MARKET NEWS, DATA AND INSIGHT ALL DAY, EVERY DAY

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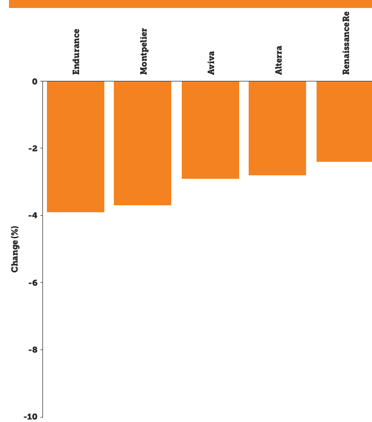

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NEWS

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Market news, data and insight all day, everyday
Insurance Day is the world's only daily newspaper for the international insurance and reinsurance and risk industries. Its primary focus is on the London market and what affects it, concentrating on the key areas of catastrophe, property and marine, aviation and transportation. It is available in print, PDF, mobile and online versions and is read by more than 10,000 people in more than 70 countries worldwide.

First published in 1995, *Insurance Day* has become the favourite publication for the London market, which relies on its mix of news, analysis and data to keep in touch with this fast-moving and vitally important sector. Its experienced and highly skilled insurance writers are well known and respected in the market and their insight is both compelling and valuable.

Insurance Day also produces a number of must-attend annual events to complement its daily output. The London and Bermuda summits are exclusive networking conferences for senior executives; meanwhile, the London Market Awards recognise and celebrate the very best in the industry. The new Insurance Technology Congress provides a unique focus on how IT is helping to transform the London market.

For more detail on Insurance Day and how to subscribe or attend its events, go to info.insuranceday.com

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Insurers develop business coalition to support more Florida cat risk transfer

Hurricane Andrew: Cecil Pearce expressed concerns about Florida's ability to borrow enough money to settle its debt if a storm of a similar size were to hit one of its major cities
AP Photo/Mark Foley, File

Greg Dobie
Managing editor

The insurance sector is building a "coalition" of the wider Florida business community to support its argument more catastrophe risk in the state should be transferred to the private sector rather than remaining within the Citizens Property Insurance Company (CPIC) and Florida Hurricane Catastrophe Fund programmes.

Influential stakeholders involved in the ongoing debate about the structure of hurricane risk in Florida told *Insurance Day* the two major business groups in the state – Associated Industries of Florida and the Florida Chamber of Commerce – are now supporting the insurance industry in its attempts to overcome political opposition.

Cecil Pearce, president of the Florida Insurance Council, said the state's business community has expressed concern because it is effectively funding close to 40% of the debt of the two programmes, which assess all commercial policies except for workers' compensation and medical malpractice.

They join organisations from a number of fields including environmental (Florida Wildlife Federation), taxpayer (Florida Tax Watch), free market (Heartland Institute and Americans for Prosperity), consumer (Florida Consumer Action Network) and not-for-profit (Florida League of Municipalities) in advocating a cut in the so-called "hurricane taxes" and downsizing the CPIC and cat fund programmes.

Speaking during a panel session on navigating the politics of hurricane risk in Florida at this month's *Insurance Day* Summit Bermuda, Don Brown, former chair of the Florida House of Representatives insurance committee said Florida's heavy reliance on debt as a strategy or mechanism to finance "the extraordinary natural catastrophe risk" the state experiences could come back to haunt it.

"I'm not aware of anyone who loans a lot of money and doesn't expect to have it paid back," he said. "I'm not sure in Florida we fully appreciate how difficult it will be to make our repayments [in the event of a major cat loss] while we use heavy debt to finance losses after the fact."

Meanwhile, senior vice-president and general counsel at RenaissanceRe, Stephen Weinstein, said more risk could be transferred to the private sector "assuming risk-adjusted pricing and adequate structures and in some instances a degree of time".

"There is an extremely elastic appetite for Atlantic hurricane risk, Florida's Pacific hurricane risk and indeed cat risk and insured risk in general," he continued.

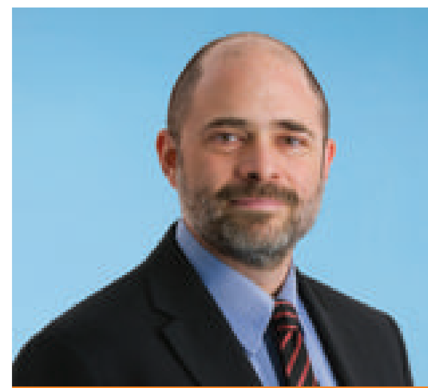
Pearce said the prospective reform of Citizens would be a major issue of discussion during the state's upcoming 2013 legislative session.

"We will spend this summer basically trying to pull the industry together to see if we have at least some kind of consensus on what we think the reform package day to day should look like," he explained.

"Then we need to sit down and speak to key legislators. When we talk about risk versus price we need to explain what the real cost of the cat fund and Citizens is.

"The message we have to get across is if a hurricane Andrew- or Katrina-type storm hits Miami or Tampa or Daytona, I am not convinced the state of Florida could borrow the money it would need to settle its debt, to be honest with you.

"Assuming we could borrow the money, it would have to be something like $15bn to $25bn. No state in the history of the US has ever borrowed more than about $10bn at a single time," he concluded.



"There is an extremely elastic appetite for Atlantic hurricane risk, Florida's Pacific hurricane risk and indeed cat risk and insured risk in general"

Stephen Weinstein
RenaissanceRe

"We will spend this summer basically trying to pull the industry together to see if we have at least some kind of consensus on what we think the reform package day to day should look like"

Cecil Pearce
Florida Insurance Council

EU responds to insurer pressure over Solvency II introduction

Herbert Fromme, Hamburg
German correspondent

The EU plans to lessen the impact of Solvency II significantly after massive pressure by insurers and also criticism from some regulators.

Brussels intends to exempt all existing life contracts for the first seven years from the new Solvency II capital rules under pillar one of the regime after the rules come into effect in 2014.

Solvency I will continue to apply to all these existing contracts. Companies will have to adhere to pillars two and three of Solvency II, however, covering risk management and reporting.

A spokesman for European Commission internal market commissioner, Michel Barnier, yesterday confirmed the plan. The commission's head of pensions and insurance, Karel van Hulle, added the proposal is on the table but said it was not an exemption, rather a phasing-in.

Should the EU go ahead with this modification, the reform will be much less threatening for insurers than previously anticipated.

Insurance shares reacted to the news with gains.

By setting a period of grace, the EU is reacting to insurers' warnings they would have enormous difficulties under the new regulatory rules. A quantitative impact study just completed internally by the German insurance industry and dubbed QIS6 showed close to 40% of life insurers would experience difficulties by not matching the required solvency capital and close to 10% would possibly not have the minimum capital required, which usually would result in the regulator stopping business immediately.

"The low interest rates are the real problem – under Solvency II they have very negative effects," one manager said.

Brussels' purpose in introducing Solvency II rules is to establish equal standards throughout the EU and stabilise insurance companies in the event of economic crises. Providers have to reserve a certain amount of equity capital in future to cover risks – insurers covering pharmaceutical companies will need more capital than rivals that only insure residential property. Insurers with capital investments in stocks and shares have to have more equity capital to cover the risks than for investments in governments bonds.

Michel Barnier yesterday confirmed the EU's plans for lessening the impact of Solvency II Jock Fistick/Bloomberg

However, as the rules are based on a mark-to-market principle, there are considerable mismatches between long-term contracts and guarantees given by life insurers and the shorter duration of their investments.

Brussels is fine-tuning the new regulatory rules with the so-called trilogue between the European parliament, the European Commission and the Council of Ministers. According to sources close to the negotiations, it was German Christian Democrat MP Burkhard Balz, who also reports for the European parliament on Solvency II, who suggested making an exception for existing contracts. German financial regulator, BaFin, had even called for a transition period of 10 years for existing contracts according to Brussels sources.

The commission has signalled its intention to approve Balz's proposal. "There is a good chance the plan will be approved, but nothing has been finalised to date," an insider said.

Grupo Catalana Occidente confirms Groupama Seguros acquisition details

Spanish insurer Grupo Catalana Occidente and its majority shareholder, Inocsa, are to acquire Groupama's Spanish business for €404.5m ($514.5m), *writes Fabien Buliard, Paris*.

The Spanish group and the French mutual insurer had been in exclusive talks since the end of last month.

Grupo Catalana will acquire 49% of Groupama Seguros, while Inocsa will buy the remaining 51%.

€404.5m
Amount Grupo Catalana Occidente and Inocsa, are paying for Groupama Seguros

Under the terms of the agreement, Grupo Catalana has an option to acquire Inocsa's stake after three years.

In a statement, Grupo Catalana said the deal will further consolidate its position as "a leading independent insurance group in the Spanish market for family and small and medium-sized enterprises".

With the integration of Groupama Seguros, which posted turnover of €940m last year, the Spanish group's top line will total close to €4.1bn, while raising its workforce to 6,800 staff.

The group added the acquisition will make it Spain's sixth-largest insurer by volume, based on 2011 figures, ranking second in multi-risk property insurance with a 10.8% market share and fifth in motor with a 6.5% market share.

Earlier this month, Groupama sold the property/casualty business of its Gan Eurocourtage brokerage unit to Allianz France (*Insuranceday.com*, Jun 8).

Since the beginning of the year, Groupama has also been trying to divest its UK units, as well as its private equity business.

Provinzial reverses buildings insurance trend with first-half growth

German public law insurer Provinzial Rheinland increased its new business in buildings insurance 22.3% during the first five months of 2012 – the first time in years it has achieved an increase, *writes Herbert Fromme, Hamburg*.

Provinzial had previously given up much of its business in this line owing to high losses.

In motor, the company – which is part of the savings banks group – lifted new business 16.1%.

In common with other public law organisations, Provinzial Rheinland is only active in one region, although this is one of the most populated in Germany. For a number of historic reasons, public law insurers are leaders in buildings insurance.

In the insurance of commercial real estate, Provinzial also managed to win new customers, after it left the line altogether some six years ago. "But we did not manage to record significantly higher premiums in 2011, as rates are under pressure," board member Sabine Krummenerl said.

"Motor insurance was our highlight in 2011," Ulrich Jansen, Provinzial Rheinland's chief executive, said. In earlier years, Provinzial regularly lost customers in the annual renewal season towards the end of the year. "At year-end 2010 and in 2011, we managed to increase the number of vehicles insured considerably," Jansen said. At year-end 2011, the company added 27,000 vehicles. If its internet affiliate S-Direkt is included, the increase was 44,000, he added.

However, both buildings insurance and motor still produce underwriting losses – in motor, the combined ratio deteriorated from 103.9% to 108.6%. The main reason was a hailstorm hitting the Moselle area in August 2011, leading to 18,000 claims and €76m ($96.7m) in losses so far. In addition, Provinzial suffered some very expensive personal injury claims. As there is little reinsurance in motor, this is hitting net results.

In buildings, the combined ratio was 103.9% compared with 101.6% in 2010, although board member Peter Slawik said this was still "much better than the market".

"Motor insurance was our highlight in 2011... At year-end 2010 and in 2011, we managed to increase the number of vehicles insured considerably"

Ulrich Jansen
Provinzial Rheinland

As market leader, the company is being attacked by rivals with special discount offers. "We don't go along with that, we stick to our rates," Slawik said.

This strategy is beginning to pay. As a consequence of their low-price strategies, many insurers have to increase premiums by hefty margins or cancel contracts. Provinzial could fill the gap.

Premium income in property/casualty was €967m in 2011, with the overall combined ratio worsening from 91.4% to 97.1%. In life, premiums were down 16.8% to €1.2bn. Provinzial had to write off close to €96m on Greek bonds and on real estate.

IIS NEWS

Brian Duperreault proposes independent microinsurance facility

Scott Vincent,
Rio de Janeiro
Deputy editor

A collaborative approach is needed to ensure the sustainable growth of microinsurance products, Brian Duperreault told International Insurance Society (IIS) seminar delegates, as he unveiled the proposed creation of an independently managed microinsurance facility.

Duperreault, a former chairman of the IIS and now chairman of Marsh & McLennan, said the proposal is for a full-scale operation jointly owned by carriers that could also serve as a research and development mechanism and act as a single point of influence for governments and regulatory bodies.

"We see Brazil as our first test market," he told delegates in Rio de Janeiro. "Brazil would make an ideal pilot environment, with the potential for 100 million policies and total premiums ranging from $1.7bn to upwards of $4bn."

"No single company has been able to crack the code of microinsurance. Developing a real market is necessary for any of us to develop microinsurance products that truly succeed. I don't believe a single or even a handful of companies can develop the market. But a collaborative approach is the potential solution to this complex problem"

Brian Duperreault
Marsh & McLennan

Duperreault said a collaborative approach is necessary, adding a sustainable business model for microinsurance has yet to develop in the insurance sector. "No single company has been able to crack the code of microinsurance. Developing a real market is necessary for any of us to develop microinsurance products that truly succeed. I don't believe a single or even a handful of companies can develop the market. But a collaborative approach is the potential solution to this complex problem."

Duperreault revealed Joan Lamm-Tennant, chief economist and strategist at Guy Carpenter, has been handed responsibility for leading the team that will put together the proposed facility. "We've engaged with global and local leaders and we are confident about the long-term viability and potential of this approach," he said.

"If all goes to plan, we expect to come back to you seeking your participation and commitment by the end of the year."

Young middle class is driving force of Brazil's future success, SulAmerica chairman says

Stimulating the new generation of clients who grew up after the years of hyper-inflation to buy wealth-protection products is the next phase in development of the Brazilian insurance market, chairman of domestic insurer SulAmerica, told the International Insurance Society seminar in Rio de Janeiro, *writes Scott Vincent, Rio de Janeiro*.

Patrick de Larragoiti Lucas told the event this emerging young middle class is the driving force of the market's future and he said the industry is hoping new regulations will be developed for wealth-protection products "very soon".

"We've had 30 million new Brazilians entering the middle class during the past eight years. These new consumers want to protect the health of their family members and their assets. We have to develop wealth-protection products so people have incomes when they retire," he said.

Lucas said the level of optimism in the Brazilian market is very high amid spectacular growth in insurance markets in the southern hemisphere. "In Brazil, the penetration level of insurance compared with GDP is 3.5%. Recent forecasts by CNSeg show this will increase to 4% by 2016. The Brazilian market will continue to enjoy an even more prominent position on the world stage."

He said Brazil's motor market is enjoying very favourable conditions, driven by economic buoyancy and increased car sales in the country. "Close to 94% of new car sales are insured for their first year of use," he said. "Many don't renew in subsequent years, so just one-third of the Brazilian motor fleet have coverage. We have to adapt our distribution channels so we can provide better protection to Brazilian drivers."

Another area of opportunity Lucas highlighted was microinsurance, following the passage of new microinsurance regulations in 2011. "According to World Bank estimates, the market for microinsurance in Brazil is estimated to be in the order of 128 million people who could benefit from property/casualty coverage.

"Some insurance companies have already run interesting pilot schemes and microinsurance is being sold in the favelas in Rio. Premiums range from Real2 [97¢] to Real50 per policy per month."

China looks to global best practice as it draws up fresh solvency rules

China's insurance regulator will welcome information exchange and information from other parts of the world as it embarks on creating the second version of its solvency requirements, delegates at the International Insurance Society annual seminar were told, *writes Scott Vincent, Rio de Janeiro*.

Yanli Zhou, vice-chairman of the China Insurance Regulatory Commission (Circ), said his country's new solvency requirement will reflect trends taking place internationally and the particular characteristics of the Chinese market.

Delivering his first speech outside of China, Zhou said the three pillars of "generation two" of China's solvency requirements will be quantitative, qualitative and transparency. "We expect it will be completed by 2016," he said.

Solvency regulation first appeared in Chinese insurance law in 1995 and further rules were formally introduced in 2003.

In 2004, Zhou said action was taken against three insurers – China Life, China Pacific and New Life Insurance Company – for failing to meet these requirements.

"In 2007, skyrocketing capital markets misled insurers to sell policies at irrationally low prices and 10 insurers could not meet solvency requirements. In 2008, 13 insurers were declared insolvent," he said.

Zhou said a market correction had since taken place and China's insurance market is now in a much healthier state.

Other regulatory developments taking place in China include the creation of a dispute-settlement department for each of the jurisdictions under Circ supervision, which is expected to be completed by the end of September.

"We think China's insurance market has very good prospects for the years to come because of the low penetration rates. We need to optimise our market structure by increasing the number of market players to encourage innovation"

Yanli Zhou
Circ

A new department was also established last year to supervise consumer protection, which Zhou said is one of the priorities of the Chinese regulator.

"We think China's insurance market has very good prospects for the years to come because of the low penetration rates," he said.

Zhou said China's insurance sector has a penetration rate of only 3.65% at present, compared with an average of 10.74% for other more developed markets in Asia such as Japan and South Korea.

"We need to optimise our market structure by increasing the number of market players to encourage innovation," he said.

Insurance-backed UNEP project 'will drive new technologies and energy sources'

Ludger Arnoldussen says industry has made 'landmark contribution' to sustainability

Scott Vincent, Rio de Janeiro
Deputy editor

Twenty-seven insurance companies from across the world, comprising close to 10% of the global insurance premium, were represented as initial signatories of the Principles for Sustainable Insurance (PSI) at the launch ceremony in Rio de Janeiro.

Launched as part of this year's International Insurance Society (IIS) annual seminar and timed to coincide with the Rio+20 conference on sustainable development, the principles are the work of more than five years of planning through joint initiatives between the UN Environment Programme's Finance Initiative (UNEP FI) and leading industry players.

The PSI comprise four key principles; first, to embed in decision-making environmental, social and governance issues related to the insurance business. Second, to work with clients to raise awareness of these issues and develop solutions accordingly. The third principle is to work together with governments, regulators and other key stakeholders to promote widespread action across society on environmental, social and governance issues. The final principle is to demonstrate accountability and transparency in regularly disclosing publicly progress in implementing the principles.

The seeds for the PSI were sown in 2007 when the UNEP FI's insurance working group produced its first report on the issue, with a global survey of 230 companies conducted in 2009. In 2010, Axa and Insurance Australia Group began co-chairing the working group,with the structure of the full principles proposed at the end of that year.

The working group is now chaired by Munich Re. Ludger Arnoldussen, member of the board of management at the German reinsurer, told delegates at the IIS seminar the PSI launch represented a "historic moment" for the industry, saying: "Some time ago we set out on a journey and today we have reached one of our historic milestones.

"Some time ago we set out on a journey and today we have reached one of our historic milestones. We have made a landmark contribution towards building a sustainable economy and advancing sustainable development"

Ludger Arnoldussen
Munich Re

"We have made a landmark contribution towards building a sustainable economy and advancing sustainable development." He said adoption of the principles will help pave the way for new technologies and alternative energy sources, as well as enhancing social inclusion.

"Several hundred senior representatives from the insurance industry, governments and regulators, business and industry associations, academia and scientific institutions, have given input to the draft principles. The last feedback loop was through the member companies of the Geneva Association." Following the launch, Munich Re will remain chair of the transitional board.

"Together with the 27 founding signatories and seven supporting institutions, we will help structure the next steps. As chair of the transitional board, we will carry the PSI beyond the launch to create a global framework which enables a consistent industry approach."

Arnoldussen said the initiative now has close to 10% of the worldwide insurance premium represented and he added: "I hope we will have many more signatories in the time to come."

In addition to Munich Re, the signatories, all of which were present at the launch, are as follows: Achmea (Netherlands), Aegon (Netherlands), Aviva (UK), Axa (France), La Banque Postale (France), Bradesco (Brazil), Delta Lloyd (Netherlands), Insurance Australia Group (Australia), ING (Netherlands), Interamerican Hellenic Insurance Group (Greece), Itaú Seguros (Brazil), Mapfre (Spain), Mitsui Sumitomo (Japan), Mongeral Aegon (Brazil), RSA (UK), Sanlam (South Africa), Santam (South Africa), Scor (France), Sompo Japan (Japan), Sovereign (New Zealand), Storebrand (Norway), SulAmerica (Brazil), Swiss Re (Switzerland), The Co-Operators Group (Canada), Tokio Marine (Japan) and Zwitserleven (Netherlands).

The seven supporting institutions are CNSeg (Brazil), the International Insurance Society, the United Association of the Caribbean (Barbados), the Insurance Council of Australia, the Insurance Council of New Zealand, the International Co-Operative and Mutual Insurance Federation (UK) and the South African Insurance Federation.

'Insurers cannot pursue sustainability in isolation,' Swiss Re says

Swiss Re's head of sustainability said the launch of the Principles for Sustainable Insurance by the UN Environment Programme Finance Initiative (UNEP FI) provides an opportunity to share ideas with a wider audience, *writes Scott Vincent, Rio de Janeiro*.

David Bresch told delegates at the International Insurance Society's annual seminar industry players have a role to play in increasing society's resilience but companies cannot do this in isolation.

He cited work that has been achieved on a macro scale through the creation of the Caribbean Catastrophe Risk Insurance Facility and on a micro scale through Swiss Re's work in sub-Saharan Africa, saying: "These were people stricken by drought to the extent they were caught in a poverty trap. Insurance could help but on its own it is not accessible. So we partnered with a non-governmental organisation – Oxfam – to build on an existing cash-for-work programme."

"These were people stricken by drought to the extent they were caught in a poverty trap. Insurance could help but on its own it is not accessible. So we partnered with a non-governmental organisation – Oxfam – to build on an existing cash-for-work programme. Some of the work these people do on the prevention side allows them to get cash they can then use to buy insurance"

David Bresch
Swiss Re

Bresch said once the risk of more frequent events has been reduced, insurance becomes more accessible. "Some of the work these people do on the prevention side allows them to get cash they can then use to buy insurance," he said.

Bresch said this helps build society's resilience and can also reduce the level of migration.

Mongeral Aegon claims Brazil pension first

Mongeral Aegon has unveiled plans to launch what it says will be the first product for Brazil's pension market, which incorporates sustainability concepts, *writes Scott Vincent, Rio de Janeiro*.

The Aegon subsidiary, which is one of the largest insurers in Brazil, said the product is the first to allow individuals to save and accumulate financial resources with a product that gives assurances it will "invest in the changes you want for the planet".

The Pevidencia Sustentavel plans will provide common benefits but the funds collected will take into account environmental, social and governance factors, the company said.

WORLD LOSS INTELLIGENCE/LIABILITY

Settlement: Prudential Life pays California $1.6m as part of Death Master File payout

$1.6m
Amount paid to California's general fund by Prudential Life in Death Master File settlement

CALIFORNIA: The state's general fund has been boosted by its share of the $17m multi-state settlement agreement paid by Prudential Life Insurance Company Group relating to the Death Master File (DMF) database.

The general fund's coffers have seen $1.6m poured in after Prudential Life became the first company to settle the multi-state insurance commissioner's investigations into the DMF.

The Social Security Administration's DMF is a database containing the names and identifying information of all those who have died within the US. As part of the settlement agreement, Prudential has agreed to check the list regularly to see whether any of its life insurance policyholders, owners of annuities or holders of retained asset accounts have died.

If one has, Prudential must conduct a thorough search for beneficiaries, using all the contact information it holds, as well as online search and locator tools. If beneficiaries cannot be located, the company must hand the proceeds owed to beneficiaries over to the states as required by unclaimed property laws.

The agreement required Prudential Life to pay $17m collectively to the states participating in the settlement. Benefits owed to beneficiaries will be paid once they have been located. Paid benefit amounts will be determined according to the terms of each individual policy.

Settlement: Facebook pays $10m

CALIFORNIA: Facebook has agreed to pay $
the social networking website of violating u
photographs and likenesses.

The lawsuit was filed by five Facebook use
tion about their preferences without paying t

According to US District judge Lucy Koh, t
cou
nam
cou
cla
one
am

$10m
Amount Facebook will pay to charity to settle lawsuit

Settlements: Refiners agree $21.6m payment to settle hot fuels

ConocoPhillips, ExxonMobil, Shell Oil Products US and BP subsidiaries BP Products North America and BP West Coast Products will each pay $5m

Citgo and Sinclair will each pay $800,000

US: Six oil refiners have agreed to pay $21.6m to settle a series of issues that have become known as the "hot fuel disputes".

It was alleged the companies knowingly overcharged for fuel by failing to adjust their prices to take into account changes in the fuel's volume caused by warmer summer temperatures.

Petroleum is sold by volume, but with temperatures rising, storage tanks warm up causing the fuel to expand and reducing the amount of energy provided per unit.

ConocoPhillips, ExxonMobil, Shell Oil Products US and two BP subsidiaries – BP Products North America and BP West Coast Products – will pay $5m apiece, while Citgo Petroleum Corp and Sinclair Oil Corp must pay $800,000 each.

The $21.6m will be shared out among the retailers and wholesalers in the 29 US states where the lawsuits were filed.

Settlement: Travelers pays California $9

CALIFORNIA: Travelers is repaying $9m to policyho
charged on their premiums as well as handing over $1.
series of violations the company made between January
July in the same year.

Specifically, the California Department of Insurance disc
76 non-rating errors and 19 termination transaction errors
existing policies and 424 policies that were cancelled, not re

Based on the results of this examination, the Californi
ance initiated an enforcement action against the Traveler

"I am pleased with the extraordinary co-operation th
ance received from Travelers in making the remedial cha
in refunding premiums where appropriate," said insuran
Jones (*pictured*).

"This settlement with Travelers is a victory for consu
once again the value provided by the California Departm
cost to the taxpayers."

IN TOMORROW'S WORL
LIVES & LIV

Y & SETTLEMENTS

m to charity to end lawsuit

10m to charity to settle a lawsuit that accused users' rights to control their own user names,

rs who accused the company of using informa- hem or allowing them to opt out.

he plaintiffs had shown how economic injury ld occur through Facebook's use of their mes, photographs and likenesses. Previous urt documents had shown how the proposed ss-action lawsuit could have included close to e in every three Americans, with the damages ounting to billions of dollars.

Settlement: AIG workers' comp payments continue

US: Missouri is using its share of AIG's $146.5m settlement for alleged under-reporting of workers' compensation premiums to bolster its public school fund.

As previously reported in *Insurance Day*, AIG is alleged to have under-reported close to $2.1bn of workers' compensation premiums – these payments are taxed at a higher rate than motor, liability and other types of insurance.

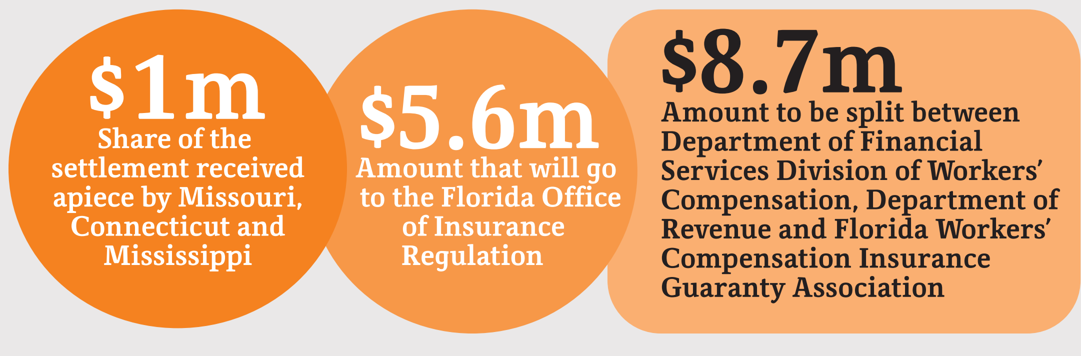
"This under-reporting of premium volume allowed AIG to pay less in taxes and gain a financial advantage over its competitors," John Huff, director of the Missouri Department of Insurance, said. "Missouri employers count on competitive workers' comp insurance markets and our laws provide consequences for companies that attempt to undermine competition."

Connecticut has been handed a $1m payment for its share of the $146.5m total, which will be placed in the state's general fund.

According to the settlement agreement, AIG has been under-reporting its workers' comp premium volume for more than quarter of a century.

Mississippi's coffers were also bolstered by $1m, while the Florida Office of Insurance Regulation will receive $5.6m of the fine and penalty, with an additional $8.7m split between the Department of Financial Services Division of Workers' Compensation, the Department of Revenue and the Florida Workers' Compensation Insurance Guaranty Association.

The states of Florida, Delaware, Indiana, Massachusetts, Minnesota, New York, Pennsylvania and Rhode Island led the examination of AIG's books that first discovered the irregularity.



Earthquake settlement: Reserve Bank questions role of Ecclesiastical in capping NZ claims

NEW ZEALAND: The Reserve Bank of New Zealand (RBNZ) has asked whether it was right for UK-based Ecclesiastical Insurance Office (EIO), part of the Ecclesiastical Group, to "shut the door" on providing further backing for claims resulting from the Canterbury earthquakes in 2010 and 2011.

This week, the High Court in Auckland approved an amended scheme under which ACS (NZ), formerly Ansvar, created a scheme of arrangement for the payment of claims should the operation go broke. Ansvar, an insurer of churches and heritage buildings in New Zealand, became part of Ecclesiastical in 1998.

RBNZ has expressed concerns EIO offered no backing other than that in the scheme of arrangement. EIO was the ultimate parent company of ACS before changing the ownership structure in December 2010. RBNZ had previously claimed the scheme of arrangement entailed an inadequate injection of capital, saying earlier this month: "The bank's view is there is a greater than 25% chance of a shortage in assets to cover costs and a higher likelihood insurer solvency requirements, which come into effect from June 30, 2012, will not be met."

It also said: "The proposed scheme is based on an inadequate injection of capital and is being promoted by a parent company [Ecclesiastical Insurance] that is distancing itself from ACS ahead of the planned implementation."

However, RBNZ said it will respect the wishes of the creditors and its paper on the matter is framed as "a provision of information", without a specific recommendation.

ACS now consists only of a settlement team for 635 former Ansvar policyholders who have quake-related claims. In terms of the scheme, EIO is providing a capital injection of NZ$24m ($19.1m), to be provided in stages, and adverse development reinsurance cover for the February 2011 quake extending ACS's reinsurance cover up to NZ$570m, plus additional share capital of NZ$4.6m upon the scheme becoming effective. Justice Venning, approving the scheme, said ACS said with the additional support from EIO there should be sufficient assets and reinsurance to enable ACS to pay all claims of policyholders in full, although it accepted this may not be the case. That EIO would provide additional support of NZ$22m on approval of the scheme was a significant factor in favour of the approval the court had given, he said.

Mark Coote/ Bloomberg

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AP Photo/Rich Pedroncelli

LD LOSS INTELLIGENCE: VELIHOODS

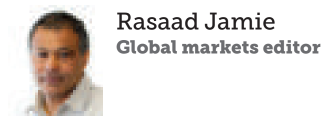
FINANCIAL WORLD TODAY

Insurance stocks pressured by uncertainty over eurozone and China

It was much more of struggle for sector stocks in Europe and Asia than it was for their counterparts in the US and Bermuda

A visitor watches stock index information displays at the Madrid Stock Exchange

Angel Navarrete/Bloomberg



Rasaad Jamie
Global markets editor

After a strong recovery the previous week, insurance and reinsurance stocks once more came under pressure in the period ending June 14, with a mixed performance by individual stocks reflecting the volatility and uncertainty in the broader financial markets.

The trend was by no means all downward, though. Indeed, the level of volatility was such that over the course of the week, one single development (such as, for example, the decision by the Spanish government to ask the EU for €100bn ($127.06bn) of financial assistance for its banking sector) could cause stock values to rise one day and fall the next, all depending on whether a positive or negative interpretation of the Spanish government's decision had gained ascendency in the markets.

Reducing the pressure

At the beginning of the week the markets rose as the announcement significantly reduced the pressure on the Spanish banking sector and on the Spanish government itself. But investor optimism soon evaporated as it became clear any relief was only temporary, as the inflow of funds into the Spanish banking sector in no way addressed many of the underlying problems of the Spanish and eurozone economies.

The uncertainty was further increased by the Greek elections set for the week-end with official polling (which by law closed two weeks earlier) suggesting a close result between the pro- and anti-austerity parties. The increase in interest rates for 10-year Spanish and Italian sovereign debt further pushed the markets downward in the early part of the week.

Struggle

As our table suggests, it was broadly speaking much more of struggle for sector stocks in Europe and Asia than for their counterparts in the US and Bermuda. This reflected investor concerns: first with the eurozone debt crisis, which continues to represent the main preoccupation for the financial markets (as it has for the previous three months); second, the economic slowdown in China, where economic data for May released over the previous week-

Table: Share prices as at close June 14, 2012

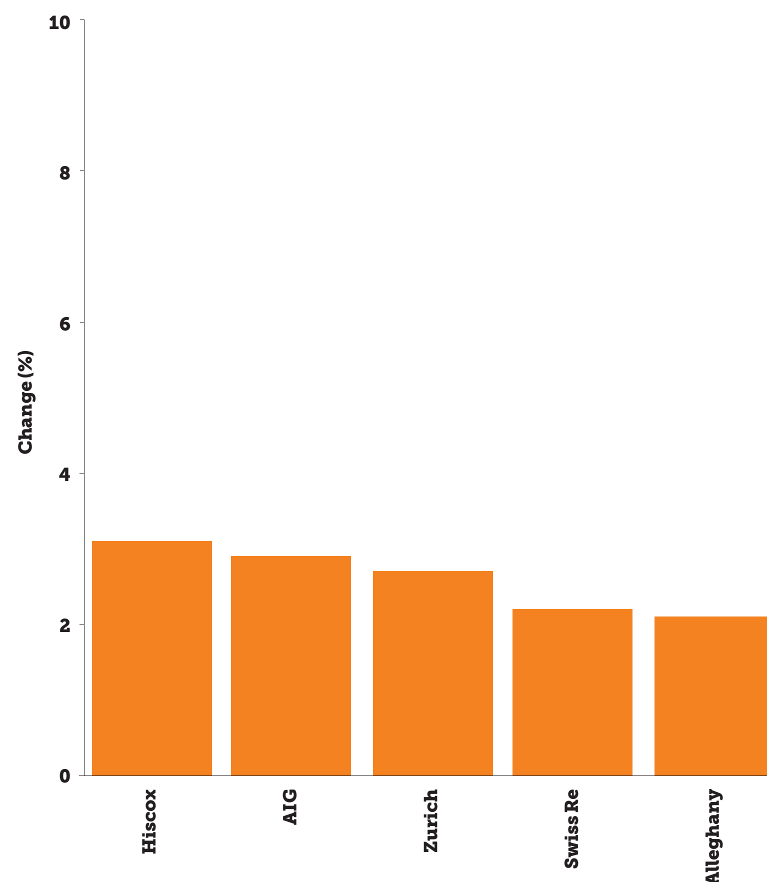
Company/group	Currency
Ace	US dollar
AIG	US dollar
Alleghany Corporation	US dollar
Allianz	Euro
Allstate	US dollar
Alterra	US dollar
Amlin	Pence
Arch Capital	US dollar
Aspen	US dollar
Aviva	Pence
Axa	Euro
Axis Capital	US dollar
Berkshire Hathaway (A)	US dollar
Catlin	Pence
Chubb	US dollar
CNA Financial	US dollar
Endurance Specialty	US dollar
Everest Re	US dollar
Generali	Euro
Hannover Re	Euro
Hiscox	Pence
Insurance Australia Group	Australian dollar
Korean Re	South Korean won
Montpelier Re	US dollar
MS&AD Insurance Group	Yen
Munich Re	Euro
NKSJ Holdings	Yen
PartnerRe	US dollar
Platinum	US dollar
QBE Insurance Group	Australian dollar
RenaissanceRe	US dollar
RSA	Pence
Scor Paris	Euro
Scor Zurich	Swiss franc
Swiss Re	Swiss franc
Travelers Companies	US dollar
Tokio Marine Holdings	Yen
XL Group	US dollar
Zurich Insurance Group	Swiss franc

Source: Insurance Day

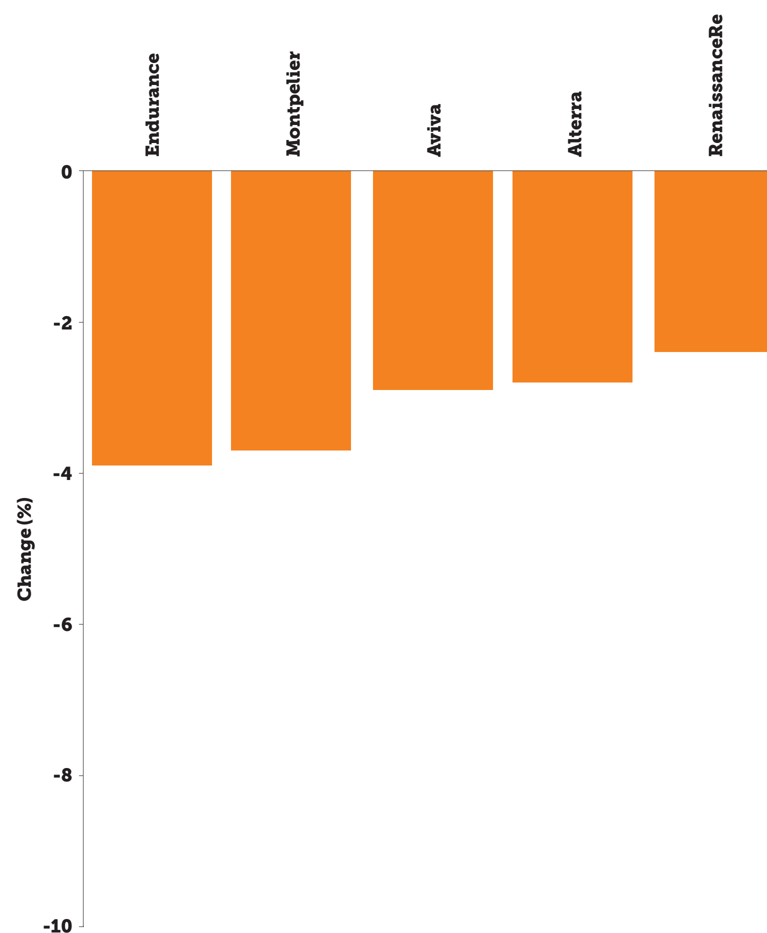
$152bn
Amount AIG has reimbursed the US government out of the insurer's total bailout of $182bn

Dec 31, 2011	Jun 7, 2012	Jun 14, 2012	Change from Jun 7 (%)	Capitalisation ($m)
70.12	72.55	72.61	0.1	24,592
23.20	30.15	31.03	2.9	55,668
285.29	325.03	331.99	2.1	5,620
73.43	72.99	72.85	(0.2)	41,817
27.41	34.07	34.44	1.1	16,922
23.63	22.91	22.26	(2.8)	2,247
313.90	325.00	324.80	(0.1)	2,506
37.23	38.23	37.65	(1.5)	5,052
26.50	28.75	28.58	(0.6)	2,044
300.80	272.50	264.60	(2.9)	11,547
10.05	9.68	9.50	(1.9)	27,476
31.96	32.65	32.51	(0.4)	4,207
114,755.00	121,175.00	122,600.00	1.2	114,141
398.70	410.80	418.80	1.9	2,339
69.22	71.03	71.33	0.4	19,256
26.75	28.49	28.16	(1.2)	7,585
38.25	39.41	37.87	(3.9)	1,643
84.09	103.34	103.51	0.2	5,460
11.63	9.25	9.34	1.0	18,254
38.30	43.88	43.95	0.2	6,694
373.5	406.40	418.90	3.1	2,479
2.98	3.31	3.30	(0.3)	6,829
15,000.00	11,250.00	11,450.00	1.8	1,120
17.75	21.13	20.35	(3.7)	1,178
1,426.00	1,252.00	1,263.00	0.9	6,708
94.59	101.00	102.00	1.0	25,430
1,510.00	1,513.00	1,523.00	0.7	30,332
64.21	72.08	71.81	(0.4)	4,635
34.11	37.15	36.76	(1.0)	1,281
12.95	12.47	12.37	(0.8)	12,737
74.37	76.04	74.20	(2.4)	3,841
105.20	101.10	101.40	0.3	5,441
18.06	18.08	18.08	0.0	4,205
21.50	20.90	21.05	0.7	4,155
47.87	54.65	55.85	2.2	21,766
59.17	61.91	63.12	2.0	24,556
1,705.00	1,836.00	1,825.00	(0.6)	18,120
19.77	20.36	20.27	(0.4)	6,318
212.50	200.30	205.80	2.7	31,889

Graph: This week's winners...



...and losers



end suggested domestic industrial output and retail sales fell for a second month in a row.

The latter development, combined with the fact the struggling eurozone is a major export market for Asian goods, weighed particularly heavily on the regional financial markets in the East.

US insurance and reinsurance stocks were notably more resilient. This was no surprise, as the previous week represented the best period the main US stock indices have seen this year as the markets were boosted by the promise of a further round of economic stimulus by Janet Yellen, vice-chairman of the Federal Reserve Bank, in the event of a further deterioration in the US employment, housing, consumer and business confidence data as a result of the worsening financial crisis in Europe.

During the week under review a number of analysts, taking a positive view, described the steep decline in US stock values in May as a necessary correction and therefore as a buying opportunity rather than as a warning to dispose of equities and to retreat into the relative safety of treasuries or gold.

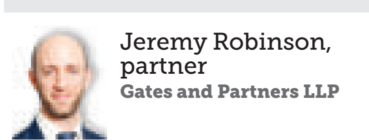
AIG

To some extent, this kind of reasoning fuelled the rise in the stock value of AIG, which gained nearly 3% during the week under review. First, there was the announcement the previous week the group's non-life division may revert back to the AIG brand as the group's financial position continues to improve and it continues to reduce its debt to the US government. Indeed, during the week under review this was further reduced when the New York branch of the Federal Reserve successfully auctioned off $7bn of securities from a special-purpose vehicle, Maiden Lane III, it set up as part of the original bailout of AIG.

According to a statement by the group, AIG had now reimbursed $152bn of the $182bn it had received from the US government. The remaining $30bn is represented by AIG shares held by the US Treasury. ■

Some unexpected D&O problems

Regulatory investigations can produce some unexpected issues for D&O insurance



Jeremy Robinson, partner
Gates and Partners LLP

In healthy economies, businesses come and go. In recession, fewer businesses come and more go. Yet whatever the state of the economy, economic regulators are here to stay, their enforcement branches rarely facing the "headwinds" with which private companies contend.

In the past year, the European Commission has imposed fines for anti-competitive behaviour the aggregate value of which is lower than in recent years. Some fines have been written off or reduced because the infringing company was unable to pay.

Enforcement zeal still strong

It would be wrong to suggest enforcement zeal has waned, however. Consequently, no matter how long the present difficulties last, we can expect more investigations to open and more fines to be imposed.

In the aviation industry, major international competition law investigations into passenger and freight surcharging have led to fines of hundreds of millions of euros and substantial damages settlements, but investigations still continue – for example, into some airline alliances and into airline co-operative agreements.

Directors' and officers' (D&O) insurance is an important way in which the insurance market covers risks faced by directors and officers. It provides additional help where a company is unable or unwilling to indemnify such officers. A company may put in place good D&O coverage as part of a package to attract talented individuals for senior roles.

As an officer of a company, you will want to know how the D&O policy is likely to respond to the types of risks that might reasonably be foreseen. Will the limits of cover be right? Will the exclusions be too broad? D&O coverage in competition law cases must respond to the risks a competition law investigation will be time-consuming, the defence costs may be high and the outcome often uncertain.

Competition investigation: investigations can distract a company from its day-to-day business

The first a company may learn of a competition investigation is through a 'dawn raid'. These are highly stressful for the company and individuals, as the authority will not wait long in reception before beginning its inspection, will generally seek to block email accounts of key individuals to prevent tampering or destruction of evidence or will seal rooms containing important documents

Competition investigations can begin by surprise and cause prolonged periods of uncertainty for companies under investigation. Individual officers and employees may be under investigation as well as the company – the Office of Fair Trading in the UK will often open simultaneous criminal and civil investigations.

Dawn raids

The first a company may learn of a competition investigation is through a "dawn raid". These are highly stressful for the company and individuals, as the authority will not wait long in reception before beginning its inspection, will generally seek to block email accounts of key individuals to prevent tampering or destruction of evidence or will seal rooms containing important documents.

A dawn raid starts a long investigatory process that distracts a company and its officers from their daily business. During this time, the outcome may be entirely uncertain. It may be clear the company is involved in some form of anti-competitive behaviour in market A, but unclear whether the same is true in markets B and C. How far should the company go to settle, with an admission of liability, the allegations in markets B and C when a cooler look at the evidence could exonerate the company and its officers?

In this context, two separate but related categories of risk arise. The first is obvious: the risk the company has infringed competition law as a result of the behaviour of individuals. For criminal cartel matters (for example, in the UK or US) there is the risk both the company and key individuals have infringed competition law.

For the costs of dealing with this risk, D&O cover may be available. As a result of the investigations into the airline sector (passenger and freight), the market is responding with aviation-specific D&O cover.

The second category of risk is less obvious, but growing in importance. It is the risk, in responding to the requirements of a competition investigation, the company or individuals within it commits an infringement of procedural law, separate from the question of whether company or individual has infringed the substantive law.

For example, the investigating authority seals a room, a cupboard containing documents or a drawer with a special seal to prevent overnight tampering and returns the next day to find the seal broken.

Another example: the investigating authority needs the company's IT department to block the email accounts of specific individuals by setting a new password only the investigators know. The authority then discovers an individual got the IT department to unblock the account, even temporarily, or to divert incoming new mail to that individual via a different server or unblocked account.

These are not academic examples. E.on was fined €38m ($48.2m) for breaching a seal attached during an investigation, a fine upheld by the General Court of the EU on appeal. Suez Environnement and its subsidiary Suez Lyonnaise des Eaux were also fined €8m for a similar infraction.

At the end of March 2012, the European Commission fined Czech energy companies €2.5m for obstructing an inspection by failing to block email accounts, diverting emails to another server and failing to open encrypted emails.

A less obvious situation: a company tries hard to meet the requirements, providing information such as an organisation chart of the company, or explanations of various documents; the investigating authority decides these efforts are in some way incomplete, late or not in agreement with the investigators' other evidence or the accounts of other witnesses.

Does that mean the company under investigation has committed a procedural infringement in those cases too? The Spanish competition authority recently imposed a penalty of €2.09m on ferry companies for delaying the start of an inspection, providing information late and in incomplete form and interrupting IT communications.

Differing interests

The problem is in part the potential gap between the company and the individuals' interests in attributing responsibility for actions that increase the company's exposure in procedural infringement cases.

A further problem is in some jurisdictions, such as the UK, individual criminal penalties may apply under the Competition Act 1998 for obstructing investigations and the failure to co-operate with an investigation may be an aggravating factor increasing a company's fine for any substantive infringement.

The problem is made more complex by the mismatch between the law in relation to obstructing investigations and the coverage, which might be provided by a D&O policy. Under EU law (Reg 1/2003), a fine may be imposed for procedural infractions committed as a result of intention or negligence. Under UK law, criminal liability can be imposed for a variety of offences where the trigger may be intention or recklessness, or even strict liability in relation to providing information.

You would expect D&O cover to exclude intentional acts, but many cases of alleged obstruction of an investigation will be less clear-cut and the possible coverage of D&O unclear. This is a question the market should now address. ■

Florida court restricts first-party bad faith claims

Mark Leimkuhler, partner
Lewis Baach PLLC, Washington, DC

Florida's highest court has ruled a first-party insured may not sue for breach of an implied warranty of good faith independently of the state's bad faith statute. The ruling means in Florida a first-party insured must prevail in its coverage lawsuit before it can sue for bad faith.

The case, *QBE Insurance Corp v Chalfonte Condominium Apartment Association, Inc*, arose out of hurricane damage to Chalfonte's property. Dissatisfied with its insurer's handling of its claim, Chalfonte sued in federal court for breach of contract and breach of the implied warranty of good faith and fair dealing.

A jury awarded Chalfonte damages, including $272,000 for breach of the implied warranty. Appeals followed, and a federal appeals court certified insurance questions to the Florida Supreme Court.

The Supreme Court explained Florida common law historically allowed an insured to sue for bad faith for failure to defend and settle third-party claims, but not for failure to pay first-party claims.

In 1982, the Florida legislature created a statutory bad faith cause of action for first-party insureds. The statute requires the insured to prevail on its first-party coverage claim before it can bring a claim of bad faith, setting up two-stage litigation of such claims.

In *QBE v Chalfonte*, the insured prosecuted its "implied warranty" claim at the same time as its coverage claim. It argued its claim of breach of the implied warranty of good faith is distinct from a statutory bad faith claim. The case thus presented the issue of whether a common law claim of breach of the implied warranty of good faith exists in Florida independently of the bad faith statute.

The Florida Supreme Court ruled it does not. Citing federal decisions predicting Florida law on the point, the court acknowledged Florida recognises an implied covenant of good faith in all contracts, but viewed statutory bad faith and breach of the warranty of good faith as "two sides of the same coin"; thus, the statutory remedy was adequate.

The court also felt allowing claims for breach of the implied warranty would effectively adopt an unworkable "reasonable expectations" standard to interpret insurance policies.

Increasingly, insureds in coverage litigation have pursued bad faith allegations contemporaneously with first-party coverage claims. The ruling confirms in Florida such allegations may be pursued solely under the statute – and only after an insured has prevailed on its coverage claim. ■

Senior managers not 'vicariously liable' for the misconduct of others

Steven Francis, partner, and Robbie Constance, senior associate
Reynolds Porter Chamberlain LLP

The law has always been clear and even the UK's Financial Services Authority's (FSA) rules are clear but there was, nonetheless, great interest in (and relief among senior managers at) the outcome of the long-awaited Upper Tribunal decision in *John Pottage v FSA*.

It confirms senior managers cannot be liable for misconduct purely because of systems and controls failures that happened on their watch – the FSA must prove personal culpability for failing to achieve a reasonable standard of conduct.

The FSA case

Pottage was appointed chief executive of UBS's wealth-management business in September 2006. The FSA alleged he failed to discharge his responsibility to carry out an adequate "initial assessment" of the governance and risk management framework of the firm and had he carried out the initial assessment properly, "it would have been apparent there were serious flaws in the design and operational effectiveness of those [governance and risk management] frameworks".

Pottage should then have instigated a "systematic overhaul" – the kind of steps the FSA thought reasonably required to ensure compliance. The FSA's complaint was he should have done such a systematic overhaul earlier.

The tribunal's decision

The tribunal did find serious flaws in the firm's systems and controls but, on the crucial question for the personal enforcement action, decided (on the facts) Pottage had not behaved unreasonably.

Importantly, the tribunal said: "no one [in the firm itself] or indeed the FSA, had suggested, before the initiation of the [systematic overhaul], that it was necessary or appropriate to carry out a wider review of systems and controls than had in fact been put in place."

Is reform possible?

The tribunal's legal analysis is unremarkable but important; making clear the test for personal culpability for misconduct under the FSA's regime is essentially the same as that for negligence – reasonableness.

The case produces no new law but serves as useful confirmation (in the words of the FSA's own rule (DEPP 6.2.7G) "the FSA will not discipline approved persons on the basis of vicarious liability (that is, holding them responsible for the acts of others), provided appropriate delegation and supervision has taken place".

True vicarious liability is appropriate for assessing an entity's liability to pay compensation but does it really have any role to play when disciplining a human being? What is the point of disciplinary liability in the absence of genuine fault?

We hope neither the law nor regulation will be reformed to invoke vicarious liability in misconduct cases. ■

A postcard from the Middle East

From the warmer shores of the Middle East, we send a short postcard looking at the state of play of the local insurance market. The global financial crisis certainly affected the regional economies. However, the international (re)insurance community ignores the Middle East market at its peril as:

- GDP in the Gulf Co-operation Council (GCC) has almost quadrupled in nominal terms since 2001, at a compound annual growth rate of 14.2%, and is expected to reach $1.5trn in 2013;
- Population growth has almost tripled the world rate with about 50 million GCC residents expected by 2013;
- The GCC population is still young (average age is 23 to 31);
- GCC government spending was estimated at $302bn in 2011, including more than $40bn focused primarily on social infrastructure alone; and
- Insurance penetration has historically been very low (less than 1% of GDP). However, attitudes are changing, fuelled by a rise in compulsory motor and health insurance.

There is no single GCC regulatory framework for the (re)insurance industry. This fragmented landscape makes it challenging to establish a regional presence presenting legal pitfalls in specific territories for the unwary. Although consolidation among the insurers is required, there remains a need for good-quality, specialist product providers.

$1.5trn
Expected GDP of the GCC by 2013

What about the events of the Arab Spring? In the short term, there has been an impact on the claims experience in the region. We have seen coverage disputes between local insurers and international reinsurers with a focus on the strike, riot and civil commotion exclusions.

If anything, these disputes have highlighted the need to ensure reinsurance treaties have appropriate choice of law and dispute resolution provisions and there is a proper understanding of the underlying policy wordings and their enforceability under local law.

The longer-term effect appears to be the countries less affected by the events of the Arab Spring (for example, Qatar and the United Arab Emirates (UAE)) now have perceived competitive advantage in seeking to attract new businesses to the region.

The regime change that has occurred in territories such as Egypt and Libya may also create opportunities for (re)insurers in these markets. Of course, the market for full political violence cover has also improved.

For those considering entering the GCC market, a variety of structures are used by insurers in the region. Most jurisdictions permit the establishment of a branch of a foreign insurer (which avoid restrictions on foreign ownership and capital requirements).

However, in Saudi Arabia it remains the case any (re)insurer wishing to establish a presence in the country must establish a listed joint stock company. A moratorium on new (re)insurance licenses in the UAE has led to a growth of foreign insurers entering into partnering arrangements with locally licensed insurers based upon a "fronting" model, but also including outsourced service agreements with the foreign (re)insurer.

Establishment in the Dubai International Financial Centre or Qatar Financial Centre is also a viable alternative for reinsurers. ■

Peter Hodgins and Wayne Jones are partners in Clyde & Co's Dubai office

• Clyde & Co will be hosting a seminar at its London office to discuss "The insurance market in the GCC – the recovery from the Arab Spring and the global recession" on Wednesday, June 27, 2012 at 4pm. For further details please contact Amanda Thomas at Amanda.Thomas@clydeco.com

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