CPCU SOCIETY
INSURING YOUR SUCCESS

The Specialist ESSL

Volume 22 Number 1 February 2008

Chairman's Corner

by Mark C. Brockmeier, CPCU, ARe

Mark C. Brockmeier, CPCU, ARe, is a senior principal for SAP's Value Engineering Group, assisting insurance companies worldwide in building business cases for strategic investments in process and technology tools. He has more than 20 years in the insurance industry and has worked for insurers, reinsurers, TPAs, and self-insurers prior to his current position. Brockmeier received his CPCU designation in 1993, and is a graduate of Boston University's Masters of Insurance Management program.

A warm welcome to the members of the E/S/SL Interest Group as I assume the duties of chairman over the next two years. My thanks to **Lynn D. Goodwin, CPCU, CIC, ARM,** and **James A. Roe, CPCU** for their service last year during a time of great change in the CPCU Society, its membership, and structure. Those topics were the focus of much discussion during the CPCU Society's Annual Meeting and Seminars in Honolulu, Hawaii in September 2007. The E/S/SL Interest Group Committee met at the beautiful Luana Hills Golf Club and enjoyed the beauty of Hawaii while talking about the business of the interest group . . . powerful incentive indeed to become more involved in the interest groups! We need your participation and ideas. I welcome new committee members **David O. Bisbee, CPCU,** and **Richard V. Rupp, CPCU;** and the reappointment of **James A. Roe, CPCU,** who has contributed to and served the CPCU Society for many years. I would like to thank **Dennis R. Childs, CPCU,** who assumes the duties of editor of *The Specialist*. Finally, please check out the interest group web site for fun photos from Hawaii.

If you have not attended an Annual Meeting since earning your designation, I encourage you to do so and put it in your plans for this year. There were fabulous educational sessions put on by the CPCU Society National Leadership Institute (now known as the CPCU Society Center for Leadership) prior to the conference, and compelling and interesting seminars put on by many CPCU Society interest groups. Our own E/S/SL Interest Group developed a seminar driven by the Lexington Insurance Group, "Surfing the Waves: Opportunities and Challenges in Today's Surplus Lines Market." Thanks go out to **Meredith Mangan, CPCU,** the associate general counsel for Lexington. She organized an interactive and interesting discussion panel that included topics on market conditions, regulatory environment, the impact of natural disasters, pricing and market conditions, and the outlook for surplus lines (which is good, by the way . . . if you want all the details and to hear all the presentations, the $99 CD on the Society' web site is an excellent value, allowing you to learn from both the Leadership and Property/Casualty tracks).

There were some exciting announcements at the Annual Meeting. Many of you have probably attended, seen, or heard of "webinars," which are presentations that are done over the Internet by an organization to many people in remote locations. These are done real time, and can be recorded for those unable to attend to view later, or to be seen again for review of difficult or new material. These kinds of meetings can literally have 1,000 users all seeing the same presentation, with the ability to dial in to hear the speaker, and ask questions via a web log during the presentation, which are then answered at the end. I am pleased to tell you that the Society

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is piloting this capability for 2008 for use by interest groups to help spread our professional education and message. Imagine if we could do sessions such as "Surfing the Waves" on a monthly basis, with member companies developing the content and presenting seminars through the CPCU Society! It's a great way to raise the awareness of who we are and what we do, as well as providing service to our members who wish to educate their constituents on various topics. I encourage each of you to think how your company, agency, or consultancy could take advantage of this new capability, and what topics you might want to put on and what panels of industry professionals you might assemble. Please submit your suggestions to me, **Dennis R. Childs, CPCU**, or any of the members of the E/S/SL Interest Group Committee. Our goal is to produce at least one webinar in 2008, in addition to producing an E/S/SL seminar at the Annual Meeting and Seminars in Philadelphia.

More changes are being discussed but are not yet final, so I'll save comment on those until the next newsletter. I wish every member a productive 2008, and look forward to your suggestions on how to improve the interest group, write articles, conduct webinars, or otherwise contribute to your own professionalism by enhancing the professionalism of others. There is no better reward than to "Pay It Forward." ■

Editor's Corner: View from the Crow's Nest

by Dennis R. Childs, CPCU, ARM, AMIM, ARe, ASLI

■ **Dennis R. Childs, CPCU, ARM, AMIM, ARe, ASLI,** is assistant vice president of Liberty Mutual Insurance, in Fairfield, Ohio.

Hello everyone and welcome to this edition of *The Specialist*. I am your new newsletter editor (actually I think I was appointed in absentia, but that is another story). I also would like to welcome you to our interest group and to urge you to "tell it like it is." We want you to actively participate and we can only do that if we know what is on your mind.

Speaking of being on our mind . . . in case you missed our E/S/SL co-sponsored session sponsored by Lexington Insurance, you really missed a treat. It was almost worth the price of admittance just to hear **Bernard J. Daenzer, J.D., CPCU,** speak about his experiences from years in the industry. I can still recall him explaining overhearing a London underwriter comment that, "I would write anything for 2 percent." The only problem is in this market to be successful in writing the risk, the rate would probably have to be 1.5 percent!

Seriously, the E/S/SL session was very well-attended and very stimulating and thought-provoking. As an example, **Bill Newton** of Risk Placement Services talked about the common misconceptions of the excess and surplus lines arena:

1. **E&S carriers are not as financially strong as the admitted market.** That is a myth as the leading E&S carriers are actually subsidiaries of large admitted carriers (as is the case with Lexington/AIG). The solvency requirements are actually the same.
2. **E&S carriers lack the protection provided by the various state guarantee funds.** True, but the guarantee funds may not provide full protection for a claim against an insolvent company either as there may be statutory limits of anywhere from $150,000 to $300,000 per claim.
3. **E&S markets are not regulated.** Untrue as E&S carriers must be admitted in their domiciliary state. Moreover, much of the oversight falls on the E&S broker to manage the financial stability of the carriers they represent.
4. **The premium must be higher for an E&S transaction since the commission is usually higher.** Actually the "wholesale" process is a very efficient use of capital serving to supplement, not to transplant the admitted market.
5. **E&S coverage is generally more restrictive than the admitted market.** Untrue again as the E&S market serves as an incubator for new coverages made easier by the freedom of rate and form. Remember when employment practices or environmental liability was available only in the E&S market?

Lastly, it is important to note that according to a recent Conning & Company study, the E&S market has grown at a faster pace then the admitted market over the past 10 years (19.5 percent annual rate of growth for the E&S market versus 7.6 percent for the admitted market) and has been more profitable (104.4 percent calendar year combined ratio for the 10-year period for the E&S market versus 107.1 percent for the same period for the admitted market).

I encourage you once again to tell us what is on your mind. We welcome your ideas, your articles, your comments, and your feedback in general. Contact information for each member of the E/S/SL Interest Group Committee is shown on page 8.

Looking forward to serving you in the new year! ■

The Future Used To Be Certain

A Summary of Key 2007 Federal Legislation and Possible Impacts on Future Property and Casualty Operations

by Jody M. Pucel, J.D.

Jody M. Pucel, J.D., is a government relations and regulatory compliance attorney in Seattle, Washington. She received her law degree from DePaul University in Chicago, Illinois. After graduation, she worked as a law clerk for the Illinois Appellate Court before entering private practice in Chicago. She then joined the Corporate Legal Department of the Safeco Insurance Companies in 1992, most recently as senior legislative counsel. Her property and casualty insurance background includes expertise in legislative strategy and analysis; environmental issues; personal property insurance; commercial insurance; intellectual property; e-commerce; claims management; and regulatory compliance.

Author's note: The views expressed in this article are the personal views of the author alone and should not be considered in any way to represent the views of any entity.

Property and casualty insurers have enjoyed some certainty that they could expect the usual legislative battles each year: opposing credit ban bills and auto body shop anti-steering initiatives while pursuing the often elusive tort reform measures and commercial lines deregulation legislation. The results of these battles, wins in some states and defeats in others, were generally balanced so that there was minimal disruption in overall market conditions, at least from a multi-state point of view. And federal legislation specific to the property and casualty industry was usually absent since there is no federal agency charged with regulation or oversight of the property and casualty insurance industry as a whole, other than through implementation of the Terrorism Risk Insurance Act of 2002 (TRIA). The pace and regularity with which state legislative agendas and results progressed and the limited federal legislative issues gave insurers some certainty about future operating environments. This future, however, is no longer so certain.

The 2007 Congressional legislative session, in contrast to prior federal legislative sessions, not only included no less than 14 specific property and casualty bills, but the insurance industry actively supported some of the bills. This support was in stark contrast to past years when the industry resisted federal legislation, preferring instead to rely on state laws and state oversight to manage the business of insurance. Pressure from global competition, improved technology and unprecedented catastrophic losses (both natural and man-made) are changing the property and casualty insurance marketplace, prompting the property and casualty industry to pursue limited federal involvement.

Analysis of individual pending federal legislation indicates that some bills promote development of a free market while others might result in more government interference, making it easy to conclude that the industry should support the former and oppose the latter, as indeed the industry is doing. There is no assurance, however, that only favorable legislation will be enacted. Rather, it is possible that a combination of bills or pieces of different bills could be enacted, resulting in fragmented federal laws that not only might be dramatically different from current state regulations but would impact the industry nationwide, rather than in just a limited geographic area.

Legislation actively supported by the property and casualty insurance industry in 2007 included the Terrorism Risk Insurance Revision and Extension Act, which creates a federal financial backstop for commercial losses arising from terrorism events, allowing insurers to spread these risks across state markets and share the losses with the federal government; the Optional Federal Charter, which creates one license allowing insurers to do business in all states and opens the door to more foreign competition; and the Nonadmitted and Reinsurance Reform Act to simplify this market. Individually, these bills are expected to foster development of a healthier, competitive national market than now exists under the current multi-state regulatory structure.

On the other hand, there were also bills pending that would allow direct federal involvement in the insurance market, raising concerns about unnecessary federal interference. The bills giving rise to these concerns include: the Multiple

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Peril Insurance Act, which would amend the National Flood Insurance Program to include wind losses; creation of a federal commission on natural catastrophes; and McCarran-Ferguson Anti-Trust repeal bills. The industry has expressed concerns that the multi-peril and catastrophe bills will allow the federal government to write property coverage in markets considered viable by insurance companies and in direct competition with the private market. The proposed repeal of the insurance anti-trust exemption raises concerns about costly and extended federal litigation challenging established industry practices, possibly disrupting the business of insurance.

As the 2007 federal Congressional session came to a close, Congress did enact the TRIA Extension, which was signed by the President at the end of December 2007. This bill reauthorizes the existing TRIA law for seven additional years without adding nuclear, biological, chemical, or radiological events into the current federal backstop program.

As we head into 2008, there is a distinct possibility that Congress will enact legislation creating a federal commission to study the property insurance market as it relates to natural catastrophes. On the other hand, it does not appear likely that either the Optional Federal Charter or expansion of the national flood program to include wind will pass in 2008, although a significant hurricane or other catastrophic event could change this outlook. Likewise, there has been no activity on the McCarran repeal legislation since April 2007 so it appears there is insufficient support to pass the bill.

Whether federal oversight of property markets can be limited to terrorism is not certain. Nor is it certain whether Congress fully appreciates the benefits of a limited federal role in regulating insurers under the Optional Federal Charter. What is certain is that the 2007 Congressional session did not include the usual legislative battles. And if this Congressional session is any indication, efforts to expand federal involvement will only continue in 2008 and beyond, quite possibly resulting in federal regulation of a complex industry facing increased global competition; and with an obsolete, 50-state patchwork of state regulation as the only basis upon which to develop national laws, making for an uncertain operating environment. As the industry contemplates its future, Congress could provide the property and casualty industry with some certainty by indicating an understanding that there is ultimately one U.S. property and casualty insurance market; the future operating environment for this market not only depends on which individual bills are enacted but also on how all the bills enacted fit together in the aggregate; and, unlike a single state law or regulation that impacts operations in only that state, a single federal law will impact all operations immediately and on a nationwide basis.

Details of Key 2007 Property and Casualty Federal Legislation

1. **Terrorism Risk Insurance Revision and Extension Act (TRIREA), HR 2761**

   Signed by the President on December 27, 2007.

   Extends existing TRIA law for seven years, through December 31, 2014. Applies to losses due to domestic or foreign terrorism events. Is applicable to only specified commercial products. Insurers are required to make coverage available for these losses and to retain a portion of risk through program deductibles. The insurers and federal government also share in the losses above the deductible, up to $100 billion.

   Federal involvement is limited to providing financial certainty to insureds and insurers for losses due to terrorism events, thereby creating a market in which insurers can compete in terms of price and coverage while sharing in the risk with the federal government.

2. **Optional Federal Charter (National Insurance Act), S.40, HR.3200**

   These companion bills would establish a dual regulatory structure, similar to the banking and securities structure, by creating a separate federal regulatory system for insurers choosing to operate under a federal license. This federal system is designed to pre-empt state regulation other than state unclaimed property and escheat laws, tax laws, assigned risk plans, mandatory residual market mechanisms, compulsory coverage requirements for workers compensation or motor vehicle insurance, participation in advisory or statistical organizations, and participation in a workers compensation administration mechanism. The federal regulator would have authority to oversee financial standards; product maintenance; unfair practices in sales, marketing, and claims handling; acquisitions and mergers; licensing; holding company issues; and insolvencies.

A federal regulatory system is expected to result in a competitive market free of artificial rate and form restrictions as well as a consistent regulatory environment in which to do business in all 50 states. By providing for a single regulatory system, the OFC would remove some of the more onerous trade barriers faced by offshore insurers wanting to do business in the United States.

3. Nonadmitted and Reinsurance Reform Act of 2007, HR 1065, S 929

Originally introduced in 2006 and passed by the House, this re-introduced version would provide a uniform system of surplus lines premium taxation, elimination of duplicative compliance requirements for multi-state surplus lines transactions, and direct access to the surplus lines market for large commercial insurance buyers. The bill would also allow ceding insurers and reinsurers to resolve disputes pursuant to contractual arbitration clauses.

This bill would simplify and streamline the often conflicting regulations among the 50 states and bring more certainty to the insurance market.

4. Multi-Peril Insurance Act, HR 3121

This bill purports to solve the perceived problem that wind coverage is unavailable and/or unaffordable in hurricane-prone areas by expanding the National Flood Insurance Program to provide coverage for hurricane-related property losses.

In effect, the NFIP would not only directly compete with the insurance industry in this market segment but it would have a competitive advantage over the industry by being able to offer the coverage for lower premiums than what the private market could charge under existing state regulations.

5. Federal Commission on Natural Catastrophe Risk Management and Insurance, S. 292, and HR 537

The proposed Commission would study the affordability and availability of property insurance in the private market, focusing on the need for federal management of natural catastrophe risks and insurance.

The industry position is that a healthy, competitive private market will result in available and affordable coverage. Therefore, federal management of the risk, including rates and coverage, equates to unnecessary interference in the private market and in the business of insurance would obstruct parallel efforts to enact true market reform legislation.

6. The Insurance Industry Competition Act of 2007, S.618, HR 1081

These bills would amend the McCarran-Ferguson Act by repealing the insurance industry's exemption from federal anti-trust laws. Currently, the exemption requires federal anti-trust enforcement agencies to refrain from enforcing anti-trust laws against the insurance industry's collective activities, such as those involving sharing data for rate development and using standardized forms, but only to the extent that the collective activity is subject to adequate state regulation.

Repealing the exemption would give the FTC "gap-filling" authority to regulate insurance companies where state laws do not exist or are deemed insufficient, and federal anti-trust laws would apply to all insurance practices. Since the FTC would have to promulgate regulations, established state-sanctioned activities would continue to operate but would now be subject to legal challenges under the "state action" doctrine under which state laws are reviewed to determine whether they adequately ensure an anti-competitive market. Also, insurers' collective activities would be subject to direct anti-trust litigation. It would likely take years for the federal government to implement gap-filling regulations and for anti-trust litigation to resolve into settled business parameters. In the interim, state regulatory schemes would be under judicial scrutiny, insurer collective activities would be subject to federal anti-trust litigation, and litigation and compliance expenses would increase, resulting in an uncertain market in which to do business. ■

A Harbinger of a Long Soft Market Is Spotted in Tempe

by George Williams, CPCU

George Williams, CPCU, will retire in February 2008 as editor and assistant to the publisher of *American Agent & Broker.*

Editor's note: This article first appeared in *American Agent & Broker* magazine in November 2007, and is reprinted with the approval of *American Agent & Broker* magazine.

As a robin or crocus is often regarded as a sign of spring, so is the appearance of a reinsurance broker promoting "reverse flow" business a sure indication of a wicked soft market. Actually, a more apt comparison might be to a groundhog's retreat from its shadow on Feb. 2. When reinsurance brokers talk up reverse-flow options, you can kiss good-bye any illusions you may harbor for an early end to a soft market.

Reverse-flow transactions mainly affect program business but have implications for anyone interested in the underwriting cycle. Typically, program administrators obtain their coverage from primary insurers, which then lay off part of the risk with reinsurers. But when the market is particularly soft and overcapitalized, primary carriers don't cede as much business. In response, reinsurers may try to get their share by going directly to program administrators or MGAs, urging them to consider a "structured" program, in which a "fronting" carrier issues policies for the program administrator, then cedes 100% of the premiums to a reinsurer.

At the annual convention of the Target Markets Program Administrators Association, which was held in Tempe, Ariz., I spotted a reverse-flow broker—the first one I'd seen since the 1990s, well before Target Markets was even formed—in the form of Dean Carberry, chief executive officer of Rattner Mackenzie (Bermuda) Ltd. During a break-out session he conducted, he gave his take on where the market stands today, more than three years after the last gasp of the hard market. Among its characteristics are:

- **Enormous capacity:** The last soft market came to a screeching halt in 2001, Carberry said, when poor underwriting results and the shock of 9/11 produced an industry-wide combined ratio of nearly 116. Then, as a market correction set in and rates for many risks skyrocketed, capacity flooded the market—and then kept coming despite the hurricane-related losses of 2004 and 2005 (which, of course, produced corrections of their own). All that capacity has increased industry surplus, the capital that supports underwriting. Surplus "is at an all-time high of $512 billion," Carberry said. "That's just incredible." As Bermuda markets and other players increase their presence in the U.S. market, Carberry said surplus could top $600 billion by year end.
- **Record profitability:** The insurance industry's combined ratio plunged to 92.5 in 2006—meaning it made a 7.5% profit before interest income—and 2007 is shaping up to be almost as strong. "The results that we're seeing at the moment are the best ever … for combined ratios since 1949," Carberry said. "Not only are they the best results, but they are the longest-sustained (profitable) results."
- **Anemic growth:** "The market's not getting any bigger," Carberrry said. "In fact, it's possibly (shrinking) because of rate reductions and increases in self-insured retentions."

Carberry said these and other factors point to a soft market that, while perhaps not as deep and long-lasting (12 years) as the last one, likely will hang on for another four to seven years. Interest rates will be one key determinant, he said. Although they've dropped recently, Carberry said he believes they are likely to rise as the government finds it has to borrow more to cover the cost of such programs as Social Security, which baby boomers will begin tapping next year. Higher rates would enable insurers to increase investment income, which would prolong the soft market, he said.

In today's extremely competitive market, program administrators can find plenty of insurers interested in partnering with them, Carberry said. (Indeed, the Target Markets attendance list included several carriers who were new applicants for association membership.) Insurers are now more willing to accept smaller programs, delegate authority and make other concessions, he said.

"Finally, reinsurers are ready to take 100% quota shares," Carberry said. "Normally reinsurers would only come into the market if the insurance carrier was taking a big retention on the risk. They're bypassing all that now, going directly to the MGA (or program administrator) and saying, 'Get me a front carrier. I'll take care of everything after that.'" Such arrangements can have advantages for program administrators, Carberry said, including a significant share in underwriting profit.

As the market continues to soften, Carberry predicted there will be considerable consolidation among carriers and program administrators. "Size counts, for sure," he said. "The bigger your program, the most likely you are going to survive." In coming years, he said, as profits deteriorate under relentless rate cutting, $5 million programs with 65% loss ratios will be doomed. "If you don't have a significant volume, there's no investment income," he said. "You won't stand a chance."

Meanwhile, the soft market won't really last forever, the way winter froze in place for Bill Murray in "Groundhog Day." It will only seem that long.

At the October 2007 convention of the National Association of Professional Surplus Lines Offices, which was held in New Orleans, an emotional highlight was a brief address by Louisiana Insurance Commissioner James J. Donelon, who said the city and state are back, after "a horrific time." He said the participation of E&S carriers in the Louisiana insurance market will be vital to its recovery and offered "Three L's" as incentives: legislative efforts (e.g., a $100 million program that provides matching funds to qualified insurers committing capacity to the state), levees ($1.5 billion in federal funds spent so far to strengthen levees, with more on the way), and litigation (or rather, the potential for less of it, thanks to the state's Napoleonic code, which Donelon said permits punitive damages only for drunk driving and child abuse). Here's hoping that insurers take the commissioner up on his invitation. ■

CPCU Travel Program

by Richard A. Vanderbosch, CPCU, CLU, AIS

■ **Richard A. Vanderbosch, CPCU, CLU, AIS,** graduated from Western Michigan University before embarking on a 36-year career with State Farm Insurance. When he retired in January 1999, he was director of data management services at corporate headquarters. Vanderbosch lists among his greatest personal achievements being named a CPCU Society Standard Setter in October 1998. Following a stint as a leader of the CPCU Society's Central Illinois Chapter, and prior to joining the Senior Resource Interest Group Committee, he chaired the national Intra-Industry and Continuing Education Committees.

What in the world is the CPCU Travel Program? Have you ever heard about it? Are you familiar with how it works and what types of trips are offered? Many CPCUs, who are busy establishing their careers, are not really aware of the program or have not taken the time to find out more about it. If you happen to be one of these people, read on for a brief synopsis of what it's all about.

The CPCU Travel Program, sponsored by the Senior Resource Interest Group, was first established in 2004 to provide an opportunity for CPCUs like yourselves to travel and to associate with each other in a relaxed, casual setting. It was designed to bring CPCU professionals of all levels, ages, and disciplines together for exciting travel adventures around the world. Family members and friends are also welcome to participate. Each year, the most popular destinations are identified and evaluated, and one is selected for the subsequent year's trip. The selection is based on the location, the length of the trip (one to two weeks max), and the cost. The announcement is then made to all CPCU Society members in the fall, and flyers are prepared for distribution at the Annual Meeting and Seminars. In 2005 we traveled to the Great Rivers of Europe; in 2006 we did a Canadian Rail Adventure, and the 2007 tour "Storybook Landscapes Along the Rhine," was a nine-day river cruise from Amsterdam to Frankfurt—the trip sold out. The 2008 Danube River trip "The Old World—Prague & Vienna" will travel through Hungary, Slovakia, and Austria.

For more information, feel free to call me at (970) 663-3357 or e-mail me at rbosch@aol.com. ■

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Global Warming and You: What Every Insurance Professional Should Know about Climate Change

by William F. Stewart

William F. Stewart practices in the West Conshohocken office of Cozen O'Connor. He concentrates his practice in insurance coverage, fraud defense, bad-faith defense, environmental, toxic tort, and mold coverage defense. Stewart is a member of the Pennsylvania, Philadelphia, Montgomery County, and Camden County Bar Associations. He is a frequent contributor to *Business Insurance, Best's Insurance*, and *Mealey's*. Stewart is an arbitrator for the U.S. District Court for the Eastern District of Pennsylvania, and for the Philadelphia Court of Common Pleas and the Montgomery Court of Common Pleas. In 2005, he was selected by the Pennsylvania Supreme Court to serve on the state rules committee. Stewart earned his law degree at the University of Notre Dame, where he graduated cum laude. He is admitted to practice in Pennsylvania and New Jersey, and has practiced pro hac vice in more than 10 U.S. states and territories.

Editor's note: Global warming has been the topic of much angst by environmental groups, governments, and climatologists; and has been studied extensively by insurers in recent years in light of severe weather events that have been attributed to its effects. But what is it, really? For those of us in E/S/SL, can we develop products and protections that "partner" with these new environmental realities of drought, rising sea levels, and warming climate? Food for thought indeed, and perhaps the genesis of a joint seminar with our CPCU Society Reinsurance Interest Group brethren. Speakers, anyone?

The good news is, if you are reading this article, you are employed in a growth industry. The overwhelming weight of evidence suggests that global warming will dramatically increase both the frequency and severity of property and liability claims. The bad news? Unfortunately, in the coming decades, our planet will experience some combination of unprecedented hurricanes, wildfires, floods, hail, heat waves, and drought. This article endeavors to provide practical commentary on what is happening, how it will impact insurers, and what the insurance industry can do in response.

Isn't Global Warming Just Scientific Conjecture?

In the 1890s, a Swedish scientist named Svante Arrhanius made a novel prediction about climate change. He opined that, if humans continued to release high levels of carbon dioxide into the air, it would trap heat within the atmosphere and increase temperatures on the planet's surface. Although Arrhanius' theory was rejected in his own time, the "greenhouse effect" is almost universally accepted by contemporary environmentalists. Indeed, according to an April 6, 2007, article published by the *Insurance Journal:* "no serious scientist today disputes the existence of global warming, even though its potential impact remains the subject of continued analysis." In February 2007, the United Nation's Intergovernmental Panel on Climate Change (IPCC) issued a report stating: (1) "warming of the climate system is unequivocal"; and (2) it was very likely that human activity since 1750 has overloaded the atmosphere with carbon dioxide—which in turn has resulted in the retention of solar heat.

In 1750, atmospheric levels of CO_2 were 280 parts per million (ppm), by 1960 CO_2 levels had risen to 330 ppm, and now CO_2 levels are 380 ppm (which is higher than at any time in the last 650,000 years). To make matters worse, the IPCC has predicted that atmospheric carbon dioxide levels could reach 450 to 550 ppm by 2050. Correspondingly, 11 of the 12 warmest years in history have occurred since 1995. Thus, the debate is no longer whether global warming is occurring, but whether we are headed toward some sort of abrupt and cataclysmic change to our environment.

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Global Warming and You: What Every Insurance Professional Should Know about Climate Change

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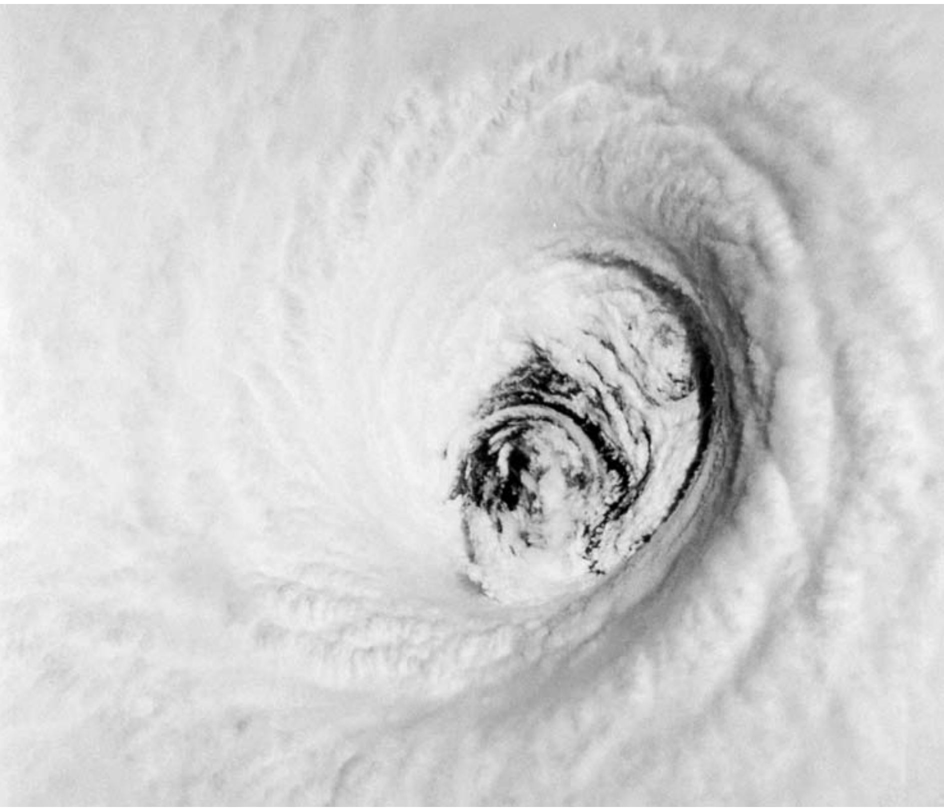
How Will Global Warming Impact the Insurance Industry?

The U.S. Environmental Protection Agency's web site states: "[w]hile the effects of climate change will impact every segment of the business community, the insurance industry is especially at risk." At an April 19, 2007, international conference on Climate Change Regulations and Policy, the insurance industry was referred to as "the big canary in the coal mine"—because insurers will be the first to feel the impact of an increase in the frequency and/or severity of natural disasters.

While it is rarely possible to conclude that any particular weather-related loss is the result of global warming, there has been an alarming increase in both the number and extent of catastrophe (CAT) claims. According to the EPA, "there were four times as many natural catastrophes in the 1990s as there were three decades ago." Seven of the 10 most expensive hurricanes in U.S. history (Katrina, Charlie, Rita, Wilma, Jeanne, Ivan, and Frances) occurred during the 14-month period between August 2004 and October 2005. The 2004 and 2005 hurricane seasons resulted in $75 billion in insurance payments, and CAT losses during that period equated to 12 percent of overall property insurance premium—which is more than three times the historical average.

One of the most alarming aspects of global warming is rising sea levels. An April 6, 2007, IPCC report stated, with "medium confidence," that "sea-level rise and human development are together contributing to . . . coastal flooding in many areas." In Florida, sea levels have risen six to eight inches over the last 100 years because of melting Arctic ice, and an accelerated upsurge is predicted because even a one-degree increase in temperature would result in massive melting of the Greenland ice cap. While there are no reliable models to predict how an anticipated two to three degree temperature increase would affect the ice caps, there is a growing view that low-lying coastal cities like Miami may be in grave risk before the end of the century.[1]



While most of the focus to date has been on coastal areas, the effects of global warming will be universal. Tim Wagner, the director of the Nebraska Department of Insurance, recently offered the following assessment: "After New Orleans, it's becoming clearer that we are experiencing more frequent and more powerful weather events that pose huge challenges for the insurance industry. . . . [but] this is both a coastal issue and a heartland issue . . . we're seeing all kinds of extreme weather in the Great Plains, including drought, tornadoes, brushfires and severe hailstorms."

How Can the Insurance Industry Most Effectively Respond to Climate Change?

Scientists broadly characterize responses to global warming into two main categories: mitigation and adaptation. Mitigation involves attempts to reduce greenhouse emissions through conservation, alternative energy usage, and underground carbon storage. The reality, however, is that while mitigation efforts are imperative, they are unlikely to eliminate the problem. By the end of 2007, China will surpass the United States as the nation with the highest level of carbon dioxide emissions. For the present and foreseeable future, China's first priority will be the elimination of poverty, and, thus, it has consistently refused efforts to reduce or capture its emissions. Moreover, because CO_2 remains in the atmosphere for decades, and because the oceans retain heat for centuries, temperatures would continue to rise even if we could curtail the global production of greenhouse gases.

Adaptation involves the response of individuals, businesses, and communities to cope with the inevitable consequences of climate change. Examples of adaptation range from the conventional construction of levies to the futuristic "seeding" of clouds with chemicals to produce rain when and where it is needed.

Insurance professionals will be called upon to employ strategies that include both adaptation and mitigation measures. Three common examples of adaptation are pricing adjustments, risk sharing with insureds (e.g., increased windstorm deductibles), and cancellation. In February 2006, Allstate announced plans to stop offering property coverage in several counties along the Chesapeake Bay. Many property insurers have ceased writing business in Louisiana and Florida, and those still issuing policies have raised rates significantly. Another example of adaptation involves a proposed National Catastrophic Fund, which would aid insurers in the event of major climatic disasters—similar in certain respects to both the Terrorism Reinsurance Act of 2002 and the National Flood Insurance Program.

In addition to adaptive measures, the insurance industry is in a unique position to mitigate climate change. The EPA has asked insurers to address global warming by: (1) educating policyholders about the financial risks associated with climate change; (2) supporting stricter building codes to minimize the impact of severe weather; and (3) promoting energy efficiency and renewables to cut greenhouse gases. And indeed, despite its unfairly maligned reputation, the insurance industry has been a leader in combating CO_2 emissions. Travelers offers a 10 percent auto insurance discount to the owners of hybrid cars. Firemans's Fund not only reduces premiums for environmentally friendly buildings, but also encourages its insureds to use "green" products to repair losses. In April 2007, AIG became the twelfth company, and the first insurer, to join the United States Climate Action Partnership (USCAP)—which supports a number of immediate mitigation measures including a nationwide limit on carbon dioxide omissions. Swiss Re has invested substantially in solar technology. And, the Risk and Insurance Management Society (RIMS) has entered into an agreement with the EPA to research and educate its members on mitigation and adaptation strategies.

In sum, climate change will be one of the great challenges of our time, and the insurance industry will be among the sectors most fundamentally impacted. While the prospects of global warming still present more questions than solutions, companies that take the lead in evaluating and addressing climate impact are likely to enjoy a significant competitive advantage in the years to come. ■

Endnote

1. See e.g., Brian Handwerk, *National Geographic News,* November 9, 2004.

The Specialist
is published four times a year by and for the members of the Excess/Surplus/Specialty Lines Interest Group of the CPCU Society. http://essl.cpcusociety.org

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The Specialist

Volume 22 Number 1 February 2008

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