

FROM THE WORLD OF GENERAL INSURANCE

World Trade Center

General insurers were recently pleased to receive further favourable court decisions with regard to the World Trade Center property claims. In May, a federal jury in New York found that ten insurers of the World Trade Center property risk were bound by the so-called Wilprop form, which defined the destruction of the two towers as a single event. Silverstein Properties Inc, the main leaseholder on the building, had contended that the policy applying to the loss was that produced by Travelers Property Casualty Corp, under which the events of 11 September 2001 could potentially be defined as two losses, and under which there was the possibility of claiming \$7bn.

This is the latest setback for Silverstein, as various insurers have been found in a series of court decisions to be subject to policy wordings under which only one (\$3.5m) limit of liability should be paid. All of these issues have arisen as a result of the fact that the policy wording had not been agreed with underwriters prior to the date of the claim, and the different insurers were in different stages of knowing the alleged intentions of the policyholder and Willis, their broker.

The decisions so far all tend to simplify the position for insurers and their actuaries trying to establish appropriate reserves for these terrorism-related losses – prior to court decisions being reached they have had to allow for the possibility that the losses would be up to double what they have contended.

The next stage of the litigation will commence on 27 September 2004, when the final group of insurers will defend themselves against a similar argument from Silverstein.

Asbestos developments (or not)

The latest attempt to pass the Fairness in Asbestos Injury Resolution (FAIR) Act in the United States has again failed. This is the third attempt which has been made to obtain agreement from the interested parties to a trust fund solution to the longstanding asbestos litigation issues. While there appears to be agreement on many of the fundamentals of the proposed solution, there are a considerable number of points of detail on which consensus has not, so far, been achieved. These include the amounts which the various parties (asbestos defendants and their insurers) would contribute to the trust fund, and the issue of finality. Insurers, in particular, are only prepared to enter into such a solution if they can be guaranteed that no further US asbestos claims can subsequently be found against them. In spite of the latest failure, talks are continuing under the leadership of Senators Frist and Daschle.

Elsewhere in the United States, Ohio became the first state legislature to pass measures which set minimum medical impairment criteria to be met by claimants making damages claims arising from exposure to asbestos and/or silica particles. This move was speedily welcomed by insurance industry representatives. It is believed that several other states may follow Ohio in this respect over the next few months.

Meanwhile, in the UK, we have seen the introduction on 21 May of the Control of Asbestos at Work Regulations, under which employers have an increased duty to manage asbestos risks in their buildings. For most employers the first requirement is for them to identify the presence of asbestos in the workplace. It is believed that many organisations have substantial amounts of work to do in this regard, and this is not likely to be a short-term issue as there are relatively limited numbers of specialist surveyors available to meet the demand. It is feared by insurers that the new regulations could open up additional sources of asbestos-related claims in the UK.

IOC buys Olympic cancellation cover

The International Olympic Committee has purchased a \$170m policy to cover the possible cancellation of the Olympic Games in Athens in August. The coverage, which is led in the Lloyd's market, includes a range of natural perils plus terrorism. It is understood that this is the first occasion on which the IOC has purchased cover of this type. The major risk, apart from terrorism, is considered to be earthquakes, to which the city is prone.

In view of the recent controversy surrounding doubts as to the timely completion of some of the Olympic facilities, it should be noted that there is no coverage provided against cancellation because of such an eventuality.

Compensation culture

Taking up the issues raised by the much-publicised GIRO paper from 2002, there have been a couple of further reports on the subject in recent weeks. First Norwich Union published a report on a telephone survey which they had carried out on the subject. This indicated that the 'blame' culture was taking hold in UK society, with a significant proportion believing they should claim whenever possible. These trends were said to worry a substantial majority of those questioned, and nearly 40% believed that people making false claims should be prosecuted. The 'no-win, no fee' approach to pursuing legal cases was considered to be a major factor in fuelling the trend towards a greater compensation culture.

Subsequently, a report by the Better Regulation Task Force came to rather different conclusions, describing as 'a myth' the idea that a compensation culture exists in the UK. This appears to be based on the fact that the cost of litigation in the UK was very much less than that in the United States, and has not increased materially as a percentage of GDP over the past decade or so. In addition, the UK percentage of GDP represented by tort costs is lower than in virtually any other European country. The report makes a number of recommendations to the government, including a proposal that medical facilities should receive guidelines on advertising permitted by claims management companies on their premises, and that research be carried out into the impact of contingency fees within the legal system. The Association of British Insurers has welcomed this report.

Large Losses

Recent notable general insurance incidents/losses include:

- The collapse of a 30-metre section of a terminal at Charles de Gaulle airport, Paris on 23 May, resulting in four deaths and dozens of injuries. Initial estimates of the cost of this loss range up to €750m. The building is insured by a number of French companies, but the loss may be subrogated against the architects and/or contractors responsible for the design and building of the terminal.
- Floods in Haiti/Dominican Republic – while these resulted in heavy loss of life and property damage, they are not likely to cause major insured loss, as very limited insurance coverage is purchased in this area.
- Marine collision of Singapore – occurred on 23 May, and involved a car carrier *Hyundai 105* (which was holed and sank with its cargo of over 4,000 cars) and a Japanese very large crude carrier *Kaminesan* (whose cargo of crude oil appears to have remained intact). There were no casualties, but the property losses have been estimated at around \$100m. The tanker risk, while insured in Asia, is likely to result in reinsurance losses arising in the London market.
- A fire at a warehouse in London's East End on 24 May destroyed or seriously damaged a significant number of works of art in storage. Insurance losses of up to £50m have initially been estimated, most of it to be borne by London market underwriters.

For further details, the latest General Insurance Current Issues newsletter is on the profession's website at www.actuaries.org.uk/files/pdf/general_insurance/gicinews20040528.pdf.

 DAVID HART

FROM THE WORLD OF PENSIONS

Opra

The Occupational Pension Schemes Regulatory Authority (Opra) has published new guidelines on compromise agreements relating to underfunded defined-benefit pension schemes.

The new guidance, 'Compromising an employer's debt – actions that Opra expects trustees to take' (Update 7) outlines important steps trustees must take when considering compromising an employer's debt in an underfunded pension scheme.

In certain circumstances, where a defined benefit pension scheme is underfunded, trustees may be able to obtain more money for the scheme and its members through a compromise deal with the employer than they would by enforcing the whole statutory debt. This is because enforcing the whole debt could lead to the employer's insolvency where the trustees would not be high on the list of creditors. Another factor the trustees may consider is that current members may also lose their jobs if the employer is forced into liquidation.

Opra's new update is aimed at pension scheme trustees, scheme actuaries, trustees' legal advisers, and other scheme advisers. When considering a compromise deal, trustees have a fiduciary duty to ensure they are acting in the best interests of scheme members, and should obtain appropriate independent professional advice.

Opra is aware of cases where trustees may not have acted appropriately to ensure that compromises are in the interests of members. This new guidance should help trustees consider possible alternatives to compromise deals, handle potential conflicts of interest, and make sure they negotiate the best settlement if they decide that such an arrangement is in the members' interests.

Opra has also published *Bulletin 31*, its latest quarterly bulletin. Its contents include:

- ◆ introducing the new regulator – a look at the new regulatory body and how it will operate;
- ◆ new scheme funding requirements – an overview of the proposed scheme-specific funding arrangements;
- ◆ demonstrating a standard of care – Brian Holden MBE outlines the principles involved in effective risk management for trustees;
- ◆ a European partnership – the role of the Committee of European Insurance and Occupational Pensions;
- ◆ suspicious transfers? – how to remain alert to the dangers of pension liberation.

Both documents may be found at www.opra.gov.uk.

Pension Protection Fund

The first chair of the Pension Protection Fund has been announced as Lawrence Churchill, currently chief executive of Zurich Financial Services.

He will take up the post in July, subject to parliamentary approval.

Prior to Zurich, he was chairman and managing director of UNUM Limited, and before that helped to set up NatWest Life. His earlier background was in systems analysis.

The government has also announced an amendment to the Pensions Bill to compensate members who have already lost out in the wind-up of underfunded final salary schemes (eg members of the much publicised Allied Steel & Wire plan).

The proposal establishes a fund with £400m of public money, to be paid in over 20 years and with the possibility of further payments from industry.

There will be consultation on the operation of this fund, and its running will be reviewed in three years' time. It is not clear who will be eligible to benefit from the fund nor the level at which compensation will be set.

Pension scheme litigation

Just as we went to press was announced the first litigation by pension scheme trustees against their former actuarial adviser. An adviser to the new trustees of the pension scheme of Blyth and Blyth said: 'We have been advised by our lawyers that a strong case can be made against the scheme actuary and certain former trustees. Based upon this advice, proceedings are being instigated by the present trustees in order to reverse three early retirement decisions and to recover other losses to the pension fund.' The scheme actuary was Buck Consultants, now part of Mellon Human Resource & Investor Solutions.

Blyth and Blyth went into receivership in January 2003 after being unable to plug a £6m hole in its final salary pension scheme. Scheme members who had not retired by November 2002 lost their entire pension, while doubts remain over the future benefits of those who had already retired.

'Two nations' in pensions – ACA

Government measures designed to promote occupational pensions are more likely to discourage provision and are expected to add to employers' costs. These are the startling findings of the latest survey conducted by the Association of Consulting Actuaries (ACA) following the publication of the government's Pensions Bill in March 2004. The survey report paints a picture of a 'divided nation' in pensions, with those fortunate enough to be covered by defined benefit schemes – an increasing number of public sector workers (supported by the taxpayer) and those private sector firms that are able and willing to bear the costs and liabilities – enjoying greater

certainty over their pension future. Set against this are a growing number of employees of all ages taking on greater investment risk, supported by generally low levels of contributions. Copies of the ACA report '2004: Smaller Firms Pensions Survey: a Divided Nation' are available from the ACA, No 1 Wardrobe Place, London EC4V 5AG or at www.aca.org.uk (go to the 'Home/What's New' page).

New pensions burden

The costs involved in running company pension schemes looks likely to rise sharply after the implementation of the Insurance Mediation Directive (IMD) in January 2005. The warning comes from the chairman of the Financial Services Committee of the Society of Pension Consultants, who believes the IMD will bring a number of activities provided by third-party pension administrators for the first time under the regulation of the Financial Services Authority (FSA).

Mike Young said: 'The cost impact of regulation by FSA will hit margins on this sort of business hard. The real cost impact will ultimately have to be passed on to the schemes themselves, which may well drive a number of smaller occupational schemes to consider that alternative arrangements such as group personal pensions, may be the way forward for them.'

'Third party administrators need to consider how they will seek authorisation to undertake these regulated activities, along with how they will ensure compliance with requirements relating to financial reporting and capital adequacy, money laundering regulations, client money regulations, and senior management systems and controls.'

Useful checklist from PMI

The Pensions Management Institute Trustee Group has drawn up a checklist of the documents and information that newly appointed trustees need to help them make informed decisions. The checklist has been issued to all members of the PMI Trustee Group and the broader PMI membership, and is now available free of charge from the PMI website at:

www.pensions-pmi.org.uk.

Commenting on this development, PMI president Roger Cobley said: 'The Pensions Bill says that "trustees must be conversant with the trust deed and rules". They will also be required to have relevant knowledge across the full range of trustee responsibilities. Therefore, the PMI felt that it was an appropriate time to publish a practical, step-by-step guidance sheet to prepare them better for the challenges ahead.'

 GORDON SHARP

Equitable actuary 'banned' by FSA

The Financial Services Authority has banned Christopher Headdon, former chief executive of failed insurance company Equitable Life, from working in a senior role in the City for six years. The punishment is the result of Headdon's failure to disclose an agreement which limited a crucial financial arrangement which the regulator thought gave Equitable £800m to meet claims for controversial guaranteed annuities. Full details may be found at www.fsa.gov.uk.

Long-term care market in difficulties

Bupa is withdrawing from pre-funded long-term care cover and has ceased to accept new business from 11 June, in an apparent U-turn in the company's strategy. Bupa announced in November 2003 it was concentrating on the pre-funded market, rather than immediate care.

The pre-funded long-term care market has been shrinking drastically over recent years. Norwich Union and Axa Lifetime Care withdrew in 2003 and were followed this year by Scottish Widows. 'The underlying problem is that consumers are confused about their choices', said a BUPA spokesperson. 'Until there is a clear policy from government and local authorities, the market will not change. However, there is scope for the development of new products and Bupa will continue to look into this segment of the market.'

Protection trends

Swiss Re Life & Health Limited last month published its latest *Term & Health Watch*, the annual benchmark analysis of new life and health insurance sales to UK consumers. Highlights included:

- ◆ Sales of term assurance policies in 2003 increased by more than 4% over the previous year, with over 2.1m policies sold. This number of sales is a record for the industry and, year on year, represents the ninth successive rise in sales.
- ◆ Individual critical illness (CI) and

income protection (IP) sales, however, experienced a decrease since the previous year, although sales of mortgage-related CI showed a modest 2.9% improvement over 2002.

- ◆ The average sum assured, across all distribution channels, for a new individual term assurance policy in 2003 was £93,299 (2002: £87,437). Sales by independent financial advisers (IFAs) account for the highest average sum assured. The average premium, across all channels, was £370 (2002: £349).
- ◆ New mortgage-related term sales in 2003 increased by more than 5%, compared with the year-on-year increase in new mortgage loans of only 3%. It is possible that these results reflect a degree of rebroking of policies alongside a remortgage – especially given the 50% rise in remortgaging in 2003 – rather than a pure increase in penetration for new customers.

- ◆ A number of factors point to the decline in new sales of CI cover, which fell some way short of the remarkable 33.9% growth that occurred between 2001 and 2002. *Term & Health Watch* signals a number of reasons for the fall, including concerns over earlier-than-expected diagnoses of critical illnesses – made possible through medical advances – which has contributed to a reduced appetite for long-term guarantees. This has resulted in significant price increases for consumers and market uncertainty for intermediaries.
- ◆ Annual increases in individual IP sales since 2000 were not sustained in 2003. The 11.8% decrease in new sales can be attributed, according to the survey, to a lack of consumer awareness about the need for IP cover and to the preference, amongst intermediaries, to concentrate on CI to protect the mortgage.

Life solvency on the mend

The Centre for Risk and Insurance Studies (CRIS) at Nottingham University has now completed its preliminary analysis of the top 20 with-profits life insurers' returns to the Financial Services Authority (FSA).

Several life insurers have now published a 'realistic balance sheet' as part of their returns to the FSA: this shows that, on average they have 2.4 times the capital that would be needed to meet the effect of specified adverse financial conditions (the 'risk capital margin'). The traditional measure of solvency shows that life insurers' finances are healthier than a year ago, with the free asset ratio up by 2.7% points to 9.3% on average (though it was 22.5% in 1999).

Chris O'Brien, director of CRIS, commented: 'The new figures from the realistic balance sheet are more helpful than the traditional but artificial approach to solvency: the liabilities rightly reflect asset shares, and contain a more robust calculation of options and guarantees. However, the realistic balance sheet is not realistic in showing financial strength: it fails to include other capital that life insurers have available if

needed; and the risk capital margin requirement does not cover all relevant risks.

'Part of the improvement in the traditional free asset ratio arises because nine of the 20 companies have used waivers from the traditional rules in calculating their liabilities: these remove some of the artificialities in the calculations (which has been a well-known problem) but it also means comparisons are difficult.

'Insurers are making less use of financial engineering: in 2002 they used £8.8bn of future profits and £2.4bn of other forms of financial engineering (such as financial reinsurance): these figures are down to £4.2bn and £2.2bn respectively.

'We are in an interim stage as FSA develops its new reporting rules. This means companies are using different methods and assumptions. Until the new rules are introduced fully we cannot make a true assessment of the financial prospects of the sector; the current mixture of methods leaves us in a muddle.'

The survey of life insurers' FSA returns is at www.nottingham.ac.uk/business/cris.