

From the world of general insurance

Asbestos and pollution developments

Eternit AG, a Swiss building products company, has established a fund of SFr1.25m to compensate employees and neighbours of its two plants in Niederernun and Payerne who are suffering from asbestos-related illnesses. It is understood that there is no relevant insurance available, so the funds are being provided by the company. The fund has been criticised by the local Asbestos Victims Association on the grounds that it will prove inadequate, and that the proposed distribution of compensation is under the control of the company rather than the courts.

In the UK, the Financial Services Authority is proposing secondary legislation to guarantee redress from the Financial Services Compensation Scheme in respect of bankrupt companies, in the event that one company (or its insurer) pays the full amount of compensation for asbestos-related disease although there are other companies also involved, as required under the Compensation Act 2006. This is an attempt to speed up the provision of compensation – there has apparently been considerable reluctance by companies and their insurers to pay the ‘shares’ of bankrupt companies when there is no guarantee of recovering the proportion for which the defunct companies were responsible.

A US appeals court has upheld an appeal by Lloyd's and London Market companies against the allocation of pollution claims in a case involving four sites near Niagara Falls owned by Olin Corp. The case was referred by the appeal court judge to the US District Court for the Southern District of New York for reconsideration, on the grounds that the original jury had been wrongly instructed to allocate the liability over a period which excluded an ongoing problem of contamination of groundwater.

Terrorism

The election of Democrat majorities in both houses of the US Congress is

believed to increase the chance of extending the federal terrorism insurance provision after the current Terrorism Risk Insurance Extension Act expires at the end of 2007. The new Democratic chairmen of the Senate Banking, Housing, and Urban Affairs Committee, Senator Christopher Dodd, and of the House Financial Services Committee, Representative Barney Frank, have stated that they see the issue as a priority, and would like to find a permanent solution, an aim not shared by President Bush.

Meanwhile, insurers are moving back into the aviation terrorism insurance market in some force, for the first time since the terrorist attacks of 11 September 2001, as premium rates in the main hull and liability markets have weakened by around 25% during the main renewal season in the final quarter of 2006.

Finite risk reinsurance

Bob Cooney, chairman and chief executive of the Bermudian reinsurer Max Re, resigned at the end of October as the company reopened investigations into two finite risk reinsurances – they were also restating earnings for periods from 2001 until the second quarter of 2006 to reflect what appears to have been inappropriate accounting for the contracts, with the company's earnings set to be reduced by about \$10m. These contracts are two of the three into which the company carried out investigations earlier in 2006, on the basis of which no adjustment was made, but apparently further information has come to hand.

Eliot Spitzer, the New York attorney general who has been instrumental in pursuing various insurance industry players for their accounting and other practices in the finite risk reinsurance and contingent commissions areas, has been elected as Democrat governor of New York in the mid-term elections. He is to be succeeded as attorney general by Andrew Cuomo – it is thought

unlikely that this will have any impact on the direction of ongoing and future investigations.

The UK Financial Services Authority (FSA) has fined Berkshire Hathaway subsidiary General Re £1.225m for carrying out illegitimate reinsurance transactions. One of the transactions consisted of a series of contracts which resulted in reinsurance profits being passed in a ‘circular’ manner from a German company, via two Berkshire Hathaway subsidiaries, to an Irish subsidiary of the German company, providing tax advantages to the Irish subsidiary. It is the second-largest fine to be imposed by the FSA.

Lloyd's

Ed Balls, economic secretary to the Treasury, has proposed amendments to the Financial Services and Markets Act 2000, which would allow all resigned Lloyd's names (and not only those who resigned on or after 24 December 1996) to participate in the Part VII transfer which forms a significant part of the proposed process resulting in the takeover of Equitas by National Indemnity Company (see the December issue of *The Actuary*). Another proposed amendment to the legislation clarifies that reinsurance business can be transferred using the Part VII procedures.

The Lloyd's names who sued the UK government for failure to implement properly the first European Insurance Directive on non-life insurance (see these columns in the October 2006 issue) have lost their case on the grounds that the names did not have the right to sue the government in a class action, and that their compensation claim had expired.

Catlin managing agency has completed the acquisition of the Wellington agency for £591m, thus forming the largest managing agency at Lloyd's with capacity of approximately £1.25bn based on 2007 combined stamp capacity. Several senior Wellington staff have already

left the combined group following the takeover.

Another Lloyd's market acquisition in November saw Disciple Holden, a company funded by private equity firm Alchemy Investment Plan, take over Cathedral Capital for £113m. It is the first Lloyd's insurance group to be owned by a private equity firm.

Managing agency Chaucer has teamed up with US insurer ICAT Holdings to form a new syndicate 4242. This will have capacity of £148m, which will be utilised to write commercial business for small and medium-sized companies in catastrophe-exposed regions of the US. Greg Butler is the active underwriter.

HIH Casualty & General Insurance Ltd (HIH)/FAI General Insurance Company Ltd (FAI)

Another executive of this failed Australian group, Anthony Boulden, who was financial controller of FAI, has been sentenced to a prison term, following his involvement in the fraudulent alteration of records to reduce the estimated claims reserves of the company. Mr Boulden was decreed to have played a role in the failure of the HIH group, and received a 12-month sentence. Another FAI employee was sentenced to 500 hours community service for making misleading statements.

In addition, HIH liquidators are suing Lloyd's syndicate 386, managed by Limit, for recovery of reinsurance amounts totalling A\$54m. The amounts are disputed by Limit on the grounds that the relevant claims were never paid by HIH, and therefore there could be no indemnification provided by the reinsurer.

Converium Holding Ltd (Converium)

Converium, a Swiss reinsurer, has achieved its aim of improving the company's credit rating, following the sale of its North American busi- ➤

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ness, as reported in the previous issue of *The Actuary*. Fitch improved the company's rating from BBB- to BBB+, and subsequently AM Best upped its rating on the North American subsidiary from B- to B+.

Travel insurance

In November, the UK government announced an investigation into the unregulated sale of travel insurance by travel agents and tour operators. This will consider the level of complaints and the standard of training provided to the sales staff in an attempt to check whether there is mis-selling prevalent in the market. The inquiry does not extend to travel insurance sold by insurers and brokers, which is already regulated.

US reinsurance collateral

The National Association of Insurance Commissioners has voted in favour of introducing a new risk-based regime for reinsurers writing business in the US. Under this, there would no longer be a distinction in the collateral required between companies domiciled in US and those from elsewhere in the world. Instead, a new Reinsurance Evaluation Office would assign each reinsurer to one of six ratings, and the collateral required to write US-based reinsurance would vary from 0% to 100% in 20% steps depending on the rating assigned. The proposals, which received predictably greater welcome in Europe than in US, are expected to be finalised later in 2007.

QBE takes over Praetorian Group

Australian insurance group QBE announced in December that it had acquired Praetorian Financial Group from Hannover Re for \$800m. The deal, which involves three US companies writing premium income of around \$1.4bn in the primary specialty markets, is expected to be completed by the middle of 2007.

Large losses

Loss updates and related issues include:

■ **Air crash near Strasbourg (20 January 1992)** Airbus, as manufacturer of the plane, and Air France, as owner of the airline, were recently (after nearly 15 years – who says aviation insurance is short-tail business?) found liable for the crash in which 87 people died.

■ **Hurricane Katrina (25–30 August 2005)** A federal judge has ruled that the Insurance Services Office wording for flood exclusions (used by many insurers) was ambiguous and that Katrina-related flood losses should be covered by the companies concerned. Some of the affected insurers are appealing the decision.

■ **Explosions and fire at oil storage depot at Buncefield, England (11 December 2005)** Estimates of insured losses have now risen from an initial £300m to £600m and are still rising, as claims have become increasingly complicated (such as those for reduced property values in the area), and business interruption periods have increased.

■ **Snowstorm in New York state (12 October)** Updated reports suggest that the cost of this unusual event is around \$210m.

■ **Earthquake in Hawaii (15 October)** Contrary to initial reports, major property damage was not sustained, and insured losses are expected to be less than \$25m.

■ **Windstorms in northern Europe (28–29 October)** These principally affected the northern isles of Scotland, and parts of Denmark and Sweden. Although there were significant power cuts owing to falling trees in both Orkneys and the west coast of Sweden, insured damage does not appear to be very significant.

■ **Air crash in Nigeria – 29 October** This involved a Boeing 737 of ADC Airlines, which crashed on take-off in seriously adverse weather conditions, on an internal flight from Abuja to Sokoto, killing 96 of the 105 people on board. It is understood that hull and liability insurance

is placed in the Russian market.

■ **Rainfall and flash flooding in Turkey (early November)** These occurred in widespread areas of the country causing significant damage and over 50 deaths. Insured losses are unlikely to be material as the areas affected were among the poorer regions of the country.

■ **Windstorm Britta in Scandinavia (1–2 November)** This produced high winds, snow, and sleet in Norway, Sweden, and Finland. The major impact of the storm was at sea, where a 15,000 ton freighter (*Finnbirch*) sank in the Baltic off the coast of Sweden with the loss of two lives, and an oil-drilling platform was cast adrift in winds gusting to 90mph in the North Sea. Insured losses in the marine market are expected to be significant although no overall estimate is to hand.

■ **Earthquake and tsunami in Hokkaido, Japan (15 November)** The earthquake measured 8.3 on the Richter scale and was centred on the Kuril Islands to the north-east of Japan. Given the magnitude of the quake, remarkably little damage appears to have resulted, and the tsunami was only measured at 40cm, much less than the warnings had predicted.

■ **Typhoons Durian and Utor in the Phillipines and Vietnam (30 November–14 December)** These two typhoons followed very similar paths across the Phillipines, approximately a week apart. Durian was the more deadly storm, with wind-speeds of up to 125mph and also created mudslides of volcanic ash and boulders off Mayon Volcano. Durian caused at least 720 deaths in Phillipines and around 100 in Vietnam. Utor was made worse by the already saturated terrain, but was less severe with 'only' 100mph winds and a much smaller loss of life. Although economic damage from these storms is very significant, very little of it is insured, so insured losses will be modest.

■ **Fire and explosions at fireworks factory at Halland, East Sussex (3 December)** This caused the deaths

of two members of the fire service, 12 injuries, and the complete destruction of the building, plus damage to surrounding properties. While no insured loss estimate is to hand, coverage is understood to be with that well-known Icelandic insurer, European Risk Insurance Company.

■ **Tornado in north-west London (7 December)** This caused damage to around 150 homes in the Kensal Rise area and injured six people. Insured losses are unlikely to be more than £20m in view of the small area affected.

■ **Winter storms in north-western United States (11–15 December)** These mainly affected Washington and Oregon states, and involved winds of up to 90mph and heavy falls of rain and snow. At least ten people have lost their lives, and initial estimates of insured losses are around \$500m.

■ **Sinking of ferry off Java, Indonesia (29 December)** This ferry was on route from Borneo to Java, when it sank in a storm with the loss of over 400 of an estimated 628 on board. Insured losses are unlikely to prove material.

Two groups of forecasters have predicted above-average hurricane activity in 2007. Tropical Storm Risk has estimated that there will be land-falling hurricanes 60% above the average over approximately the previous 50 years. The Colorado State University research team forecast 14 named storms including seven hurricanes, three of category 3 or higher. Happy new year!

Current Issues Newsletter

Other recent developments are covered in the General Insurance Current Issues Newsletter, which can be accessed via the profession's website at:

www.actuaries.org.uk/Display_Page.cgi?url=/general_insurance/gen_ins-curr-issues.html

 DAVID HART

2006 a benign year

According to preliminary estimates from Swiss Re (www.swissre.com), natural and man-made catastrophes triggered total economic losses of around \$40bn, and cost property insurers worldwide \$15bn in 2006. Earthquakes, cold spells, windstorms, and also shipping disasters claimed numerous victims. In all, an estimated 30,000 people lost their lives in catastrophes.

After years of record losses, property insurers appear to be getting off lightly in 2006: catastrophe losses of only \$15bn will allow them to replenish their risk capital, depleted by record payments for hurricane damage in 2005 and 2004. Only three loss events in the billion-dollar range have made themselves felt: two tornados in the US and a typhoon in Japan. Among the past 20 years, 2006 has produced the third-lowest insured losses, after 1997 and 1988. This is attributable mainly to the quiet hurricane season in the US and surrounding countries. Unlike in previous years, Europe has also been spared expensive catastrophes. And finally, no major industrialised regions have been hit by earthquakes, and very expensive man-made disasters – such as aircraft crashes or large-scale fires – have been conspicuous by their absence.

The geographic distribution of the biggest loss events is reflected in the amounts of both the economic losses and the insured claims. As the typhoons and earthquakes in 2006 hit mainly newly industrialising countries where insured values are relatively low, the directly attributable financial losses were quite mild, at around \$40bn. Of these economic losses of \$40bn worldwide, only \$15bn, or less than one-third, were actually covered by insurance.

Later retirement and more private pensions essential for European pensions systems

To address Europe's pension problems, governments need to encourage later retirement and ensure the growth of private pensions, according to Aon Consulting.

The firm's 2006 *European Pensions Barometer Report* shows that the countries which have the most favourable position are those where the majority of people between 55 and 64 are contributing to the economy, not drawing from it. The other key factor in determining the relative position within Europe is the extent of the private funded pensions sector.

Because of Europe's ageing population there is a dilemma between the adequacy and affordability of state pensions, which are already the single biggest item of government expenditure in most EU countries. This can be mitigated by

the existence of substantial funded pensions.

A number of European countries have acted to extend private pension provision and this is a key reason behind their strong showing in the *Barometer* rankings. Countries like the UK, with a tradition of strong funded pensions through corporate defined benefit schemes, will see their position coming under pressure as companies withdraw from these schemes because of their high cost and the unfavourable regulatory environment.

Donald Duval, chief actuary at Aon Consulting UK, said: 'The UK government has recently announced plans to extend the provision of private pensions through personal accounts. However, these plans will not start to come into effect until 2012 and in the meantime company pension schemes will continue to decline. The UK state pension is currently the poorest in Europe, and that is unlikely to change in the near future. In combination, these factors mean that the UK is likely to slip further down the ranking of EU pensions systems in future.'

'So far as the EU as a whole is concerned, the influx of new member states to the EU and increase in cross-border migration will add to the challenges of providing adequate retirement income for citizens. Ultimately, reforms to pension systems need to target two key issues – lifting state retirement ages and increasing private pension provision.'

Green light for Britsaver

Millions of workers are to be encouraged to save for their future under new proposals published in December in the government's white paper, *Personal accounts: a new way to save*. Up to 10m people will be automatically enrolled into personal accounts, with a guaranteed employer contribution of at least 3%, kick-starting a new savings culture in the UK. The government expects that the millions of people who will save into personal accounts will contribute around £8bn annually in savings.

The secretary of state for work and pensions, John Hutton, said: 'Low charges are critical to ensuring that people build up the maximum pension fund from their savings. The government estimates that the long-term costs for personal accounts will be in line with those set out by the Pensions Commission of around 0.3% of funds under management, or even lower.'

The white paper also revealed that the government has decided the NPSS model proposed by the Pensions Commission is the best way to deliver personal accounts.

Andrew Power, insurance partner at Deloitte, commented on the potential impact on the life and pensions industry: 'The introduction of the

new personal accounts scheme will bring up to 8m new savers into the pension market, generating up to £8bn of new savings. The new scheme presents a number of opportunities to the insurance and investment management industries:

- ◆ absorbing new money into existing insurance-run pension schemes as some employers look to bring all employees into existing schemes rather than set up personal accounts;
- ◆ running personal account investment funds: many of the large insurers own some of the biggest UK investment management brands, which are well positioned to win the new fund management mandates;
- ◆ administering personal accounts: a small number of insurers will have the scale and infrastructure to run the administration contract likely to be put out for tender by the government;
- ◆ accessing new savers: the insurers will have the opportunity to develop a commercial relationship with a new segment of savers (notably women who only make up a third of current savers).

The proposals were welcomed by Stewart Ritchie, president of the Faculty of Actuaries: 'People are living longer and we all need to think about, and plan for, our future financial security. This paper is a constructive and necessary step towards achieving that outcome', he said.

However, Mr Ritchie also said that concerns outlined by the Actuarial Profession in its response to an earlier government white paper, *Security in Retirement – towards a new pensions system*, still need to be addressed. He said: 'We're still concerned that the provision of advice for members and potential members of personal accounts hasn't been addressed. For personal accounts to succeed it's vital that information products are developed in the context of financial capability strategies. We look forward to working with the government and the new delivery authority to get this right.'

Purple Book published

The Pension Protection Fund (PPF) and the Pensions Regulator (tPR) have published a report to help defined benefit schemes recognise and manage risk. The *Pensions Universe Risk Profile (Purple) Book* is based on data from 5,800 schemes and is designed to provide the industry with a credible information source.

The report will be published annually to enable tPR, PPF, employers, and scheme trustees to track changes in risk over a period of time.

One of the key objectives of the document is to provide an overview of the DB pension landscape, enabling risks surrounding scheme size, ➤

► industry-type, level of funding, insolvency, and asset allocation to be correlated and assessed effectively. In the future the book will contain crucial information on the PPF's operations such as the number and size of claims, the number benefiting from PPF payments, the scale of levy payments to the fund, and its assets and liabilities. The book can be found at:

www.thepensionsregulator.gov.uk/pdf/PurpleBook.pdf

Dutch pensions act

The Dutch parliament recently approved a new Pensions Act to replace the previous pensions law, which dates back to 1952. The new Act combines half a century of amendments and brings the legislation into line with EU directives.

Set to come into force this year, the Act requires pension schemes to value assets and liabilities at market rates. The Act introduces the mandatory 'Levensloop', a life-long savings scheme intended to finance periods of unpaid leave during the employment career, and also introduces the new FTK or financial assessment framework.

Various amendments covering transparency of the indexation element of pension schemes have also been accepted.

Scottish Re attracts new equity of \$600m

Scottish Re Group has announced that MassMutual Capital Partners LLC, a member of the MassMutual Financial Group, and affiliates of Cerberus Capital Management LP, a leading private investment firm, will each invest \$300m into the company, resulting in a total new equity investment of \$600m.

'This completes the process announced earlier this year to evaluate strategic alternatives, and will stabilise Scottish Re while providing long-term liquidity benefits', said Paul Goldean, chief executive officer of Scottish Re Group Limited. 'In addition to the financial strength afforded by MassMutual Capital and Cerberus as majority shareholders, these firms offer Scottish Re extraordinary insurance, operational, and investment expertise. We look forward to their input and guidance as we move aggressively towards our financial and business goals in the interest of returning value to all of our stakeholders.'

Successful IPO for new life company

Langholm Capital announces the successful IPO of Just Retirement (Holdings) plc, a specialist UK life assurance group focusing on the provision of

financial services to those at or in retirement.

The company has successfully raised an initial £50m through a placing of new shares on AIM valuing the company at £422m (up to over £600m as we went to press).

Just Retirement was established in April 2004 by Mike Fuller, the current chief executive, and certain other members of the senior management team, with £24.5m of financial backing from Langholm Capital. Since opening to new business in 2004, Just Retirement has developed key positions within the fast-growing enhanced annuity and equity release markets. The company reported total sales (audited) of £297.9m in the year to 30 June 2006, its second year of operation, while in the quarter ended 30 September 2006 the company made total sales (unaudited) of £143.1m, over three times the value made in the quarter ended 30 September 2005.

Just Retirement's strategy is to continue to enhance its product offering to take advantage of growth within its core markets and to gain competitive advantage through further development of new products, distribution channels, and its technology platform. The IPO proceeds will be used to provide capital to fund the future growth of the company and to expand the company's distribution capability.

Paternoster hires actuaries in India

Paternoster, a new life insurer, launched its India operations in December with a focus on recruiting the brightest graduates to the actuarial profession amid a global talent shortage. The company, which was set up to buy companies' final-salary pensions liabilities, will have 50 people in its Bombay office from the first quarter of this year working on policy pricing, valuations, and liability profiling.

This compares with eight actuaries working in London and reflects not only the cost arbitrage

offered by India – typically salaries are 30% to 40% lower than in Europe – but also the 'dearth' of intellectual capital in the UK.

'There is a global shortage of actuaries so it is not so much a question of relative pay grades', said Mark Wood, chief executive of Paternoster and former head of Prudential's UK life assurance business. 'The reason we were attracted to India is because we see a very high standard of education and a very high work ethic. This might represent a new concept in offshoring. Our model is not about call centres but highly skilled individuals.'

Even in India, which produces more than 2m English-speaking graduates a year, there are just 400 qualified actuaries in the country, compared with 40,000 worldwide. Efforts will therefore be put into training students under what Paternoster describes as its own 'actuarial academy'. Actuarial training can take up to six years. Viswanathan Balamurugan, also formerly of Prudential, will head the Indian company as its chief executive. Former Institute President Jeremy Goford, a non-executive director, said: 'We need a new mindset and that is what we think we will find here.'

Watsons expands to Pakistan and in the Netherlands

Watson Wyatt has extended its reach in Asia by teaming up with Pakistani firm Sidat Hyder. In what is becoming a busy year for deals, Watson Wyatt has announced the strategic alliance which it said would give it 'significant presence' in Pakistan, while giving Sidat Hyder access to its global network of experts.

The news came days after it was announced that Watson Wyatt is to buy its long-term partner in the Netherlands, Watson Wyatt Brans & Co. The two have worked in partnership since 1999, when the Netherlands office of Watson Wyatt merged with Dutch firm Brans & Co.

Controversy in India

The Indian Insurance Regulatory and Development Authority (IRDA) is reported to have dragged itself into a controversy with the appointment of R Kannan, senior adviser, Reserve Bank of India, and president, Actuarial Society of India, as its permanent member (actuary).

In a letter to the regulator and the finance ministry, a group of actuaries has pointed out that though there were five applicants for the post, none except Mr Kannan was called for an

interview. IRDA formally announced the appointment of Mr Kannan at the beginning of December. Apart from Mr Kannan, GN Agarwal, chief actuary, Life Insurance Corporation, who had also applied for the position, had been called for an interview. But he withdrew his candidature later. According to selection guidelines, any person who has either 15 years' experience in a life insurance company or has three years' experience as an appointed actuary can apply for the post.