

NEWS FROM THE INDUSTRY – DECEMBER 2007

FROM THE WORLD OF GENERAL INSURANCE

Asbestos and pollution developments

Federal-Mogul Corp., the automobile parts maker and asbestos defendant, is attempting to finalise its Chapter 11 bankruptcy reorganisation plan in US before the end of 2007, when the favourable terms it has negotiated for financing its exit strategy will expire, but has met a number of obstacles. Two of its liability insurers, Travelers Indemnity Co. and Employers Insurance Co. of Wausau, have objected to one of the two versions of the plan because they say it does not comply with bankruptcy rules and it impairs their policy rights. In addition, Hartford Financial Services Group, one of the insurers of PepsiAmericas Inc., which was previously the owner of one of the subsidiaries of Federal-Mogul, has refused to join its co-insurers in a settlement with PepsiAmericas – this could overturn the plan.

In mid-October, the House of Lords ruled that claimants in England and Wales with pleural plaques, but no visible symptoms, should not be compensated under tort law, as “proof of damage is essential in a claim in negligence”. This reverses the practice of the last 20 years during which employers and their insurers have compensated such workers with payments of up to £12,000. Based on the findings of the actuarial profession’s 2004 Working Party on UK Asbestos, the House of Lords ruling is estimated to save insurers between £200m and £1.4bn. Employers’ liability insurers welcomed the decision, but there remains some concern that common law claims may be pursued instead of claims in tort. Some lawyers, however, believe that the costs involved and the uncertainty of the outcome of such a move may prove too great a barrier and that amending legislation may be more likely.

At the end of September, the Rhode Island Attorney General filed a “public nuisance” lead paint abatement plan against 3 paint manufacturers, Sherwin-Williams Co., NL Industries Inc. and Millenium Holdings. Under this plan, the manufacturers would be liable for the cost of lead testing and abatement in nearly quarter of a million homes, schools and child care centres in the state. The estimated cost has been put at US\$2.4bn. The defendants, who claimed that blood-lead levels in the state’s children are declining and that the problem relates only to small areas of poorly maintained housing, were given until 15 November to respond to the plan. Public nuisance suits have failed in all the other states where they have been put forward.

A lawsuit brought by the California Attorney General seeking millions of dollars from automobile manufacturers for damaging the Californian environment with carbon dioxide emissions, was rejected by a federal judge on the grounds that it was impossible to determine the percentage of blame to be attributed to individual companies.

Terrorism

In mid-October, a committee of the the US Senate passed a revised version of the Terrorism Risk Insurance Revision and Extension Act, the principal revisions being a reduction in the period covered from 15 to 7 years, the removal of coverage for nuclear, chemical, biological and radiological risks and the addition of coverage for domestic terrorism attacks. The US Treasury indicated that President Bush is likely to support the revised version, which makes its passage through the full Senate more likely. It remains likely that the final steps for this legislation will be delayed until the last few days before the expiry of the current Act on 31 December.

The latest news from Germany is that the Government is likely to support an extension of the life of EXTREMUS AG., its terrorism backstop insurer, for one more year after the current provisions expire at the end of 2007. After that, it is rumoured that the extent of the Government guarantee would progressively reduce from its current €8bn by €2bn pa.

Contingent Commissions and Market Rigging

A court case against 7 firms of brokers and 17 insurers under the Racketeering Influence and Corrupt Organisation Act has been dismissed by a US district court judge in New Jersey. The case arose out of the investigations by the former New York Attorney General, Eliot Spitzer, into the way in which sales and pricing of commercial of US commercial insurances were carried out, and was brought by a number of insurance buyers who had opted not to participate in the settlements which Mr Spitzer had organised. The judge contended, however, that the plaintiffs had not produced evidence to prove that they were misled into thinking they were receiving the most economical and appropriate insurance product or that the defendants had engaged in a conspiracy to suppress and eliminate competition. The judge also refused the plaintiffs' case for leave to amend their submission, as this was already their fourth attempt.

The Connecticut Attorney General has brought a "market rigging" case against reinsurance broker Guy Carpenter and Excess Reinsurance Company (now in run-off) contending that they conspired with numerous other (unnamed) reinsurers to fix prices, shut out competitors, manipulate the markets and thus increase profits. The defendants have angrily denied the charges, which they intend to defend vigorously.

Shareholders of American International Group (AIG) have filed an action in Delaware against a number of parties including Mash & McLennan, ACE and PricewaterhouseCoopers, holding them responsible for the 2006 US\$1.64bn regulatory settlement by AIG, arising out of the earlier Eliot Spitzer investigations.

Solvency II

The Comité Européen des Assurances (CEA) has claimed that more needs to be done to ensure consistency of application of the new Solvency II rules, particularly consistency between the different member states in their interpretation of the rules. Otherwise, there is a risk that insurance businesses will move to the forum of weakest application. In other respects CEA, which represents European insurers, expressed strong support of the regime which is due to be introduced in 2012.

Lloyd's

The UK Court of Appeal has dismissed an appeal by disgruntled Lloyd's names who did not accept the Reconstruction and Renewal plan in the mid-1990's, and refused to pay the premiums demanded of them by Lloyd's to reinsure their Lloyd's liabilities into Equitas. Instead, they counter-sued Lloyd's for misrepresentation, which, they claim, induced them to become, or remain as, names. When this case failed some years ago, the plaintiffs successfully applied to amend their case to one of misfeasance in public office. The case was dismissed at first instance, and the appeal has now also been dismissed, apparently leaving the plaintiffs with no further options available to them.

US Tax Proposal

At the end of September, a number of US insurers (led by WR Berkley) called on the US Government to amend the tax rules to prevent foreign-based insurers from gaining a tax advantage by reinsuring US-based risks from their US subsidiaries into an affiliated company in a low tax environment, such as Bermuda. They claimed that this gave such foreign companies an unfair competitive advantage over their US counterparts. A number of major European insurers have countered that the US system should be made more competitive rather than penalising the efficient use of capital, which they see as the prime reason for carrying out such inter-group reinsurances.

UK Bodily Injury Awards Study

This study, jointly commissioned by the Association of British Insurers (ABI) and the International Underwriting Association, with the actuarial analysis provided by EMB, has shown that the rate of inflation applying to motor bodily injury claims is substantially greater than the level of inflation in the economy in

general, and the margin becomes greater the more serious the claim. Thus, while overall motor bodily injury claims have increased by 6.5% pa over the last 10 years, those for £100,000 have increased by 11% pa and those over £5m by a staggering 30% pa. This is in addition to a significant increase in claims frequency for bodily injury claims in spite of the fact that fewer people are getting injured in motor accidents. There are a number of contributory factors giving rise to the high level of inflation on these claims, including the recovery of National Health Service costs, the high level of medical expense inflation, the increase in the life expectancy of seriously injured claimants, and the need for more carers because of the European Working Time Directive. The impact of these continuing trends, whilst serious for insurers, is even more dramatic for their excess of loss reinsurers.

UK Flood Defences

In the pre-Budget report by the Chancellor of the Exchequer, the Government promised £800m to improve UK flood defences, spread over 3 years. The ABI claimed that this was less than had been requested even before the floods during the summer, and was completely inadequate to address the problem.

Independent Insurance

On 23 October, the court reached its verdict on the three ex-executives of the failed Independent Insurance Company - Michael Bright (chief executive), Dennis Lomas (finance director) and Philip Condon (deputy managing director). All three were found guilty of charges involving conspiracy to defraud and/or concealing facts from fellow directors, advisers, reinsurers and policyholders. They were subsequently sentenced to jail terms of 7 years, 4 years and 3 years respectively. All three were also banned from acting as company directors.

Large Losses

Loss updates and related issues include:-

Theft of Leonardo da Vinci painting, Scotland – August 2003 – the “Madonna of the Yarnwinder”, which was stolen from the Duke of Buccleuch’s Drumlanrig Castle was recovered from a solicitor’s office in Glasgow in October. The police were tipped off regarding its whereabouts, it is believed, as the thieves were trying to dispose of the painting. As a result of the recovery, it is understood that the £30m insurance claim has been refunded to underwriters. It is good to have some favourable news on losses to report!

Storms in New South Wales, Australia – 8-11 June – insured losses from this event, previously reported in these columns in the August edition, have now risen to A\$1.35bn, five times the initial estimate.

Severe tropical storm Lekima, Philippines and Vietnam – 29 September- 4 October – this first hit Luzon in the northern Philippines, where it brought heavy rains, landslides, flooding and damage to the infrastructure, resulting in at least 9 deaths. It then crossed the South China Sea to make landfall in central Vietnam where further flooding resulted in at least 55 deaths, the destruction of 6,000 homes and evacuation of many thousands more. Whilst no estimates are to hand, insured losses seem likely to be no more than a small percentage of the economic losses in view of the relatively poor nature of the areas affected.

Typhoon Krosa, Taiwan and China – 6/7 October – this category 4 typhoon, which produced winds of well over 100mph and over 3 feet of rainfall in places, devastated the fruit crops in north-eastern Taiwan, where it also claimed at least 5 lives. In China, 1.6 million people were evacuated from their homes and 75,000 fishing vessels recalled to port in Zhejiang and Fujian provinces south of Shanghai. Precipitation was even more severe here with a maximum of over 5 feet of rainfall recorded. In spite of severe flooding and some landslides, no fatalities have been reported. Early estimates of insured losses are of the order of US\$0.5bn, with economic losses of well over US\$1bn.

Earthquake in South Island, New Zealand – 16 October – whilst this measured 6.7 on the Richter scale, it struck a largely uninhabited region north-west of Queenstown. Losses are, therefore, unlikely to prove material.

Wildfires in southern California – 21 October – 6 November – these consisted of at least 23 separate fires, some of them believed to be due to arson, and destroyed at least 2000 homes and commercial properties, burnt over 500,000 acres and resulted in 7 deaths and the evacuation of about 0.5million people in the area between Santa Barbara and the Mexico border. They were spread through the tinder-dry region by unusually strong Santa Ana winds which reached 85 mph at times. Some of the affected properties were multi-million pound homes, including several in the Malibu area owned by film stars. Insured losses have been estimated to be as high as US\$1.6bn. It is thought that reinsurers are unlikely to be severely affected by the losses in view of the level of retentions now being held by the primary insurers, and the potential difficulty in proving that the fires constitute a single event.

Tropical storm Noel, Caribbean – 28 October – 2 November – this first hit the Dominican Republic with heavy and prolonged rainfall, causing major flooding and landslides. At least 79 lives were lost and over 60,000 people were displaced from their homes. It next hit Haiti with similar problems and a further 43 deaths. Cuba, the Bahamas and parts of the east coast of US were also hit by heavy rain, but by this time the storm was blowing itself out. In spite of the high death toll, insured losses are likely to be minimal, given the low insurance penetration in the areas principally affected.

Fire at oil refinery in Coryton, Essex – 31 October – the fire followed an explosion at the plant (recently purchased by the Swiss firm Petroplus Holdings) on the Thames estuary. Insurance coverage is understood to include €2bn of property and €15m of business interruption, mainly placed in the London market. No insured loss estimates are currently to hand, although it is thought that the main losses will fall on the business interruption coverage.

Current Issues Newsletter

Other recent developments are covered in the General Insurance Current Issues Newsletter. The latest edition, dated October 2007, which covers International, Claims and Legal Issues, Market News, Solvency II and Government and Regulatory Issues can be accessed via the profession's web-site on http://www.actuaries.org.uk/link/general_insurance/gen_ins-curr-issues.html.

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