34TH ANNUAL GIRO CONVENTION

CELTIC MANOR RESORT, NEWPORT, WALES

The Actuarial Profession
making financial sense of the future

Agenda

- What is a latent claim?

- Where actuaries are involved

- Valuation of loss

- Application to insurance coverage

- Summary

What is a latent claim?

ST3 Definition

"Claims resulting from perils or causes that the insurer is unaware of at the time of writing a policy, and for which the potential for claims to be made many years later has not been appreciated. The first claims from these sources may often not be apparent until many years after the period of cover."

What is a latent claim?

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Examples of latent claims

EXISTING   **POTENTIAL?**

- Asbestos

- Pollution

- PCBs

- DES

- Lead Paint

- Agent Orange

Where actuaries are involved

- Pricing

- Reserving

- Claims settlement

Valuation of latent claims

Key questions to be answered in valuation:

- Identification of underlying loss

- Valuation of underlying loss

- Insurability

- Application to insurance coverage

- Discounting

Identification of loss

- Definition of loss

- WHERE did loss occur?

- WHEN did loss occur?

- Link to product?

- Link to company?

Identification of loss – lead paint

- Approx 30m US homes contain lead paint and represent a health hazard (mostly poorly maintained homes with children)

- Bodily injury or public nuisance?

- 22 February 2006: 1st successful public nuisance ruling in Rhode Island - Appeal pending in RI Supreme Court
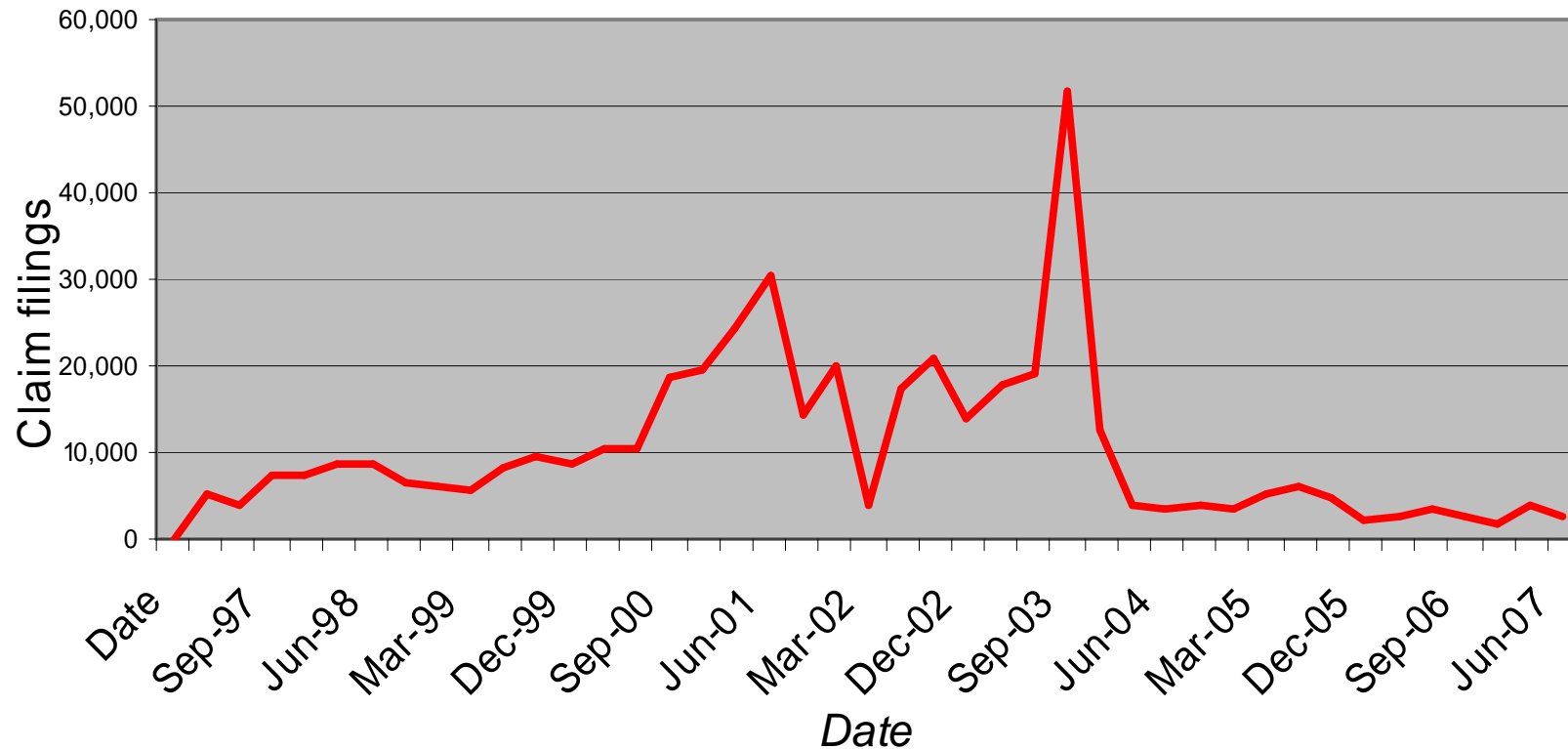
Valuation of loss

- How much will ultimately be paid?

- When will the company make payments?

Valuation of loss - asbestos

- Tort reforms in many US States

- Impact on malignant claims?

- Bankruptcy trusts

Valuation of loss - asbestos

Incremental number of new filings to the Manville Trust

Valuation of loss - asbestos

US Exposure	Lung Cancer	Meso	Other Cancer	Non Malig	Other	Total	% Malig
1995 & Prior	21,259	11,402	4,519	191,794	867	229,841	16%
1996	2,237	1,159	526	43,047	327	47,296	8%
1997	1,778	1,041	474	18,373	243	21,909	15%
1998	1,532	1,027	433	24,481	70	27,543	11%
1999	1,903	1,259	483	25,405	99	29,149	13%
2000	2,718	1,577	591	49,684	171	54,741	9%
2001	2,957	1,735	722	76,024	512	81,950	7%
2002	2,627	2,001	772	47,678	316	53,394	10%
2003	4,892	2,800	1,262	77,625	2,368	88,947	10%
2004	1,068	1,817	342	9,580	538	13,345	24%
2005	1,837	2,033	608	10,982	1,099	16,559	27%
2006	1,621	1,497	424	5,219	402	9,163	39%
Total	46,429	29,348	11,156	579,892	7,012	673,837	13%

Source: www.mantrust.org

Valuation of loss – lead paint

- Total clean-up costs for US homes estimated at **$500bn**

- Recently released state clean-up plan for Rhode Island estimates a cost of approx $2.4bn

- **Litigation will go on for several more years**

Determination of insurability

ST3 Definition – Liability insurance…

"…Provides indemnity where the insured, owing to some form of negligence, is legally liable to pay compensation to a third party. Note that an illegal act of negligence will often invalidate the cover."

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Application to insurance coverage

Definition of OCCURRENCE?

- Aggregation of asbestos claims?

- Aggregation of pollution sites?

- Aggregation of lead paint claims across US States?

Application to insurance coverage

Understanding of policy wording?

- Aggregates – particularly in Products cover?

- Multi-year limits

- Exclusions

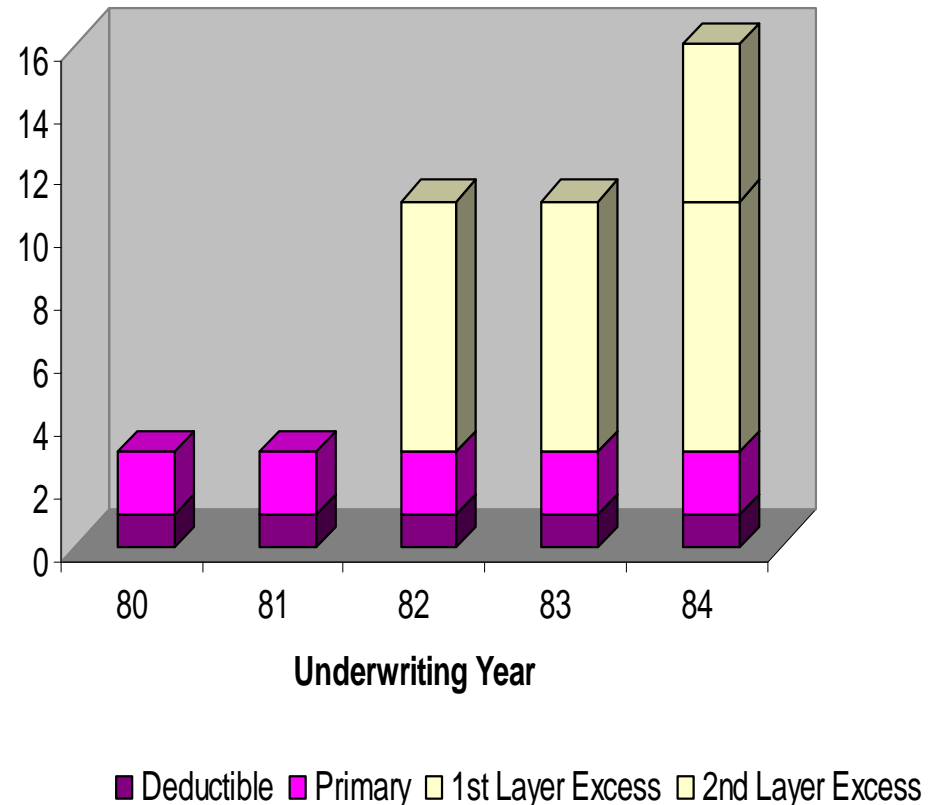# Application to insurance coverage

Allocation methodology?

- Pro Rata vs All Sums

- Contributions

- Uniform vs Date of First Exposure ("DoFE")

Allocation to insurance coverage

Pro rata allocation

- E.G. – ground-up costs of $15m spread over 5 years. Resulting in an allocation of $3m per year.

- Insured is liable for $5m

- Insurers must pay $10m

Policy Chart - Pro Rata

Underwriting Year

■ Deductible ■ Primary □ 1st Layer Excess □ 2nd Layer Excess

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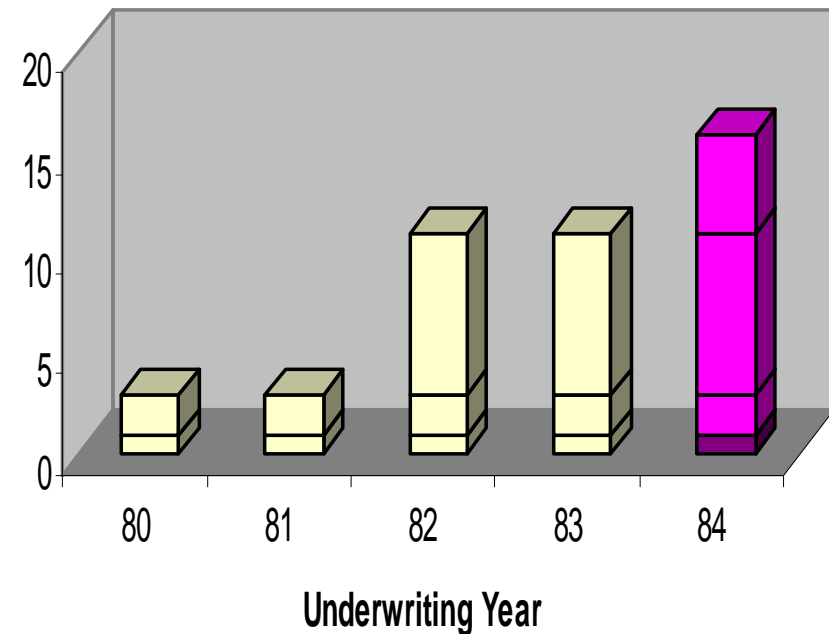making financial sense of the future

Allocation to insurance coverage

All sums allocation

- E.G. - costs of $15m being applied to the latest year, 1984.

- Insured is liable for $1m
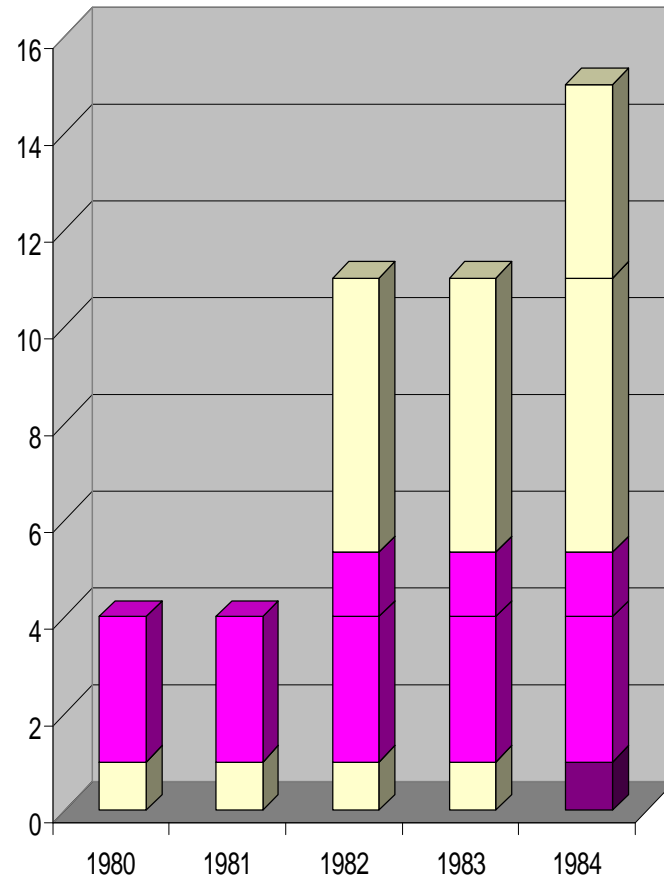
- Insurers must pay $14m

Policy Chart - All Sums

Underwriting Year

# Allocation to insurance coverage

All sums net of contributions

- Contribution rights estimated using rising bath-tub method.

- Policies eroded from the ground up, allowing for insolvencies and gaps in cover.

- Insured is liable for $1m

- Insurers must pay $14m

Allocation to insurance coverage

- State specific issue

- Even once applicable State Law has been decided, allocation methodology likely not to be clear cut
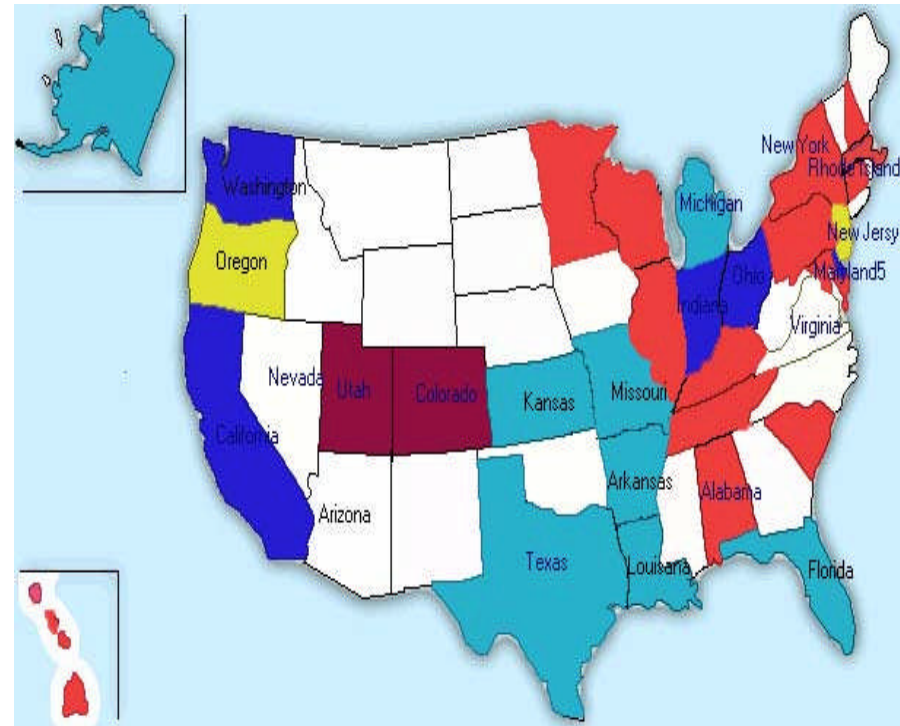
Summary

Current issues:

- Asbestos claim filings – Tort Reform etc

- FAIR Act

- Bankruptcy trusts

- Allocation – All Sums Net of Contributions

- Lead paint – insurability, quantum, aggregation

Closing remarks

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