

## From the world of general insurance

### Asbestos and pollution developments

A California appeals court ruled in January that the exposure to asbestos of each claimant against Kaiser Cement and Gypsum Corp constituted a separate occurrence under the terms of the company's coverage with Truck Insurance Exchange. This overturned a lower-court decision which indicated that there was one occurrence each year arising from Kaiser's decision to continue manufacturing asbestos products. The new decision is likely to adversely affect Kaiser (which will have to pay many more policy deductibles) and beneficially affect Truck and the London market (which provided excess coverage).

Also in January, the California Supreme Court published its ruling in relation to the Stringfellow waste site. This found that policyholders do not lose insurance coverage for a partially insured loss when they are unable to determine what proportion of the loss is covered by the insurance. In addition, the court found that groundwater contamination (which is not excluded by the watercourse exclusion in the commercial general liability policy) occurs when pollutants leak into the groundwater, not when they are deposited at the waste site.

A Florida appeals court has ruled that the recently introduced law stipulating medical criteria needed for asbestos claimants to be successful can apply to cases which have already been filed, on the basis that the law only laid down the procedures to be followed by claimants and did not affect their right to sue. The American Insurance Association, the US Chamber of Commerce and other insurer representatives welcomed the decision; they will be hoping that the same attitude will be taken in the other states where medical criteria apply.

In spite of the Michigan Circuit Court decision reported last month, a number of major policyholders of Royal & Sun Alliance (RSA) are

opposing the granting of regulatory approval for the acquisition of the insurer's US liabilities by Arrowpoint Capital Corp, on the grounds that the company is under-capitalised to take on such substantial potential liabilities. The relevant state regulator (Delaware) approved the sale in February but imposed conditions, which RSA believes may be sufficiently onerous as to scupper the deal.

The Federation of European Risk Management Associations has called on insurers to develop covers to enable businesses to protect themselves against new environmental liabilities which will arise after the European Environmental Liability Directive is signed into national law throughout the European Union; this must be done by 30 April. National governments will, under the new law, have the responsibility of suing polluters on behalf of the environment, which is effectively considered to be a legal entity.

### Finite risk reinsurance

Two more insurers have settled with US regulatory authorities in respect of investigations into their use of finite risk reinsurances. Bond insurer MBIA has paid \$75m, made up of \$50m to the Securities and Exchange Commission (SEC) for the benefit of investors, plus a further \$10m for investors and a \$15m fine to the New York attorney general's office. MBIA will restate its earnings for the years 1998 to 2004 to correct the inappropriate accounting for a finite risk policy which was purchased to hide a loss. In the other case, Renaissance Re paid \$15m to the SEC for a similar accounting anomaly – in this case, the finite risk contract purchased was designed to defer profits from 2001 to 2002 and 2003.

### Terrorism

While there appears to be a degree of unanimity between the Senate and the House of Representatives committees that they will extend the US federal terrorism insurance back-

stop before it expires at the end of 2007, there is a fairly fundamental disagreement as to whether the further extension should be permanent. Meanwhile, increasing commercial capacity, from both London and Bermuda, continues to flow into this class of business, and a new terrorism risk model has been launched by Room Solutions in London.

It has been proposed by the mayor of New York that WTC Captive, the insurer set up with federal funding following the terrorist attacks in 2001, to provide otherwise unavailable liability insurance coverage, especially to those cleaning up the World Trade Center site, should now be closed down, and its remaining funds merged into the Victim Compensation Fund.

### Financial Services Authority (FSA)

The FSA has announced that it is giving UK insurers greater freedom in how they present their individual capital assessments (ICAs), provided they comply with the guiding principles of the new regime. Following this, a group of insurer bodies has published 'A guide to the ICA process for insurers' incorporating the increased flexibility.

The UK government has published its report on the sale and regulation of travel insurance (see January/February issue). The major findings are that consumers may have been sold policies which do not meet their requirements, there is a lack of awareness of policy exclusions, and the problems are particularly acute where the policies are sold through an intermediary, such as a travel agent. The recommendations include the introduction of regulation of such policies through the FSA and the development of plain English policy wordings in collaboration with the insurance industry and the FSA.

The FSA budget for 2007/8 requires all FSA-regulated firms to pay fees increased by 16.2%. This is to fund consumer education, refur-

bishment of FSA offices, upgraded IT systems, and additional staff recruitment and remuneration.

### Protection & indemnity (P&I) business

The 20 February renewals in the P&I market saw a further (the eighth consecutive in most cases) increase in rates for shipowners, following the record high level of claims experienced in 2006 and concerns about the impact of the new Solvency II regime on the P&I clubs. The high level of 'large claims' activity in the market has resulted in between £300m and £350m being ceded by the individual clubs into the International Group pool which sits directly above the clubs' net retentions, thus affecting all International Group clubs to a material extent. Competition in the market is such that a significant proportion of members is changing clubs if faced with substantially increased premium demands. In addition, one club, the West of England, has made a supplementary call on members in relation to the 2006/7 year.

### Insurance reforms in Florida and other US states

Insurance industry sources have estimated that the reforms announced recently (see these columns last month) will reduce the worldwide property catastrophe reinsurance premiums in the commercial market by 15–20% and their profit margin by possibly 30%. While it is thought that the changes will lower household premium rates for coastal residents, there is a real risk that the state will eventually have to bear substantial losses if the state-run insurer of last resort (Citizens Property Insurance Corp) fails.

The Florida state governor, Charlie Crist, courted further animosity from the insurance industry by banning rate increases or refusal by insurers to renew policies for a three-month period up to the inception date of the new legislation.

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► Other states are understood to be considering whether they should institute reforms along similar lines. Of these, Mississippi is the first to put forward proposals which, in particular, would prevent insurers from providing automobile cover in the state if they did not also provide personal and commercial property insurance.

### Converium

An attempt by SCOR to acquire a controlling interest in Converium has been rejected by the board of the Swiss reinsurer. The bid followed SCOR's acquisition of 32.9% of the Converium shares on the open market. It is thought that further bids may be forthcoming.

### Large losses

Loss updates and related issues include:

■ **Hurricane Katrina (25–30 August 2005)** The State Farm settlement of 35,000 claims reported in these columns last month was subsequently rejected by the judge on the basis that he had insufficient information to confirm that it was an equitable solution of the issue. Discussions are understood to be con-

tinuing at the time of producing these notes (early March).

■ **Two ice storms across USA (mid-January)** These have now been estimated to cost insurers \$290m.

■ **Windstorm Kyrill, northern and central Europe (18 January)** The total estimated cost of this event has tended to increase from the average initial estimate of €5m reported in the last edition. Munich Re estimated the insured market loss at €5–7m, of which its share was around 10%. Allianz has estimated its proportion of the losses at around €350m.

■ **Spacecraft explosion on launch from California (31 January)** An NSS-8 craft blew up as a launch was being attempted from a sea platform at Long Beach. The spacecraft is understood to have been insured for \$256m, in addition to which the converted oil rig forming the platform was valued at \$240m and support vehicles at \$150m. The latter two sources of claim are understood to be placed in the marine market. The space loss is believed to be widely distributed in London and other markets.

■ **Outbreak of avian flu (H5N1 strain) in Suffolk (early February)** This affected a large poultry factory

farm owned by Bernard Matthews Ltd, and resulted in the culling of 160,000 turkeys. It is understood that no relevant insurance coverage for such outbreaks exists in the UK, although some compensation is payable by the government for the enforced slaughter of healthy birds. At the time of writing, no further spread of the disease (which appears to have been introduced to the UK from Hungary) has occurred.

■ **Floods in the Jakarta area of Indonesia (first half of February)** These were caused by monsoon rains, and resulted in the inundation of hundreds of thousands of homes, making an estimated 420,000 people homeless. Schools and businesses were also seriously affected and this was the main reason why insured losses were relatively high, at an estimated \$500m, with economic losses probably near to double this figure. A significant outbreak of water-borne disease, affecting around 200,000 people, followed the flood.

■ **Derailment of train in Cumbria (23 February)** This occurred when a London to Glasgow express hit faulty points at 95mph. Amazingly, only one fatality occurred, plus eight others were seriously injured. The

line was closed until mid-March, the remote location of the crash site having necessitated the building of a new road so that the wreckage could be removed. No insured loss estimate is to hand.

■ **Tornadoes in southern states of US (1 March)** These affected mainly Alabama, Georgia, and Missouri, resulting in an early estimate of at least 20 dead, eight of them while sheltering in a school in Enterprise, Alabama, which was demolished by the tornado. No insured loss estimates are yet available.

### 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](http://www.actuaries.org.uk/Display_Page.cgi?url=/general_insurance/gen_ins-curr-issues.html)

The latest edition contains sections on international issues, claims and legal issues, market news, solvency II and government and regulatory issues.

 DAVID HART

## 'Mother Nature, bless her heart, went on vacation'

The truth of Warren Buffett's above comment about 2006 is borne out by the news in the latest edition of *sigma* from Swiss Re that losses owing to natural catastrophes and man-made disasters were below the long-term trend in 2006. Of the \$48bn in catastrophe-related economic losses, \$15.9bn was covered by insurance. Insurers have modified their catastrophe simulation models, where appropriate, to bring them into line with higher expected damage – especially in the light of the record loss years 2004/05 and an increasingly volatile climate.

In 2006, natural catastrophes and man-made disasters claimed more than 31,000 human lives worldwide. Swiss Re's latest *sigma* study, 'Natural catastrophes and man-made disasters in 2006', recorded 349 catastrophes. Unlike in the

two previous years, natural catastrophes affected mainly developing countries where property values are low, resulting in comparatively light economic losses of \$48bn. Low insurance penetration in developing countries also meant that only one-third of these economic losses in 2006 was actually covered by insurance.

More on this at [www.swissre.com](http://www.swissre.com).

## Booming cross-border business from Ireland

Sales of cross-border life and pensions from companies based in Ireland exceeded €15bn in 2006, an increase of 25% on the year before, according to new figures compiled by actuarial consultants Life Strategies. The republic's cross-border life and pensions industry is now almost double the size of the domestic life and pensions market, which enjoys sales of €8bn.

Sales of cross-border life assurance products are also increasing at a faster rate than in the buoyant domestic life and pensions market, where new sales increased by 21% in 2006. Further growth is expected in 2007 following the news that large US insurance group MetLife had secured regulatory approval and began writing cross-border business from Ireland in January. Two companies, Standard Life International and Axa Life Europe, started writing cross-border business from the Ireland in 2006.

The 2006 performance, which Life Strategies described as 'impressive', followed 33% growth in 2005 and 43% growth in 2004. Sales in the sector have increased every year since 1995. Life Strategies director Jim Murphy said the financial regulator's principles-based (rather than rules-based) approach to regulation – as well as the low corporation tax rate – was proving attractive to overseas companies.

## Reliance Mutual to acquire Hearts of Oak

In what is the first deal of its kind with an insurance company taking over a friendly society with tax-exempt business, Reliance Mutual Insurance Society Ltd is to acquire Hearts of Oak Friendly Society Ltd via a transfer of engagements. This is the sixth Reliance Mutual acquisition since 2003 and involves £320m assets under management with 72,000 policies, including with-profits and unit-linked endowments, whole of life, personal pensions, and annuities.

Mark Goodale, chief executive of Reliance Mutual said: 'We are pleased to be able to offer the Hearts of Oak policyholders the benefit of our lower and more stable cost base, efficient and friendly service as well as the security of being part of a larger, well-capitalised insurance company. However, this is not just a financial deal for us. Being a mutual organisation, Reliance Mutual shares the ethos of friendly societies like Hearts of Oak. Our approach is also very much people-based with our priorities being committed to policyholders and making sure they are treated fairly.'

This landmark acquisition has become possible through a technical change in tax law proposed in the December 2006 Pre-Budget Statement. Friendly societies often contain portfolios of business which enjoy tax exemption and to date this tax treatment is lost if the friendly

society business transfers to an insurance company. The proposed change removes this artificial barrier and will enable insurance companies like Reliance Mutual to provide opportunities to friendly societies looking for partners (or support).

## JPMorgan launches longevity index

JPMorgan has launched its LifeMetrics Index, the only international index designed to benchmark and trade longevity risk. The LifeMetrics Index, developed with advisers Watson Wyatt in the UK and US and the Pensions Institute at Cass Business School, is part of an overall platform the investment bank has created called LifeMetrics, aimed at measuring and managing both longevity and mortality exposure.

JPMorgan has designed the LifeMetrics Index to be the leading industry index used to create securities, derivatives, and other structured products. LifeMetrics will enable pension plans to calibrate and hedge the risk associated with the longevity of their beneficiaries. The index incorporates historical and current statistics on mortality rates and life expectancy, across sexes, ages, and nationalities. Initially the index is available for the United States and England and Wales. JPMorgan intends to introduce similar indices for other countries in the coming

months. The index is calculated by an independent calculation agent and will be governed by an international advisory committee including experts from different organisations.

The potential for the development of a traded market rests on the standardisation of the measurement of longevity risk associated with pension funds and the mortality risk facing life insurers. Further information on LifeMetrics is available at [www.jpmorgan.com/lifemetrics](http://www.jpmorgan.com/lifemetrics).

## PPF levy concerns

Nearly two-thirds of scheme managers believe proposals to increase Pension Protection Fund (PPF) levy payments for the 2007–2008 year fail to strike the right balance between protecting weaker schemes and not penalising stronger schemes, an exclusive survey by *Professional Pensions* (PP) last month revealed.

Some 63% of PP's panel of 100 top scheme managers said that an increase in levies would not achieve what the PPF intended. As one manager explained: 'Increasing the levy will mean penalising all – and end up finishing final salary schemes.' Other managers agreed – and warned that, as the investment strategy is not taken into account, the balance cannot be right.

The survey followed the PPF's earlier announcement that it hoped to collect £675m from schemes in 2007–2008 in a bid to shore up its £343m deficit. Last year it collected only £310m despite a target of almost twice that figure. PPF chief executive Partha Dasgupta said it was important it recouped the funds using a 'measured approach'.

## The benefit of advice

At a conference in March, Resolution Foundation published a report summarising the predicted impacts on the financial services industry of improved financial decision-making, driven by increased access to financial advice, by low to median earners. It is based on economic modelling carried out for the Resolution Foundation by Deloitte.

The findings show how the financial services industry will benefit from consumers having increased access to financial advice. Although the impact will vary by product, the overall effect on the industry will be positive. The results are based on 10% of the Resolution Foundation's target group acting on advice. Within four years of this being the case:

- ◆ new contributions to medium-term savings plans would increase by £1.5bn net;
- ◆ pensions premiums would increase by £560m;
- ◆ annuity premiums would increase by £58m (but would increase by £300m by 2060 as more people retire with larger pensions pots);

- ◆ life assurance premiums would increase by £225m;
- ◆ young lower earners would have credit card balances averaging £800 – but this figure would be £1,900 without advice;
- ◆ credit card debt would fall from £2.5bn to £830m;
- ◆ unsecured debts would fall by £2.2bn;
- ◆ mortgages and secured debt would remain relatively stable.

The Resolution Foundation believes that the overall effect will be beneficial for the majority of the industry – particularly when wider benefits of more financially capable consumers are taken into account. The Resolution Foundation has suggested that both the government and the financial services industry should contribute to the funding of a national generic financial advice resource. It has argued this on the basis that the industry would benefit not just directly from better financial decision-making, but also that more financially capable consumers would lead to a healthier, more sustainable financial services market.

## Current conventional wisdom will never provide enough

We thought the following letter of 8 March to the editor of the *Financial Times* from Mark Wood of Paternoster deserved to be seen by all actuaries:

'Sir, it would seem that the debate on future longevity has become unnecessarily polarised. Some actuaries have been slow to pick up on trends and some are still in denial regarding the extent of likely future improvements.

'Life expectancy at retirement has for some time now been improving at a more rapid rate than at any time in our history. We have seen the same improvement over the past ten years as in the previous 150.

'Fundamentally, given what we know about life expectancy today, the issue is that the current conventional wisdom for pension and insurance company reserving, the so-called medium cohort basis, will never be enough to provide the promised pensions.'