AN EMERGING RISK ISSUE FROM

AUSTIN&STANOVICH
RISK MANAGERS LLC

Winter 2005

Risk Management Issues and Resolutions for the New Year

Year 2005 has arrived and presents the risk management community with a smattering of issues both old and new. From our perspective, there are four key issues. While the issues may at first appear to be unrelated, a closer look reveals each issue may actually have a significant impact on the others.

Key risk management issues for 2005

- Tort reform
- Future of TRIA
- Agent and broker ("producer") remuneration
- Continued softening of the insurance market

Tort reform may aid market softening by reducing future liability insurance costs as liability premiums paid today are for future liability losses. Congressional failure to reauthorize TRIA this year may create capacity issues for risks considered *high profile* and may also destabilize the current marketplace for property, liability and workers compensation insurance. Full disclosure of producer remuneration may create a new form of client competition as producers vie for prospective clients using the issue of contingent commission as leverage point.

Tort Reform: It is no surprise that this subject was a cornerstone of President Bush's State of the Union address on February 2 after hearing his point of view repeatedly during his re-election campaign. Efforts are already underway to reform class action litigation, limit frivolous lawsuits and to place a cap on medical malpractice non-economic damages. These changes, if enacted, will not occur quickly. Risk managers still need to practice "*internal tort reform*" by seeking ways to reduce the frequency of third party claims and to more effectively manage the third party claim settlement process.

Future of TRIA: The Terrorism Risk Insurance Act ("TRIA") was signed into law in 2002 and is to expire on December 31, 2005. As reauthorization is uncertain, ISO has promulgated endorsements for insurance policies written in 2005 that include limitations on terrorism coverage as of January 1, 2006 if TRIA expires while these policies are in force. Stand alone terrorism coverage continues to be available, albeit a limited market, and has stabilized since 2001. Risk managers required to purchase terrorism coverage by lease, mortgage or other contract should start contingency plans for terrorism coverage in anticipation of possible market disruptions later this year.

Producer remuneration: This issue will continue to be a central topic to insurance buyers in 2005, whether a professional risk manager or not. Larger insurance accounts may move to a fee for service arrangement in lieu of commissions. Insurance buyers and risk managers need to see value in the services rendered that is commensurate with commissions paid or fees charged.

Continued softening of the insurance marketplace: Rates continue to soften in 2005 as announced by MarketScout.com in a monthly survey reported by *Business Insurance Daily News* on February 8. We expect this trend to continue throughout this year. Unexpected events such as economic downturn, terrorist act (domestic or foreign) or catastrophic natural event could stem the softening and harden the marketplace for certain buyers. Risk managers need to continue risk control efforts strengthened during the recent hard market and not relax such practices simply due to reduced insurance costs.

Risk manager issues and resolutions for 2005

We asked eight risk managers from various industries for their risk management issues and resolutions for the New Year. Each welcomed the opportunity to speak to us but most did not want to be identified. We decided to treat all comments as anonymous. Risk control issues, including business continuity, is a central issue for many of the risk managers we interviewed. We hope the insight gained from these risk managers will help you plan *New Year resolutions* for your organization.

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RISK MANAGEMENT ISSUES AND RESOLUTIONS FOR THE NEW YEAR

Risk Manager 1-Northeast university: Risk control efforts are the dominant issue. He identified two workers compensation concerns: return to work programs in general and increased frequency of surgery associated with an aging work force. In addition, he is working on protocols when research involves bio-hazard materials.

Risk Manager 2-Northeast university: The emphasis is on risk control techniques and development of a holistic approach to analyzing and managing risks of the organization. Disaster recovery planning and emergency response protocols will be a key issue. There will be increased attention focused on use of university vehicles through enhanced driver training initiatives and review of employee and student driving records.

Risk Manager 3-New England based manufacturer of building products and materials: He has two risk financing resolutions for 2005. The first is cost of excess insurance. He is attacking the issue by seeking more aggressive means of managing losses within the organization's self-insured retention ("SIR"). His second resolution is to become more astute at risk and insurance issues related to conducting business in China.

Risk Manager 4-National entertainment company: Sarbanes-Oxley and corporate governance is one of his primary issues, especially that of directors and officers insurance at the subsidiary company level. In addition, he will continue to focus on workers compensation claims, specifically looking for ways to ratchet down the cost of medical expense.

Risk Manager 5-New England governmental entity: He wants to move from a theoretical model for business continuity to a tested functional plan, but realizes 2005 budget dollars may not allow it. He expressed more concern for devastation from a natural event (i.e. tsunami, windstorms, etc.) than terrorism and will focus on ways to limit windstorm damage to owned buildings. He added domestic terrorism is underestimated in the USA as we seem to experience increased violence from citizens seeking public attention for their agendas.

Risk Manager 6-Northeast based international manufacturing company: This risk manager is preparing for a meeting with the organization's external auditor. As a result, one of her resolutions is to create a way to reconcile the organization's casualty loss accrual to the understanding and satisfaction of the auditor. An ongoing resolution is her continued quest of risk management best practices for her organization.

Risk Manager 7-Mid-Atlantic chemical company: Her resolution for 2005 is to ensure there is a clear service agreement with all risk management service providers utilized by her organization, not just insurance brokers. The agreements will better define the obligations of both the service provider and the risk management department. In addition, she will use a menu approach to purchasing services and ask for the cost of each service, purchasing services only as needed.

Risk Manager 8-national financial services company: Even though insurance cost may decrease in 2005 she is resolved to continue to take a long term view of risk financing arrangements and insurer relationships. She believes the risk model first established in her organization in 1993 continues to work in 2005. She expressed concern about market integrity as softening has occurred rapidly, with little time for insurers to experience sustained profitability.

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