIG's stock price on three days in 2005 could be linked to disclosures about AIG's bogus loss portfolio deal with Gen Re. The declines resulted in shareholder losses of between \$544 million and \$597 million, he concluded.

As the amount of loss is the largest single factor in setting sentence recommendations under federal sentencing guidelines, Judge Droney's findings produced guideline recommendations of life in prison for all five defendants. Observers doubted, however, that any of the convicted would receive such lengthy terms.

Judge Droney is scheduled to sentence the first of defendants—Mr. Ferguson—on Dec. 16.

—Mark A. Hofmann

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Rates continue dropping for most P/C coverages

Property/casualty insurers slashed rates in all lines through most of 2008 as abundant market capacity spurred insurer competition despite mounting losses, until the weakening economy's negative impact on insurers' balance sheets triggered rate stabilization in the fall.

The willingness of insurers to cut rates regardless of deteriorating claims conditions was most evident in the directors and officers liability market.

4 While financial institutions and real estate risks faced rate hikes of up to 200% and a doubling of self-insured retentions as subprime mortgage-related securities claims mounted, risks in other industries were able to negotiate 5% to 40% rate cuts.

Likewise, the property market

remained soft until the third quarter despite a rash of tornadoes and extensive flooding this year. Accounts that renewed midyear negotiated 15% to 30% rate cuts off of their 2007 rates, which had been pared 5% to 7% from the previous year.

Energy risks with offshore operations in the Gulf of Mexico saw their rates drop 20% to 30% at midyear, while onshore risks negotiated 15% to 20% rate reductions. But that was before Hurricane Ike caused \$7 billion to \$12 billion of onshore and offshore losses in mid-September.

Workers compensation and auto fleet insurers also cut rates during the year by double digits despite rising claim activity.

Marine insurers, backed by plenty of capacity, attempted to win greater market share by agreeing to hefty rate cuts. Those insurers' losses have mounted this year because

Continued on next page

CONTINUED FROM PREVIOUS PAGE

of the increase of piracy off the Somali coast, but the market is expected to raise rates only for shippers that move their goods through that area.

General liability insurers were more circumspect at midyear, seeking more information and walking away from some accounts. But ample capacity still fed competition, with insurers typically cutting rates 3% to 10%.

Meanwhile, reinsurers were cutting rates from 5% to 25%. But reinsurers expect increased demand for reinsurance as a form of capital relief will allow them to increase rates by at least 10% or more in certain lines at Jan. 1, 2009, renewals.

—By Dave Lenckus

IRS drops plan to remove tax break for captives

In 2008, the captive insurance industry scored a big victory over the Internal Revenue Service.

In February, the IRS withdrew a rule it had proposed five months earlier that would have stripped a key tax advantage from hundreds of captives.

Under the withdrawn rule, captives no longer would have been allowed to take an immediate tax deduction at the time reserves are established. Instead, tax deductions would have been allowed only at

the time claims are paid.

The change in the timing of tax deductions would have applied to sponsors that use their captives to fund risks of various corporate affiliates and that file a consolidated tax return covering the affiliates and the captive.

For captives writing long-tail business, experts said such a change would have been extraordinarily costly, making captives much less attractive financially and perhaps leading sponsors to move their insurance subsidiaries offshore.

The publication of the IRS rule in September 2007 triggered a massive lobbying effort by the domestic cap-

tive industry. Two of the nation's largest captive trade associations—the Vermont Captive Insurance Assn. and the Captive Insurance Cos. Assn.—banded together to form the Coalition for Fairness to Captive Insurers to battle the IRS. The coalition retained the law firms of Dewey & LeBoeuf L.L.P. in New York and McDermott, Will & Emery L.L.P. in Chicago to prepare a rebuttal of the IRS' position.

It wasn't only lobbyists and lawyers that took on the IRS. They were joined by federal legislators, such as Sen. Patrick Leahy, D-Vt., who warned Treasury Secretary Henry Paulson of the economic damage Vermont, the nation's

largest captive domicile, would suffer if the IRS rule was adopted.

Just a few days before a scheduled hearing it was to hold, the IRS, with little explanation, withdrew the rule.

But other threats to captives remain. California has been aggressively asserting its right to determine whether risk retention groups licensed in other states are writing coverage permitted under California law and the federal law that authorized RRGs. RRG advocates say out-of-state regulators lack such authority, with federal law delegating that responsibility to the state where an RRG is licensed.

—By Jerry Geisel

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CNA

Top risk management newsmakers of 2008



Mr. Dinallo

New York Insurance Superintendent **Eric Dinallo** kept the state's insurance department in the news throughout the year as he tackled tough, often contentious issues.

On the broker front, Mr. Dinallo and New York Attorney General Andrew Cuomo in July sought to address the compensation system

established by their predecessors in 2005 and 2006 settlements with certain brokers and insurers, by holding three separate joint hearings on the issues of contingent commissions and compensation disclosure requirements.

Mr. Dinallo also tackled timely policy issuance by calling on insurers and brokers doing business in the state to develop and implement practices within a year to ensure that documentation is delivered to policyholders within 30 days of inception in most circumstances.

He also sought to relax reinsurer collateral rules in New York and

began talking about reviving the New York Insurance Exchange, a Lloyd's of London-style marketplace for reinsurance and other large-scale insurance products that originally shut down in 1987 due to a soft market, poor claim experience and inadequate capitalization.

U.S. District Court Judge **Christopher Droney** may lack the star power of Judge Judy, but in insurance circles, he's a man to be reckoned with.

The Hartford, Conn.-based jurist presided over the trial of five former reinsurance executives accused of executing a sham reinsurance deal between General Re Corp. and American International Group Inc. that made AIG look financially stronger than it was. After a jury convicted the five on all counts, it was up to Judge Droney to determine how much the fraudulent deal cost AIG shareholders and how those convicted of the charges should be punished.

Last month, after weeks of briefings and oral arguments, Judge Droney found that drops in AIG's stock price on three days in 2005

could be linked to disclosures about AIG's bogus loss portfolio deal with Gen Re. He determined the declines resulted in shareholder losses of more than \$500 million. The amount of loss is the largest single factor in setting sentence recommendations under federal guidelines and a loss of that magnitude could mean life sentences for some of the defendants.

Judge Droney is scheduled to hand down the sentence on the most prominent of the defendants—former Gen Re Chief Executive Officer Ronald Ferguson—on Dec. 16.

One could almost hear the sigh of relief at Marsh & McLennan Cos. Inc. in January when it hired well-respected insurance veteran **Brian Duperreault** to lead the struggling firm back to prosperity.

The former ACE Ltd. chief executive officer came out of retirement to replace outgoing CEO Michael G. Cherkasky, whose three-year tenure at the helm of the New York-based MMC was fraught with turmoil.

It didn't take long for Mr. Duperreault to boost morale at the firm and get employees to feel positive about the organization again. He also very quickly got to work on a

turnaround plan that included taking a hard look at all of MMC's operating units, divesting some assets, reducing expenses and laying off employees.

"I didn't take the job to be a caretaker or oversee incremental improvements and results," Mr. Duperreault said on a May conference call with analysts.

The first signs that recovery efforts were under way came this

summer when MMC reported better-than-expected second-quarter results, driven by strong revenue and margin improvement at its financially challenged brokerage unit.

In November, MMC announced plans to issue up to \$500 million in stock to fund future acquisitions, sparking speculation that the firm could be looking to make a large deal.

It was not the way **Ronald E. Ferguson**, former chief executive officer of General Re Corp.—or anyone else—would want to spend retirement.

Once one of the most prominent executives in the reinsurance industry, Mr. Ferguson was found guilty in February on 16 federal counts in connection with a fraudulent 2000 reinsurance deal between Gen Re and American International Group Inc. The transaction occurred while Mr. Ferguson headed Gen Re.

During a trial in federal court in Hartford, Conn., prosecutors alleged Mr. Ferguson knew the loss portfolio transfer was a no-risk transaction for AIG that served to make AIG

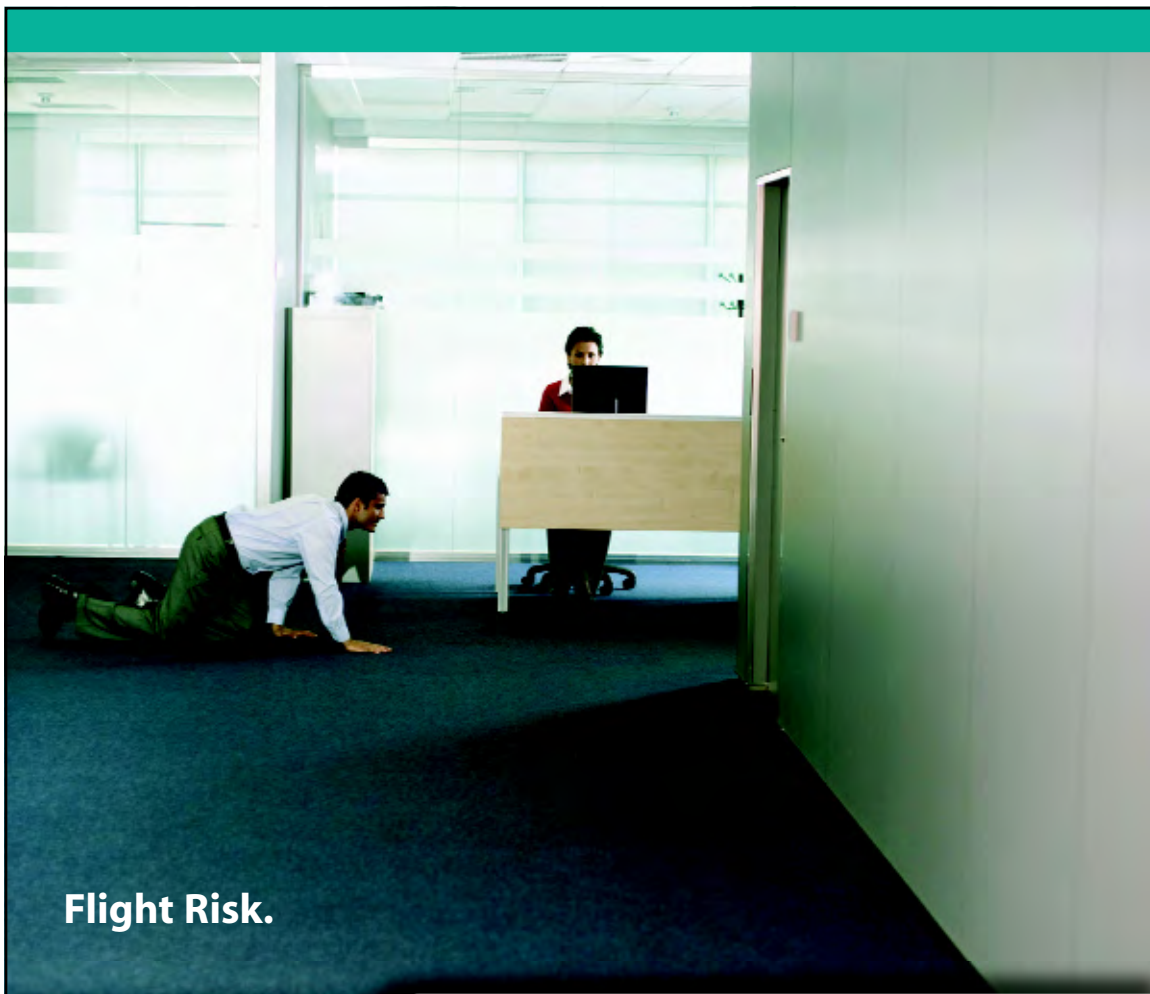
appear stronger than it was. Although Mr. Ferguson denied there was ever any side agreement not to cede risk to AIG and that he believed the deal to be legitimate, a federal jury found prosecutors' arguments more compelling.

Mr. Ferguson's attorney argued that he should receive a lighter sentence than called for under federal guidelines because he was not personally enriched by the deal. Whether that argument sways the federal judge who presided over the case will not be known until Dec. 16, when Mr. Ferguson learns his sentence.

William Gilman, the alleged architect of Marsh Inc.'s infamous bid-rigging scheme for excess casualty placements, was found guilty in February of violating New York's antitrust law, but was acquitted on 20 other counts of fraud and larceny.

In the first conviction to come out of New York's bid-rigging investigation into the brokerage, Mr. Gilman was sentenced to 16 weekends in jail, 250 hours of community service and five years of probation. His sentence has been stayed pending his appeal.

Mr. Gilman, a former managing director and executive marketing director in Marsh's Global Broking unit, and six other former Marsh executives were accused of colluding with certain insurers to



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arrange noncompetitive excess casualty bids and conveying the bids to clients under false pretenses.



Mr. Gilman

Edward J. McNenny, former managing director and global placement director, was convicted with Mr. Gilman. Former managing directors Joseph Peiser, Greg J.

Doherty and Kathleen M. Drake are on trial in New York for their alleged roles in the scheme. And former Marsh Senior Vps William L. McBurnie and Thomas T. Green Jr. are awaiting trial.

Former American International Group Inc. Chairman and Chief Executive Officer **Maurice R.**

Greenberg has never been shy about voicing his opinions, and that continued to hold true as he watched the company he once led become enveloped in crisis during the past several months.

He has been particularly outspoken about the terms of the federal bailout. In November, for instance, Mr. Greenberg, who now is chairman

and CEO of C.V. Starr & Co. Inc., said "there's a lot of money in the Middle East and Asia" that would be willing to invest in AIG. But he said such foreign investors will not put money into a "nationalized company."

He also has charged that Citibank received a more favorable deal from the federal government than AIG.

Meanwhile, litigation between Mr. Greenberg and his former company continued. In December, a state judge refused to dismiss charges, including breach of fiduciary duty, against Mr. Greenberg and others in an ongoing battle with AIG over the insurer's shares.

In June, in a parallel federal case, a federal judge granted Starr's motion to dismiss four of AIG's charges, including breach of contract, but denied its bid to dismiss three others, including breach of fiduciary duty and trust.



Mr. Greenberg

Edward M. Liddy

proved that he was a man up for a challenge when he became chief executive officer of American International Group Inc. in September.

Mr. Liddy, the retired CEO of Allstate Corp., became AIG's third CEO in four months. He faced a daunting task as AIG struggled with hundreds of billions of dollars of exposure to credit default swaps that nearly drove the financial services industry giant into bankruptcy. That led to a massive federal bailout in which the government received a 79.9% equity stake in AIG. More



Mr. Liddy

government assistance followed.

Mr. Liddy found himself under fire from Congress and regulators after AIG allowed previously booked events at resorts for independent producers and others to go forward despite the bailout. The company also drew criticism for bonuses and compensation paid to former executives. After

Mr. Liddy agreed to freeze those outlays, AIG also adopted voluntary executive compensation restrictions.

Under the new rules, Mr. Liddy will receive an annual base salary of just \$1 for 2008 and 2009, with

the rest of his compensation consisting entirely of equity grants. If he can turn the company around, those equity grants could potentially pay quite handsomely for a dollar-a-year man.

XL Capital Ltd.'s Chief Executive Officer **Michael S. McGavick** may have an even bigger task ahead of him than when he took over the reins at the Bermuda-based insurer in May, as XL said last week that it is exploring alternatives for its future.

The former SAFECO Corp. president and CEO was the outsider chosen to succeed XL's



Mr. McGavick

longtime leader Brian O'Hara—and charged with working to revive the struggling insurer. The industry veteran has had to negotiate steep challenges,

including XL's massive exposure to financial guarantee insurer Security Capital Assurance Ltd. An August commutation agreement with SCA relieved some pressure on XL, but resulted in a \$1.4 billion charge

Continued on next page

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reported in the company's third quarter. XL raised roughly \$2.88 billion in capital to fund the deal, as well as additional capital to cushion itself from \$221 million in losses related to Hurricanes Ike and Gustav.

XL's third quarter net loss totaled \$1.62 billion.

Analysts note that Mr. McGavick inherited XL's financial difficulties, which have only been exacerbated by growing financial market problems this year.

What remains to be seen is how he will steer XL in the months to come as the insurer grapples with those problems and plots its course for the future.

Few people would mistake Treasury Secretary **Henry Paulson** for a radical.

But the onetime Goldman Sachs executive offered a truly radical plan for modernizing the nation's financial services industry in March when he released a blueprint for regulatory reform. One of the blueprint's key recommendations



Secretary Paulson

was to allow property/casualty and life insurers to choose whether to be regulated by state authorities—as all are today—or to be overseen by a new federal regulator.

Property/casualty insurers have been split on the issue for years. Although legislation had been introduced—but never passed—to create optional federal charters, Mr. Paulson's call gave new hope to OFC advocates.

But the incoming Obama administration is not bound by the recommendations of its predecessor. At a time when even more radical steps are being taken to shore up the tottering economy as a whole, the OFC may find itself on the back burner for some time to come.

It's hard to say whether **Eliot Spitzer** will be more remembered

for his tenacious attack on the insurance industry in 2004 and 2005 or for being "Client No. 9."

The former New York attorney general-turned-governor abruptly resigned from office in March after he was identified in federal court papers as a patron of an expensive international prostitution ring.

He will not face criminal charges, however, as federal investigators said in November that they found no evidence that Mr. Spitzer



Mr. Spitzer

misused public or campaign funds to pay for prostitutes.

As attorney general, Mr. Spitzer launched a series of investigations that resulted not only in billions of dollars in settlements but

also changed the way insurers and brokers do business and altered the structures of the companies themselves.

He is probably best known for his 2004 fraud and bid-rigging suit

against Marsh & McLennan Cos. Inc. and his 2005 investigation into a sham reinsurance deal between American International Group Inc. and General Re Corp. That investigation led to the ouster of

longtime AIG Chief Executive Officer Maurice R. Greenberg and the conviction of former Gen Re CEO Ronald Ferguson and four other former executives of Gen Re and AIG.

2008: A look back at major events

JANUARY

■ Marsh Inc. overhauls its upper management for the second time in four months. The New York-based brokerage also reorganizes its global structure by consolidating its business into two geographical divisions. Former ACE Ltd. Chairman and Chief Executive Officer Brian Duperrault is named a few weeks later as the new president of Marsh & McLennan Cos. Inc.

■ Trial begins in federal court in Hartford, Conn., for five former executives of General Re Corp. and American International Group Inc. accused of having engineered a 2000 loss portfolio transfer from Gen Re that involved no risk and served only to inflate AIG's loss reserves to counter investor concerns.

■ The Supreme Court ruling in *Stoneridge Investment Partners L.L.C. vs. Scientific-Atlanta Inc.; Motorola Inc.* limits the potential liability of third parties in securities fraud lawsuits.

FEBRUARY

■ An explosion at the Imperial Sugar Co. refinery in Port Wentworth, Ga., kills 13 workers and injures another 40. The Occupational Safety and Health Administration later alleges safety violations and proposes an \$8.7 million fine against the company and two affiliates.

■ Two former Marsh Inc. executives are found guilty of breaking anti-trust law by a New York judge but are acquitted on 20 other charges against them, including fraud and grand larceny. The convictions are the first to come out of the state's bid-rigging investigation of the brokerage.

■ A federal jury in Hartford, Conn., finds five former executives of Gen Re and AIG guilty on all counts stemming from a sham finite reinsurance deal. Sentencing is postponed until later in the year.

MARCH

■ Windstorm Emma tears across parts of Central Europe, causing insured losses of more than \$1 billion.

■ New York Gov. Eliot Spitzer, who as state attorney general attacked bid-rigging and other abuses in the insurance industry, abruptly resigns after admitting to having patronized prostitutes.

■ XL Capital Ltd. chooses former SAFECO Corp. President and CEO Michael McGavick as its new CEO.

■ Aon Corp. founder and Chairman Patrick G. Ryan announces he will retire later in the year.

■ The U.S. Treasury Department endorses allowing insurers and producers to choose federal rather than state regulation.

APRIL

■ Louisiana's Supreme Court upholds the flood exclusion in a commercial all-risks insurance policy, curtailing the ability of some policyholders to get coverage for Hurricane Katrina-related claims.

■ Joseph P. Brandon steps down as CEO of Gen Re. Federal authorities had launched an investigation into the company and Mr. Brandon over any role they might have played in the sham reinsurance transactions for which five former Gen Re and AIG executives had been found guilty in February.

■ Two U.S. representatives introduce a bill to allow risk retention groups to write property as well as liability risks. The measure, however, does not become law before the 110th Congress adjourns.

■ Liberty Mutual Group Inc. announces it will buy SAFECO Corp. for approximately \$6.2 billion.

MAY

■ The House gives final approval to the Genetic Information Nondiscrimination Act, which bans making health insurance and employment decisions based on individuals' genetic information. President George W. Bush signs the bill into law later in the month.

■ The Insurance Services Office Inc.'s Property Claim Services unit reports catastrophes caused \$3.35 billion in insured property damage in the United States during the first three months of 2008. That makes the first quarter of the year the costliest first quarter in terms of catastrophe losses in 10 years.

■ The Assn. of Insurance & Risk Managers announces it is launching a benchmarking service for insurance buyers in the United Kingdom. The survey will track insurance buying trends.

JUNE

■ The Supreme Court rules in *CBOCS West Inc. vs. Hedrick G. Humphries* that racial retaliation employment claims are allowed under the Civil Rights Act of 1866, even though the Reconstruction era law does not explicitly say so. Employment law experts say the decision could spur more claims of race-based retaliation.

■ Willis Group Holdings Ltd. announces it will acquire Hilb Rogal & Hobbs Co. in a \$2.1 billion buyout. The merger of the brokerages receives final approval later in the year.

■ AIG ousts President and CEO Martin Sullivan as investor pressure for change grows. Robert Willumstad, AIG's chairman, replaces

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YEAR IN REVIEW - RISK MANAGEMENT

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him until he, too, is forced out in September as the insurance giant's fortunes continue to falter.

■ The Supreme Court holds in *Exxon Shipping Co. et al. vs. Grant Baker et al.* that punitive damages cannot exceed compensatory damages under federal maritime law.

JULY

■ The Rhode Island Supreme Court rejects the state's attempt to use its public nuisance law to force three former makers of lead-based paint to fund the inspection and remediation of hundreds of thousands of structures that might contain lead paint. Although the ruling affects only Rhode Island, tort reform advocates say it could doom similar approaches using public nuisance law being considered in other states.

■ AIRMIC calls on the U.K.'s Financial Services Authority to make full disclosure of broker remuneration mandatory.

■ New York authorities hold a series of public hearings as they consider whether to allow the world's largest brokers to accept contingent commissions again. In 2005, the three largest brokers entered into agreements with New York authorities to cease accepting contingent commissions to settle charges that they had steered clients to the insurers that paid the highest commissions.

■ ACE Ltd. completes its redomestication to Switzerland from Bermuda.

AUGUST

■ A three-judge panel of the 9th U.S. Circuit Court of Appeals overturns a lower court's ruling that a flood exclusion in an all-risk excess policy was ambiguous. The decision adds to a series of decisions that interpret the flood exclusion in an insurer's favor when policyholders seek coverage for Hurricane Katrina-related claims.

■ Aon announces that it will buy Benfield Group Ltd. for \$1.75 billion. The move solidifies Aon's position as the world's largest reinsurance intermediary.

■ A group of major European companies forms the European Captive Owners & Reinsurance Owners Assn. in Luxembourg. One of the new group's key goals is to simplify the rules for captives under Solvency II.

SEPTEMBER

■ Hurricane Gustav misses New Orleans but makes landfall in Louisiana as a Category 2 storm. Estimates of insured damage run as high as \$7 billion, but losses aren't enough to reverse a still-softening property/casualty market. Hurricane Ike later blasts the Louisiana and Texas coasts, causing as much as \$21 billion in insured damages, according to catastrophe modeler Risk Management Solutions Inc.

■ Reinsurance professionals meeting at the annual Rendez-Vous de Septembre predict rates will continue to drop absent major catastrophe losses.

■ The Federal Reserve Board provides AIG with an \$85 billion revolving credit facility as the insurer faces bankruptcy as liquidity problems stemming from the

insurance holding company's large portfolio of credit default swaps nearly destroy it. In return, the government takes a 79.9% equity share in the insurer. The Fed also replaces Chairman and CEO Robert Willumstad with former Allstate Corp. CEO Edward Liddy.

■ President Bush signs into law the ADA Amendments Act, which requires judges to interpret the Americans With Disabilities Act broadly when determining whether an individual has been discriminated against because of a disability. The new law enjoys the support of employment groups and advocates for the disabled.

OCTOBER

■ Wells Fargo & Co. wins a battle

with Citigroup Inc. to acquire Wachovia Corp. The deal could make Wells Fargo the fourth largest insurance broker as it adds Wachovia's brokerage business—which generated \$422.5 million in 2007—to its own brokerage operations, which generated \$1.28 billion in 2007.

■ AIG, already under fire from congressional critics over its sponsorship of corporate events for independent producers, agrees to help New York Attorney General Andrew Cuomo recover bonuses and other payments to former executives.

■ New York Insurance Superintendent Eric Dinallo calls on insurers and brokers doing business in the Empire State to craft practices

that would assure that documentation is delivered to policyholders within 30 days of inception under most circumstances.

NOVEMBER

■ Democrats sweep both houses of Congress, as well as recapture the White House, raising the possibility that federal government will become more involved in insurance regulation. President-elect Barack Obama had advocated increasing the federal role in guaranteeing catastrophe insurance on several occasions during the campaign.

■ AIG and the federal government work out a deal to revise the terms of Washington's bailout of the troubled company.

■ Hartford Financial Services Group Inc. buys a Florida savings bank to qualify for up to \$3.4 billion in federal bailout funds. Few other property/casualty insurers show any interest in tapping funds available through the federal government's Capital Purchase Program.

DECEMBER

■ Longtime American International Group Inc. executive Kevin Kelley has been named chief executive officer of Ironshore Inc. Mr. Kelley was formerly chairman and chief executive of AIG's Lexington Insurance Co., the world's largest excess and surplus lines insurer. Bob Deutsch, Bermuda-based Ironshore's founding CEO, was named the insurer's president.



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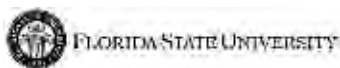
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- Aon Corp.
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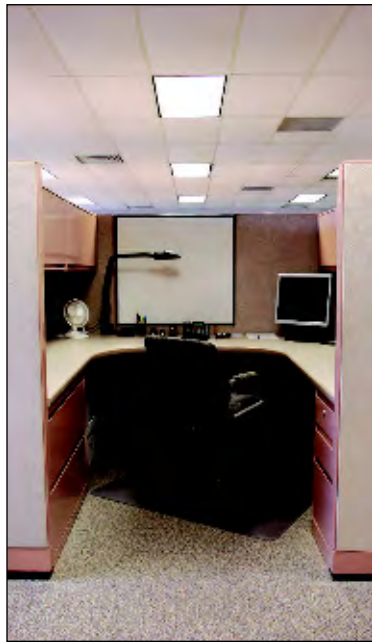
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programs and design customized plans to match members' needs, according to the Knoxville, Tenn.-based software company.

The NavigatorMD software tracks claims history, pharmacy data, health risk assessments and relevant demographics to assess each employer's particular workforce, determine if individuals are following treatment regimens, and address emerging risk factors or gaps in health care, the company said.

San Antonio, Texas-based Personalized Prevention has programs to improve workforce health and productivity, lower health care costs and encourage individual behavior changes, the company said.

For more information contact Ernest T. Youngblood, founder, president and chief executive officer of NavigatorMD at 888-462-8428, ext. 101 or Lisa VanAckeren, executive vp of Personalized Prevention at 210-481-7584.

Swiss Re introduces Agency Shield for E&O

OVERLAND PARK, Kansas—Swiss Re Commercial Insurance has announced the Agency Shield Program for its insurance agency errors and omissions policyholders.

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BI's Products & Services column reports on new product offerings.

Please send Product & Services news to: Colleen McCarthy, 711 Third Avenue, New York, NY 10017 or e-mail cmccarthy@businessinsurance.com.

BI's Market Moves column reports on activities by insurance industry companies and related entities.

Please send Market Moves news to: Zack Phillips, zphillips@businessinsurance.com.

ACE unit to focus on indoor air quality

PHILADELPHIA—ESIS Inc., a unit of ACE USA, has launched an environmental consulting service to help organizations minimize their exposure to indoor air quality hazards.

The Leadership in Energy and Environmental Design Consulting Practice is offered as part of ESIS's Global Risk Consulting Services and will be led by J. Michael Strange, a certified industrial hygienist.

The group will assist customers in achieving sustainable building and maintenance practices with a focus on energy-efficient design. Consultants will evaluate ventilation and exhaust systems, waste management processes, identify sources of chemicals or pollution, evaluate natural lighting, and recommend alternative materials. The service includes program development for new projects as well as on-site evaluation and auditing for existing buildings.

The service can be used by companies in various stages of LEED certification, part of the U.S. Green Building Council rating system, according to the Philadelphia-based third-party administrator.

For more information, contact Michael Strange, practice leader at michael.strange@esis.com or Frank Westfall, vp-environmental services at francis.westfall@esis.com.

Benefits software helps collect, organize data

SAN ANTONIO, Texas—Personalized Prevention, a wellness and risk management program from Van Ackeren Consulting L.L.C., has begun using benefits intelligence software from NavigatorMD Inc., according to a joint release announcing the partnership.

The benefits software will collect and organize health care data into a single data warehouse, allowing benefit managers to view their

A VICIOUS TORNADO. AN UPCOMING RACE. YET THE ATLANTA MOTOR SPEEDWAY COULD REMAIN



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Survey: Most ready for risk

CONTINUED FROM PAGE 4

the economy is the No. 1 obstacle to improving risk preparedness.

"The economy is really putting a lot of weight on what we do on a daily basis," said Mr. Baker, who participated in the survey and agreed to a follow-up interview.

Nearly 37% of respondents said they communicate the risk of loss of reputation to employees once a year and nearly 25% do so two to three times annually.

"We communicate with our employees five to six times a year, if not more, often regarding our reputation in the marketplace," Mr. Baker said. "It could be because of the nature of our product. Our name brand means a lot."

Nearly 32% of respondents said they communicate two to three times a year with partners about potential supply chain interruption or disruption, but a nearly equal percentage was split between such communications only once a year and doing so more than six times in a year.

One point on which there was strong agreement is that risk transfer mechanisms, such as insurance, genuinely transfer the various risks.

"It's always important, all the time, regardless of the economy," said Bailey Pipkin, risk manager of Bell, Tenn.-based frozen vegetable supplier PictSweet Co. Mitigating and spreading anticipated risks saves an organization's money without tying it up at a time when liquidity is scarce. "It goes to the very heart of what we do," said Mr. Pipkin, who also participated in

the survey.

The survey found that 80.3% of respondents plan to buy about the same amount of insurance in the future and 16.7% plan to buy more coverage. Just 3% anticipated buying less insurance in the future.

Broker roles

As for factors influencing the survey group's choice of risk adviser, knowledge of the business/marketplace and experience/expertise were cited most often.

Nearly 72% of respondents said their reliance on brokers looks to remain the same, but nearly 25% said they will rely on their brokers more in the future for answers in the five areas of risk.

Given the poor economy, Solo Cup's Mr. Baker suggested that the role of the broker will grow.

"I think it'll increase in the negotiations for rates on different pieces of the entire insurance package. The clients are going to be much more demanding of what the brokers do or don't do," Mr. Baker said.

"What I found is that the big brokers are getting very complacent. They're not offering the level of service that they used to and the smaller brokers are making a huge comeback right now. They're offering a lot of services, a lot of expertise that the big brokers either are unwilling or unable to offer."

According to the survey, risk managers said that more benchmarking of peer organizations, enhanced technology and tools, innovative solutions, and a better understanding of the organization's business and industry are necessary to improve broker value.

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General Motors Corp. no longer an 'unsinkable ship'

By John J. Hampton

The USS General Motors was the grandest cruise ship ever built when it came out of the shipyard in 1908. Luxurious and unsinkable, it was destined to overshadow the USS Ford and the USS Chrysler, two other fine vessels. GM maintained its leadership position for a long time.

Rather than unsinkable, GM's bulkheads were only somewhat watertight. It had other design flaws, but a string of captains and first mates saw no need to make changes. As former GM leader Charles Wilson said in the 1950s: "What was good for the country was good for General Motors and vice versa."

The ship's owners took excellent care of the ship's officers. From the vessel's formidable captain's quar-

ters on the Renaissance deck, the entire world looked rosy. In 1986, Chief Executive magazine named Roger Smith, then GM's captain, as CEO of the year.

could afford. The vessel once had more than 1,000 crew members supporting a handful of retirees who left the vessel with lifetime health care and a pension adjusted for inflation. During labor negotiations, the UCW insisted on maintaining the benefits approved by earlier captains. At first, no problem existed. Crew members took early retirement with a relatively short life expectancy after years in the engine room and at sea. As time passed, the retirement pool grew dramatically, accompanied by a longer life expectancy. Although

the agreements with the UCW grew increasingly untenable, a series of captains and the union did not address the situation.

This year, a serious problem became a crisis. The vessel was crossing the North Atlantic during iceberg season. Because the shipbuilders believed the USS General Motors was unsinkable, the ship did not carry enough lifeboats. The captain, proud of recent successful voyages to China, had the vessel going full speed ahead. Unfortunately, it hit an iceberg as did the USS Ford and USS Chrysler that were on the

same pattern. The situation was not good for the three vessels.

GM's captain Rick Wagoner, Ford's Alan Mullally, and Chrysler's Robert Nardelli launched their private yachts and steamed toward Washington to talk to Congress. Chief mate Ron Gettelfinger from the UCW joined them. They said they had no warning about risk when icebergs suddenly hit their vessels. They told Congress they needed money from the government to rescue them. When asked what would be done with the money, they said they would buy

lifeboats. When asked what they had been doing in recent years, they pointed out that all three vessels had increased the size of the musical band for the enjoyment of passengers and crew. When asked what would happen if Congress denied the request, they explained that the JSS Toyota, JSS Honda, GSS Volkswagen and other shipping lines would increase their presence in U.S. ports and may even hire their displaced crew members.

Any day now, we can expect Congress to act upon the request from the captains.

Emerging Risk STRATEGIES



John J. Hampton is the KPMG Professor of Business and Dean of the School of Professional and Continuing Studies and Graduate Business Programs at St. Peter's College in New Jersey. To read Mr. Hampton's columns and interviews, visit www.BusinessInsurance.com/ERM.

At the time, the USS GM was dealing with some quality-of-voyage issues. The vessel still had comfortable facilities, particularly for passengers on the Cadillac deck. The problem was that the vessel was somewhat run down compared with the JSS Toyota, JSS Honda, and GSS Volkswagen. Passengers noticed a declining quality of the fit and finish of cabins, failure to replace aging sheet metal and paint in public areas, and serving lower-quality food and beverages.

The bursar talked with a succession of captains about the vessel's growing legacy obligations, particularly pension and health care benefits for retired crew members. It also paid ongoing wages to nonworking engine room employees displaced by automation. He was concerned that the benefits negotiated with the United Crew Workers were more generous than the vessel

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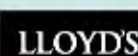
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Compensation: Hard times may hit guaranty funds

CONTINUED FROM PAGE 4

by Dec. 7.

Companies nationwide often meet their workers comp obligations while reorganizing under a Chapter 11 bankruptcy filing. But several fund directors said a rising bankruptcy rate is a warning that companies may default on claims in the future.

"The last thing they do before they shut off the lights is to default on paying their workers comp claims," said Jeff Pettegrew, executive director of the California Self Insurers' Security Fund based in Walnut Creek.

Many states require self-insureds to contribute to state security funds. Additionally, they require companies to post collateral either with state regulators or the security fund as a condition of self-insuring their workers comp risks.

A company's posted collateral usually is exhausted before tapping the security fund.

Should they see a participating company facing financial troubles, fund managers can apply various measures to require the struggling self-insured company to post additional collateral.

In some states, a concern about future defaults also allows a security fund to increase its routine assessment of all members, although regulations can limit the amount.

In worst-case scenarios, some funds would have to assess members after defaults to make up for a shortage of funds.

Fund managers say they would rather learn of a company's troubles early, while there is time to require additional collateral and before the fund has to tap other members to bolster the security fund balance.

"Frankly, as a member of the executive committee of New Jersey Self Insurer's Guaranty fund, I have an obligation to the other self-insured companies in the state to watch closely because if someone goes belly up (other members could) be assessed" to maintain the fund's balance, said Larry Holt, a member of the executive board of the New Jersey Self Insurer's Guaranty Assn. and executive director of

the National Council of Self-Insurers in New Providence, N.J.

Shortages have occurred previously in self-insured workers comp funds.

California, for instance, had a \$54 million deficit in 2003, after several bankruptcies by companies that understated their workers comp exposure and, consequently, posted inadequate collateral, Mr. Pettegrew said.

Since then, California has tightened its rules for posting collateral and restructured its security fund. Companies with the highest ratings can participate in an alternative security program.

The amount companies pay to the fund is determined by their credit rating, but they do not have to post collateral with the state. Companies that do not have the credit rating to qualify for the alternative fund must post collateral that is at least 135% of their claims with California.

In November, the fund took over paying about \$19 million in claims for Hayward, Calif.-based Mervyn's L.L.C., which filed for bankruptcy reorganization in July and operates about 150 department stores.

The fund has more than \$200 million in assets and another \$100 million line of credit, so Mervyn's claims will not cause a strain, Mr. Pettegrew said. Given the tough economic times, though, other self-insured companies could default in the future, Mr. Pettegrew said.

He is considering hiring a claims professional to manage claims handled by the fund's contracted third-party administrators.

Mr. Pettegrew said his immediate concern is with about 30 alternative security fund participants whose credit ratings have fallen below B-/B3 credit ratings because of economic conditions.

They won't be eligible to participate in the alternative security fund beginning in April when the fund's new plan year begins. So Mr. Pettegrew has been calling them with an early warning that they may have to post collateral with the state.

But making such arrangements could prove difficult given the credit market, Mr. Pettegrew said.

NAIC: Revised collateral rules for non-U.S. reinsurers adopted

CONTINUED FROM PAGE 3

potential negative effect.

"This just isn't the right time to ask us to swap collateral for a new and untested strength-rating system," Scott Gilliam, assistant vp and government relations officer for the Ohio-based Cincinnati Insurance Cos., said in a letter to the regulators at the meeting.

David Snyder, assistant general counsel for the Washington-based American Insurance Assn., said the vote was "an imprudent action" that disadvantaged U.S. consumers and insurers by reducing their secu-

global insurance practices. Also, the United States got nothing in return for relaxing the rules on non-U.S. reinsurers, he said.

From a primary insurer's perspective, "the imperfect part of the plan is that at times when a reinsurer's finances are deteriorating, it may not be possible for the reinsurer to collateralize its obligations to the ceding insurer," Bill Boyd, financial regulation manager for the Indianapolis-based National Assn. of Mutual Insurance Cos., said in an e-mail.

Supporters disagreed, however, and said it is important to modernize U.S. regulation to keep pace with

Pensions: Congress passes funding relief

CONTINUED FROM PAGE 1

en funding rules that legislators tightened in a 2006 law and are being phased in currently.

The most significant change in the legislation eliminates a provision set in the 2006 law that requires employers to dramatically accelerate plan contributions if they miss certain funding targets.

Under the 2006 law, employers must put enough money in their plans each year so the plans will be fully funded after seven years. That 100% funding target is being phased in so in 2008, plans have to fund toward a 92% target, while the target is 94% in 2009, 96% in 2010 and 100% in 2011.

If the target is missed in any year, employers then are required to fund toward the 100% target. The relief legislation, known as the Worker, Retiree and Employer Recovery Act of 2008, approved by Congress last week removes that requirement so that even if the funding target was missed for a year, the funding target for the next year would not bump up to 100%. For example, if an employer missed the 92% funding target in 2008, its funding target for 2009 still would be 94%, not 100%.

More action needed

Benefit groups welcome the relief, but say it is only a first step.

"We applaud Congress for acting quickly and hearing our urgent plea for relief. But much more needs to be done next year," said Kathryn Ricard, vp-retirement policy at the ERISA Industry Committee in Washington.

"Additional relief is very important," said Jan Jacobson, senior

FUNDING REPRIEVE

What the Worker, Retiree and Employer Recovery Act of 2008 would do:

- Removes transitional provision in 2006 law that requires employers to start to fully fund their plans if they miss set funding target percentages.
- Allows employers whose plans are less than 60% funded to value plans' funded status as of Jan. 1, 2008.
- Suspends for 2009 requirements that retirees age 70 1/2 and older take a minimum distribution from their defined contribution plans.

counsel-retirement policy for the American Benefits Council in Washington.

Even with passage of the legislation, current market conditions would require employers to contribute \$120 billion to their plans in 2009, up from \$50 billion this year, according to projections made by Watson Wyatt Worldwide.

Without the legislation, the contribution tab next year would be \$138 billion, Watson Wyatt estimated.

"This is very modest relief," said Mark Warshawsky, Watson Wyatt's director of retirement research in Arlington, Va.

For example, the measure, which President George W. Bush has not indicated whether he will sign, does not include a relief provision sought by business groups. That provision

relates to so-called plan asset smoothing, a type of averaging. Under a provision in the 2006 law, which last week's legislation clarified, asset values generally are averaged over a 24-month period.

However, the so-called smoothed value must be within 10% of current market value.

For example, if the smoothed value of plan assets was \$100 million and the current market value of the assets were \$50 million, plan assets would have to be valued no higher than \$55 million.

Corridor expansion

Given how much the value of plan assets has fallen, employers say either the temporary removal or lifting of the so-called 10% corridor is crucial to easing employers' funding burden next year.

Expansion of the corridor "will be a top issue for us next year," said Ms. Ricard of the ERISA Industry Committee.

The legislation also provides some relief for plan participants. For example, the measure allows employers whose plans now are less than 60% funded to go back to Jan. 1, 2008—before the equities markets plunged—to determine the plans' funding levels.

In many cases, that will avoid triggering a provision in the 2006 law under which plans that are less than 60% funded must be frozen with participants not accruing new benefits.

Additionally, the legislation suspends for 2009 a requirement in which retirees age 70 1/2 and older must take a minimum distribution from their defined contribution plans accounts to avoid a 50% penalty tax.

Innovation: Court rules for policyholder

CONTINUED FROM PAGE 4

to say even if a design is state of the art, the exclusion will apply should the machine prove faulty. Even then, he said, such changes may not always protect insurers.

Mr. Chouc said insurers will have to decide whether to refine exclusion provisions or adapt the

premium to the magnitude of the risk the court said insurers must assume.

"We're mindful of the fact this will lead to changes in the insurance world, but at the same time, to be honest with you, when we negotiated this policy way back when, we paid a fairly hefty premium to insure against that risk," Mr. Chouc

said. "We paid to protect against that risk and we were of the view the risk had been transferred to insurers and they had to pay for the loss once it materialized."

Canadian National Railway Co. vs. Royal and Sun Alliance Insurance Co. of Canada; Supreme Court of Canada; 2008 SCC 66; Nov. 21, 2008.

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potential negative effect.

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Supporters disagreed, however, and said it is important to modernize U.S. regulation to keep pace with

global insurance practices. Also, the United States got nothing in return for relaxing the rules on non-U.S. reinsurers, he said.

David Matcham, chief executive of the London-based International Underwriting Assn., said he was encouraged by the NAIC's vote. Non-U.S. reinsurers currently have more than \$50 billion posted for U.S. liabilities, which he said is an inefficient use of capital.

Also supporting the measure were Lloyd's of London, the Washington-based Reinsurance Assn. of America and the New York-based Risk & Insurance Management Society Inc.

"RIMS is hopeful that this modified regulatory framework, when fully implemented, will result in addi-

tional capacity and the equitable and efficient regulation of the reinsurance industry in a manner that meets the needs of commercial policyholders," it said in a statement.

In light of the NAIC's action, New York plans to withdraw its proposal to reduce collateral requirements and Florida plans to adopt the NAIC proposal, regulators from those states said at the meeting.

In other business, the NAIC:

- Elected Florida Insurance Commissioner Kevin McCarty as NAIC secretary/treasurer. Roger Sevigny of New Hampshire moved up to president and Jane Cline of West Vir-

ginia became president-elect.

- Indicated a willingness to grant an American Council of Life Insurers' request for reserve and capital relief during the turbulent economy. NAIC officers described regulators' responsiveness as "practical" during "unprecedented times," adding that no U.S.-based life insurer is in danger of insolvency. A decision is expected by year-end.

- Adopted a 2009 budget that anticipates a 7.1% increase in revenue and a 6.3% increase in spending. Revenue is projected at \$73.1 million and spending is projected at \$70.7 million.

Lexington: Ironshore picks up big names from AIG unit

CONTINUED FROM PAGE 1

Since its first federal bailout deal in September, AIG has implemented a retention award program for 168 key executives, believed by observers to include Mr. Kelley. Those payments, due in two installments over 12 months, apparently were not enough to keep him at Lexington, though, noted one wholesale brokerage executive who requested anonymity.

"The problem here is, there's nothing to keep them at AIG other than their salaries," the executive said, citing the drop in AIG's stock. "They can go somewhere else and make as much."

Mr. Kelley could not be reached for comment.

AIG last week named Peter Eastwood as Lexington's new president and CEO. Mr. Eastwood has held several management posts at AIG since 1991, most recently as executive vp in charge of Lexington's healthcare insurance operations.

In a statement, an AIG spokesman said, "We are grateful to Kevin for his contributions and are sorry to see him leave. That said, Lexington is greater than any one person. It is an enduring franchise with over 1,400 highly dedicated employees...We expect the organization to continue to be successful and to thrive under Peter's leadership."

Meanwhile, the moves are widely seen as a coup for Ironshore, a specialty property/casualty insurer

formed in 2006 with more than \$1 billion in capital from private equity investors.

"It's very significant," said Mark Murray, an analyst at A.M. Best Co. Inc. in Oldwick, N.J. "Any time you can get a 30-year veteran out of a company like AIG, and certainly someone who has run a unit like Lexington, it can't be overstated."

Robert Deutsch, Ironshore's president, said the two executives will strengthen the company's U.S. casualty operations, which include units handling management and professional liability and healthcare liability business.

Casualty "is an area where Kevin and Shaun really excel," Mr. Deutsch said. "They will be able to drive that faster than we would be able to without them."

Ironshore building staff

Mr. Kelley and Mr. Kelly will be based in Ironshore's Boston office, which now consists of four employees but will expand significantly, Mr. Deutsch said.

Asked whether he expects to hire more employees from Lexington, he said, "We will certainly be hiring additional people, but where they will come from is pure speculation...It's not like we're targeting anybody."

The departures are the latest in a string of executive defections from various AIG units, including Lexington, that began after AIG reached an agreement on a bailout by the Federal Reserve in September

and outlined plans to sell most of its operations except for its core U.S. property/casualty and foreign general units.

Several surplus lines executives say they understand that Mr. Kelley explored the possibility of buying out Lexington with an investor group.

An AIG spokesman denied that the company considered spinning off its surplus lines unit, though, noting that AIG CEO Edward M. Liddy has identified Lexington as one of the core operations that the insurer plans to keep.

The impact of the two executives' departure on Lexington's ongoing business remains to be seen, though the insurer is expected to remain a major force in the surplus lines market.

"In one sense, this is familiar territory for AIG, in that they have a history of developing strong managers who are, from time to time, recruited as senior managers at other companies," observed Bruce Balentine, vp and senior credit officer at Moody's Investors Service in New York. "On the other hand, this is an especially challenging time for AIG and several other financial services firms."

"It's a huge blow to them," said the wholesaler who requested anonymity. "Will Lexington survive? Of course they will."

"The big question," he added, "is how many people are both of them going to take with them?"

Facing financial pressures and a

battered stock price, AIG has made an effort to hold onto key executives with a retention payment program, which Mr. Liddy defended earlier this month against criticism from Rep. Elijah E. Cummings, D-Md.

Responding to a letter from Rep. Cummings questioning the payments, Mr. Liddy said they were necessary to retain executives on whom AIG's credit rating may partially depend. Mr. Liddy cited a Standard & Poor's Corp. announcement that if losses of business and personnel at AIG are "significant and threaten future business prospects," S&P could lower the insurer's credit ratings in 2009.

Mr. Liddy also noted that some AIG reinsurers have begun asking for provisions in their treaties that would allow them to cancel coverage upon the departure of critical AIG employees. A spokesman declined to comment on whether Lexington reinsurers are among this group.

In his Dec. 5 letter, Mr. Liddy reported that 168 AIG officers with base salaries ranging from \$160,000 to \$1 million have been offered retention awards ranging from \$92,500 to \$4 million.

Thirteen executive officers who will receive retention awards have agreed to defer the first installment from the end of this year to April 2009, he said, while 40 participants in the retention pool will not get salary increases through 2009.

Zurich: SEC settlement announced

CONTINUED FROM PAGE 3

entering into two additional reinsurance agreements for which risk transfer was negated by undisclosed side agreements, the SEC alleged.

"This was a scheme by former executives of Zurich Re, and later Converium, to manipulate their performance results through sham transactions and improper accounting," Linda Chatman Thomsen, director of the SEC's Division of Enforcement, said in a statement. "It had the effect of artificially boosting Converium's market standing and IPO offering price, causing significant harm to the investing public."

Neither Zurich nor SCOR admitted any wrongdoing.

"Zurich concluded that it was in the best interests of the company to resolve this matter with the SEC

'This was a scheme by former executives of Zurich Re, and later Converium, to manipulate their performance results through sham transactions and improper accounting.'

Linda Chatman Thomsen, U.S. Securities and Exchange Commission

XL: Move ignites buzz over possible operations sell-off

CONTINUED FROM PAGE 1

losses on securities sales—to be largely in line with the \$1.12 billion reported for 2008's third quarter.

The company also said in its statement that it expects to report approximately \$200 million to \$220 million in net investment fund affiliate losses from its alternative investment portfolio for 2008's fourth quarter.

XL reported a \$1.13 billion loss for the nine months ended Sept. 30, compared with a \$1.49 billion profit for the comparable period a year ago. Results reflect a \$1.4 billion charge related to a commutation agreement with financial guaranty insurer Syncora Holdings Ltd. and certain of its subsidiaries.

Change of plans

Paul Newsome, a managing director with Sandler O'Neill & Partners L.P. in Chicago, referred to a statement made by XL chief executive officer Michael S. McGavick in October that XL expects a "strategic review" of the company's life operations to conclude during the fourth quarter.

"The difference between what we learned...and what we knew previously is that they're willing to sell the rest of the company," he said.

Mark Lane, a principal and research analyst with William Blair & Co. in Chicago, said: "Given their investment losses and some of their

problems over the last few quarters, it has become obvious that they either needed to raise additional capital or sell the company, because they need to keep their ratings at an A level in order to compete in the reinsurance business and the long-term liability casualty business, and they are losing business because of concerns about capital."

But a sale could be challenging, said Mr. Lane.

"This is absolutely the worst time to be selling an asset," he said.

"A lot of traditional buyers lack financial flexibility themselves, and no one wants to take on additional asset risk, balance sheet risk," said Mr. Lane.

"But at least at this point I think it is a good franchise that will have some value. It's just that asset prices are so ambiguous in this market" it is difficult to evaluate them, Mr. Lane said.

Some observers believe the market turmoil means the company may be more readily sold in pieces. John L. Ward, chief executive officer of Cincinnati-based Cincinnati Partners L.L.C., said, market conditions "will add complexity to finding a solution in the short term, but given the magnitude of the issues

they're dealing with, and the problems in the market, that may be the only option they have."

Mr. Lane said one possible scenario would be for XL to sell its reinsurance business for cash and put that capital into its insurance business, which would stabilize its A rating. "They could keep that business, but there's execution risk," he said. "They need to do it fast," because clients are leaving due to their concerns about XL's capital, he said.

Susan Spivak Bernstein, a senior analyst with Wachovia Capital Markets L.L.C. in New York, said she is skeptical there would be a buyer for the entire company. It would be difficult for someone to buy the company right now because of the illiquidity of XL's investment portfolio, she said.

Furthermore, market conditions are not right for an acquisition. "You're looking at a market right now that has a finite amount of capacity" and is facing higher demand. "Many companies have gotten hit on the asset side of the balance sheet, and have a lot less capacity to write more" business, said Ms. Bernstein.

She said she believes most potential buyers now would be more

interested in new business and organic growth, "vs. integrating an acquisition of that size. It's a surprising announcement, in that it's something I might have thought six months ago would have made more sense," said Ms. Bernstein.

Observers say another complicating factor for XL may be the sale of units of American International Group Inc. The availability of AIG's Transatlantic Holdings Inc. reinsurance unit in particular "doesn't help," said Mr. Lane.

Meanwhile, Jeffrey Berg, an analyst with New York-based Moody's Investors Service, said, "We have concerns about exposure to potential further losses on their investment portfolio." Moody's put XL's operating units' insurance financial strength ratings under review for possible downgrade in October.

Also of concern are "the implications of possible operating weakness on its franchise and its balance sheet stress," Mr. Berg said.

Mr. Berg said Moody's is actively monitoring XL's prospective profitability and its ability to cover its debt obligations. "Those are the key drivers," he said.

Since October, "The investment markets have only performed worse, and given their investment leverage profile relative to other property and casualty names," it appears market deterioration could have an outsized impact on XL, Mr. Berg said.



XL Chief Executive Officer Michael S. McGavick expects a company review to conclude soon.

News In Brief

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proposal that could increase taxes on certain reinsurance transactions. According to a description of the proposal released by the committee, the change would affect only related-party reinsurance in which an offshore parent company reinsures a policy written by its U.S. subsidiary. The statement said the proposal is designed to "address the concerns that current law does not adequately level the playing field between domestic and foreign related-party reinsurance." The committee noted that the draft contains similarities to a bill introduced by Rep. Richard Neal, D-Mass., in September. The Neal bill—H.R. 6969—would "amend the Internal Revenue Code of 1986 to disallow the deduction for excess nontaxed reinsurance premiums with respect to United States risks paid to affiliates," according to the bill's text.

Carvill to exit treaty market

R.K. Carvill & Co. Ltd. will discontinue its treaty reinsurance business in 2009, citing its inability to keep up with industry changes and spiraling costs as being among factors that forced the move. The London-based reinsurance broker will neither place nor renew any treaty business after April 1, 2009. A spokeswoman for Carvill said the company would not comment on its decision to exit the treaty market, but confirmed details of a letter written by Carvill Chairman Rory Carvill that outlined the change to clients.

Comp costs, loss ratios increase in California

Average workers compensation rates in California declined during the first nine months of 2008, but indemnity costs rose and loss ratios increased, the Workers' Compensation Insurance Rating Bureau of California reported. Policyholders paid an average of \$2.30 per \$100 of payroll for policies written during the period, the WCIRB said. That is 6% below the average rate charged during the second half of 2007. It also is 64% below the average rate charged in the second half of 2003, before system reforms reduced costs. The WCIRB projected an ultimate accident year loss ratio of 52% for the 2007 accident year. While still low in historical terms, it would be a 14% increase from 2006 and a 23% increase from 2005.

Gallagher to buy Treiber Group

Arthur J. Gallagher & Co. is acquiring Treiber Group L.L.C. in a purchase for which terms were not

disclosed. The Garden City, N.Y.-based retail brokerage specializes in construction, surety, health care, executive risk and workers compensation insurance coverages, Gallagher said in a statement. The deal also includes Treiber Agency Group L.L.C., a wholesale insurance brokerage that serves retail agency clients throughout the Northeast. Treiber Group was the 75th-largest broker of U.S. business with \$34 million in 2006 brokerage revenues, according to *Business Insurance's* 2007 rankings. The brokerage did not participate in the 2008 rankings.

NCCI: Medical share of comp losses up

Medical costs across the United States now account for nearly 60% of workers compensation losses, up from 40% during the early 1980s, NCCI Holdings Inc. determined in a recent analysis. Slightly more than half of the increased medical share of losses resulted from medical and wage inflation, NCCI said. The balance is related to differences in medical and indemnity utilization. While there are state-to-state differences in medical costs, similar patterns exist across all states, NCCI found.

Reinsurers settle North Korea claim

London market reinsurers have agreed to pay about 95% of a Korea National Insurance Corp. reinsurance claim and withdraw allegations of fraud and impropriety made against the company, ending a commercial court dispute that began in January 2007. KNIC, the state-owned insurance company of North Korea, sought to enforce in England a judgment made by the Pyongyang Court—the agreed jurisdiction of the policy—for more than €44 million (\$56.5 million). That lawsuit followed a decision by the London market reinsurers to contest the claim, which arose from a 2005 accident in which a helicopter crashed and destroyed a warehouse in Pyongyang. The reinsurers' primary defense was struck out by the High Court in August 2007 and the Court of Appeal also struck the claims in October 2007. The reinsurers, however, continued to state that they believed the claim and the original Pyongyang judgment to be fraudulent.

Chicago RIMS chapter donates to Spencer

The Spencer Educational Foundation Inc. has received a \$100,000 commitment from the Risk & Insurance Management Society Inc.'s Chicago chapter. The money will go toward the RIMS Chicago Chapter Scholarship, which will be awarded annually to students who are pursuing an undergraduate degree in risk management or insurance at colleges or universities in Illinois, Indiana, Iowa, Michigan and Wisconsin. This is the first time that the Chicago Chapter is offering this scholarship, and the first recipient will be announced in March 2009.

Toxic: Dems, DOL at odds over risk assessment plan

CONTINUED FROM PAGE 4

in Rockville, Md. and a member of New York-based RIMS' board with responsibility for governmental affairs.

"As risk manager, I would have preferred to see a little more vetting of the actual proposal," Mr. Fleming said. "Most risk managers were not even aware of the proposal."

Scientific evidence to establish how the proposed rule would affect future exposures also is lacking, Mr. Fleming said.

When the "scientific community" asked for an extended period to comment on the Labor Department proposal, it was denied, Mr. Fleming said.

One part of the proposal, however, could reduce employers' workers compensation and general liability exposures, Mr. Fleming added. But without sufficient scientific examination it is difficult to say for certain.

That portion of the proposal applies to an established OSHA assumption that a typical employee's working life, and thus their exposure to substances, spans 45 years. The Labor Department's proposal would adjust that time span by reflecting an average working life that varies by industry.

Permissible exposure limits would be set based on industry-by-industry evidence rather than maintaining a uniform exposure limit for all industries.

"We are not in a position to express an opinion whether that is a good thing or not," Mr. Fleming said. "We think that the scientific community needs to evaluate that issue to let us know if that is a reasonable standard."

In addition, the Labor Department also proposes that all relevant documents it receives on occupational exposure be posted electronically for public review.

The Labor Department closed its 30-day comment period on Sept. 29 after posting its proposal, RIN 1290-AA23, in the Aug. 29 Federal Register.

Democrats charged that the Labor Department developed the rule in secret and criticized the federal agency for not holding a public hearing.

"It's obvious to us that they are trying to push this to get it done before the end of the (Bush) administration," said a spokesman for the U.S. House of Representatives Committee on Education and Labor, which is chaired by Rep. George Miller, D-Calif.

Labor advocates say they agree. "The administration is rushing to lock in place requirements to make it more difficult for the next administration to protect workers from known health risks," Margaret Seminario, director of safety and health for the AFL-CIO in Washington, said during testimony before a congressional committee.

The Labor Department would not comment on a possible release date for its final rule or whether it will be completed before President Bush

leaves office. It maintains it is trying to develop a best practice for the risk assessments.

The U.S. Chamber's Mr. Freedman disputed the allegation that the rule was developed in secret and pointed to the public comment period.

Should the rule be adopted before President Bush leaves office, Democrats said they could cut off funding needed to implement it next year. They also could conduct a congressional review aimed at scuttling the rule or proceed with a regulatory repeal process under new Labor Department leadership after President-elect Barack Obama takes office.

Critics also maintained that the proposed rule would unnecessarily add years to an already lengthy time to develop safety standards that protect workers from substances such as asbestos, lead and vinyl chloride.

They said it would do so by requiring OSHA and MSHA to issue an "advanced notice of proposed rule-making."

'The administration is rushing to lock in place requirements to make it more difficult for the next administration to protect workers from known health risks.'

Margaret Seminario
AFL-CIO

The chamber argued that requiring the additional step would help standardize the process and allow interested parties to gain greater understanding of the information OSHA and MSHA would use to develop a health standard.

The Des Plaines, Ill.-based American Society of Safety Engineers supports mandating publication of ANRPMs because they encourage stakeholder input and greater review of scientific studies of exposure to substances before regulatory action is adopted.

ANRPM publication would provide another opportunity for the regulated community to object to a health standard if necessary, the ASSE said in a statement.

While some critics said the additional step would delay implementation of health standards, the system for adopting them already is dysfunctional and can take a decade or longer to do so, according to Dave Heidorn, manager of government affairs and policy for the ASSE.

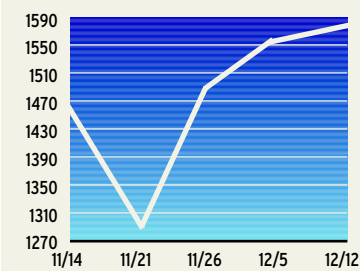
"When things are so broken, to take another step that would allow some transparency seems somewhat of a relative idea at this point," Mr. Heidorn said.

Stock Index

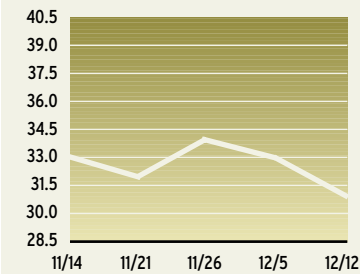
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Up-to-the-minute data for all 82 companies that comprise the BI Stock Index can be found at www.IndustryFocus.com.

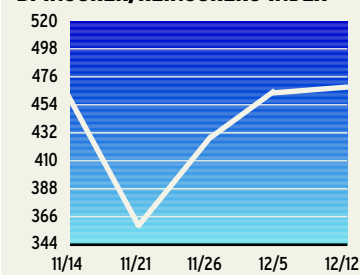
BI STOCK INDEX



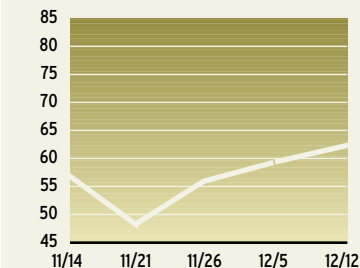
BI BROKERS INDEX



BI INSURER/REINSURERS INDEX



BI MANAGED CARE ORGANIZATIONS INDEX



Percentage change of BI Stock Index vs. key indicators

BI STOCK INDEX	1554.24	▲ 2.64%
DOW JONES	8629.68	▼ -0.07%
S&P 500	879.73	▲ 0.42%

LARGEST GAINS

AEGON N.V.	28.79%
ING Groep N.V.	22.35%
American Safety Ins.	18.47%
AXA	13.12%
SCOR S. A.	12.64%

LARGEST LOSSES

SCPIE Holdings Inc.	-62.13%
XL Capital Ltd.	-55.70%
Harleysville Group Inc.	-10.49%
Ambac Financial Group	-10.39%
UNUMProvident Corp.	-9.71%

Source: Financial Content Inc.
<http://financialcontent.com>

Now playing: '2008: A Claim Odyssey'

Although it's not likely to make the short list of Oscar contenders this year, a video spoofing the classic 1968 film "2001: A Space Odyssey" is getting attention within workers compensation circles.

Sacramento, Calif.-based attorney Matthew Brueckner created the short video using clips of the infamous rogue supercomputer HAL 9000 from Stanley Kubrick's sci-fi adventure. The workers comp defense attorney says he was poking fun at the gigantic computer system California's Division of Workers' Compensation is developing, called the Electronic Adjudication Management System.

When fully implemented, EAMS is supposed to better serve injured workers and employers by simplifying case management through the electronic filing of forms. But the project already has drawn criticism from workers comp system participants.



Matthew Brueckner and his computer nemesis are the subject of a short film about a workers comp claim filing system.

Mr. Brueckner's video shows the potential for frustration. He shot the video in the office of his solo practice and cast himself as "Dave," a lawyer attempting to file a declaration of readiness using EAMS.

He intercut close-ups of the increasingly agitated attorney with the clips from "2001" featuring the unblinking red eye and monotone voice of HAL, which blames a filing problem on human error.

Mr. Brueckner is funny, scrunching his face in frustration. But he admits he is not an actor so it's a case of artificial intelligence meets artificial acting.

Fortunately, he has a good day job as a Sacramento defense attorney with a healthy sense of humor and created the video to enclose in a client newsletter he says is meant to be informative and entertaining.

His video can be viewed at www.mblegal.net/eams_online_help_center.wmv.

Business Insurance END PAGE

Contributing: Jeff Casale, Roberto Cenicerros, Mark A. Hofmann, Dave Lenckus



Chris Martin, left, frontman for Brit rockers Coldplay, says he didn't borrow a melody from guitarist Joe Satriani for a recent hit song.

Guitarist picks fight with band Coldplay

Coldplay frontman Chris Martin supports reforming trade rules, but what about applying that idea to music?

Guitar virtuoso Joe Satriani filed a lawsuit in Los Angeles federal court claiming that the British power pop band ripped off his 2004 song "If I Could Fly" for their "Viva la Vida or Death and All His Friends."

Coldplay denies accusations in the suit filed earlier this month. "Joe Satriani is a great musician, but he did not write the song 'Viva la Vida,'" Coldplay said on its Web site. "We respectfully ask him to accept our assurances of this and wish him well with all future endeavors."

"Viva la Vida" has been nominated for a number of

Grammy Awards, so Mr. Satriani's claim comes at a time when it appears he's seeking recognition for the song's success.

"Everybody assumes I'm trying to go after these guys in Coldplay, as if I'm doing this with malice," Mr. Satriani told U.K.-based music Web site MusicRadar.com. "I'm just doing what I need to do as an artist, to protect what's mine, to protect those feelings I put down in song."

This is not the first time Coldplay has been accused of plagiarism. Last summer, New York-based band Creaky Boards claimed "Viva la Vida" ripped off their melody, "The Songs I Didn't Write."

Coldplay responded that "Viva la Vida" was, indeed, a song the Creaky Boards did not write.

Know whose pants are on fire? Keep it to yourself

Employers who learn of results of a lie detector test before terminating an employee better not accept, use or even refer to the results.

SunTrust Banks Inc. found that out when a panel of the 4th U.S. Circuit Court of Appeals overturned just enough of a lower court's ruling to reinstate an unlawful termination claim by an ex-employee once suspected in an attempted heist.

The incident occurred in August 2005, when Daniel Worden was an employee at SunTrust's branch in Anderson County, S.C. He phoned the bank and police and said gunmen were holding him hostage and demanding money from the bank, court records state. The incident ended hours later when the gunmen aborted their plan and abandoned Mr. Worden in nearby woods, he said.

But police doubted Mr. Worden's veracity and administered two polygraph examinations, both of which he failed. While SunTrust did not seek the polygraph results, it learned of them from police and Mr. Worden, court papers say.

The bank later fired Mr. Worden. Agreeing with a lower court, the 4th Circuit panel ruled in November that inadvertently learning the results did not violate the Employee Polygraph Protection Act's prohibition against employers actively accepting the results. The panel also agreed that SunTrust showed it would have fired Mr. Worden even if it did not know the results.

But the appeals panel ruled that SunTrust still may have violated the EPPA because of its use of and reference to the results—no matter how small a factor they were in the bank's decision. The panel remanded the case to the lower court.

Police never charged Mr. Worden in the case, said his Clemson, S.C., attorney, Mary C. McCormac.

University changes 'Undie Run' in bid to end streak of problems

Students at the University of California, Los Angeles, aren't afraid to grin and bare it during exam week.

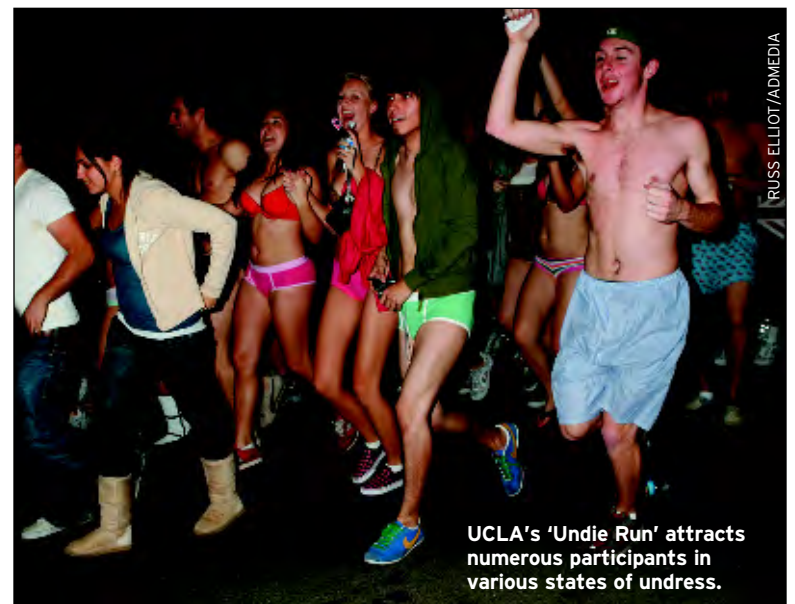
In fact, one of their hallowed traditions is an event called the "Undie Run," in which thong-clad students run around campus on the Wednesday of every finals week. The event has become so popular throughout the years that it draws participants who aren't students, and the sheer mass of runners ends up costing the school tens of thousands of dollars in

repairs and extra staffing. And, of course, the event, like any other event involving a large number of college students, tends to involve the consumption of considerable amounts of alcohol, which leads to injury among those running while impaired.

So a few days ago, in the spirit of anticipatory risk management, university officials changed the route of last week's Undie Run. The previous course was unsafe, according to the administration. According to an article in the Daily

Bruin, UCLA's student newspaper, students will be directed to Intramural Field as their destination. A student involved in negotiating the new course said the IM field was chosen "because it's a large, contained, well-lit space."

Administrators made clear that they're expecting students to behave well or they might ban future Undie Runs. One can but hope that a new route and better behaved runners will provide this story with a happy end—or thousands of them.



UCLA's 'Undie Run' attracts numerous participants in various states of undress.



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