

Risk Factor

Volume 1, Issue 2

Your Guide to Risk and Exposure

The Race for Reform

With the threat of a federal solution to insurance reform issues, state insurance commissions are stepping up efforts to standardize a complex industry.

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Quick quote:

"I'm starting to lose confidence that all 50 states are capable of coming together and solving this problem." Rep. Paul Kanjorski, D-Pa, speaking at the March 31 hearing on insurance regulatory reform.

Just try unraveling fifty states worth of insurance regulations. State Insurance Commissioners have been at it for years. Now the Federal Government wants to try. Yet how to do that? During recent Congressional oversight hearings into the insurance industry's attempts to bring about reform, insurer groups and the feds alike are sure about one thing—the solution to state insurance reform and its ultimate implementation is still quite uncertain.

It's not entirely clear who's advocating what: The Alliance of American Insurers (AAI) is prompting the National Association of Insurance Commissioners (NAIC) to move faster to avoid federal intervention. The Risk and Insurance Management Society (RIMS) has issued a statement that "fully supports the Oxley-Baker reform proposal, and urges Congress to enact these reforms as soon as

News Briefs—April 15, 2004

The Survey Says: According to a recent RIMS survey of corporate risk managers, 88 percent say that workers' compensation is "not under control" in California. What's more, 92 percent say that it costs their company more to maintain a business in that state than in any other, and half say that it's become a deciding factor in whether to move out of California.

EU and Microsoft: Accusing Microsoft Corp. of "near monopoly" tactics to snuff out competition, the European Union has slapped the software giant with a record \$613 million fine. In late March, the EU's antitrust authority gave Microsoft 90 days to give European computer manufacturers a new version of Windows, minus MS's digital media player. The software company also has 120 days to provide the necessary software code that has essentially "shut competitors out of the market", according to the European Commission. The code is to be provided to rivals in the server market so that their servers are able to work with Windows operating systems.

Asbestos and Politics: Though the bill is doomed, the insurer-backed asbestos bill will be introduced to the Senate by U.S. Senate Republican leaders. Republicans are charging Democrats with protecting their own interests and those of trial lawyers who support them politically. The bill is a revision of one stalled earlier by Democrats who contended that the bill did not provide enough capital to pay victims' claims.

possible,” according to a statement by RIMS’ VP of external affairs Janice Ochenkowski. AAI’s Lenore Marema told regulators that “the NAIC needs to act sooner rather than later on key areas such as rate and form filing, company licensing, and market conduct.”

Confusing? Indeed. Even those in the NAIC agree—there is too much work to do, too little time in which to do it, and no clear plan “We know very well should look like con- detail, we know what the state level,” says senior VP of industry for the Property sociation of America Ill. “There is modest, incremental progress, but not nearly enough. Ergo, a lot of people are looking at the discussions in Congress to see what further can be done to get reform or to use federal tools to facilitate state-based reform.”

“Far and away, speed-to-market is the most important reform that is being sought—the ability to have a competitive market out there.” Robert Zeman.

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The Reforms

To date, all parties involved have been able to identify six areas of concern: agent licensing, company licensing, market conduct, rate relief, implementation of an Interstate compact, and some type of federal representation within the Treasury Department. “Far and away, speed-to-market is the most important reform that is being sought—the ability to have a competitive market out there,” says Zeman.

It took just over a year and eleven drafts for the Interstate Compact Working Group, co-chaired by Michigan Insurance Commissioner Frank Fitzgerald and Texas Insurance Commissioner Jose Montemayor to come up with the NAIC’s Regulatory Modernization Action Plan, which is a commitment by state regulators to work toward improving the state-based system of insurance regulation. If all goes well, the NAIC hopes that at least thirty states will have begun reforms by 2008.

“What it clearly does is provide for a single point of entry for review of life products and long-term care products,” says NAIC president Ernie Csiszar, who is also South Carolina’s Insurance Commissioner. “You would have that same interstate compact adopted in the states. Once you have that in place, the only thing missing is the standards. It’s a two-fold process—we have to get the interstate compact passed, and then we can develop the product category standards on a national basis.”

Can it be done? In a small number of cases, it already has been. A few states have already adopted their own rate reforms. For over thirty years, Illinois has had a competitive regulatory approach, meaning it was independent of the approval process by the insurance regulators. Says Zeman, Illinois’ system has worked because the competition has helped to keep rates low.

Yet will this work on a national level for all states? Tough to say, according to the experts. One reason is that federal implementation may ignore some fundamental changes in state laws and procedures. “Going from the federal level down instead of the state level up sounds easy, but it’s enormously complex,” says Zeman. “You immediately get into the different considerations of state license insurers versus property/casualty insurers, which vary from state to state.”

Even if a federal solution comes, state regulations need to be in place or on their way to adoption. Can that be accomplished any time soon? “The jury is still out,” says Csiszar. “We have to get our act together and get it done at the NAIC. The task is made more difficult by the fact that you have to go through fifty legislators. I’m optimistic enough to believe that it can be done. I’m also realistic enough to see that the only way to get it done is to put pressure on the organization and the commissioners through whatever means we can.”

Speed-to-Market

Currently, most state insurance regulations require approval from the State Insurance Commission in order to raise or lower rates. While the new proposals are not attempting to eliminate that, there is a push to modify it.

What’s being proposed, and has been adopted by at least five states at press time, is a flex-rating arrangement.

Flex rating allows companies to raise or lower their rates within a certain percentage without gaining prior approval by the State Insurance Commissioner. "It's viewed as an intermediate approach," says Zeman. He adds that NCOIL has developed a flex-rating model that Zeman suggests states adopt.

The insurance groups are not sitting back waiting for Congress to move. Zeman and others still continue to push reforms through each state, hoping to resolve the issue at the state level before the legalities of the federal reform proposals would take effect. "We need competitive markets, quite frankly, and we're out there to get the state-based reforms. We're not waiting for final actions in Congress," says Zeman.

And the news coming from the states is encouraging. Approximately fifteen states are engaged in discussions regarding reform. State legislators, says Zeman, are slowly awakening to the fact that reform is needed. "The problem is that it's not a completely uniform understanding, and legislators may not agree on what type of reform is appropriate."

"The way it looks now," says Csiszar, "is that we (the state insurance commissions) would have a three-year period for the states to implement these different pieces of legislation and if it does not become implemented, then it becomes a federal mandate."

That may change, say the experts. As discussions continue, there is more of a sense of a unified approach than any sense of agendas being pushed. All agree that the current state system isn't working. Says Csiszar, "How the industry got itself into this over the years, God only knows. At some point, it may have made some sense. At this point, I'm the first to agree that reform is needed."

Moves & Notes

New Willis leaders: **Jeanne Scampas** has joined Willis Group Holdings as executive vice president for Global Information Systems and Global Operations. Also, **Leslie Nylund** has joined Willis as New York regional executive officer, executive vice president.

New Council: RIMS has announced the election of its Executive Council for 2004-2005. Officers include: **Nancy Chambers, president; Ellen Vinck, Janet Barnes, Sanford Bragman, Lance Ewing, Daniel Kugler, Michael Liebowitz, Deborah Luthi, Janice Ochenkowski, and Joseph Restoule.**

RM of the Year: RIMS has announced **Christopher Mandel** as its choice for the 2004 Risk Manager of the Year. Mandel, past president of RIMS, was honored for his enterprise risk strategy that includes sixteen divisions of the United Services Automobile Association, Mandel's employer.

Merger: The St. Paul Cos. and Travelers Property Casualty Corp. have announced the shareholder approval of the companies' \$16.4 billion merger.

California Workers Comp: Reform?

California's no longer the most expensive place in the country for workers' compensation coverage. That's because last week, the state's lawmakers passed legislation that promises to reform the current state workers' comp program. Specific savings are not known, but many believe employers stand to save billions of dollars because of the legislation's tougher standards of proof for workers claiming to be injured. Claims of pain would be ineligible for benefits, and employees would be required to use doctors approved by the employer and their insurance companies.



AP Photo

Critics are arguing that the new legislation does nothing to set limits on what insurers can charge businesses for workers' comp. Democrats in California's legislature tried to get rate controls built into the bill, where the cost savings would be passed on to businesses. Governor Arnold Schwarzenegger refused, insisting competition would drive the rates lower. That has lawmakers worried that the bill will do nothing to alleviate California's workers' comp costs, which totaled \$17.9 billion last year in claims paid, up sharply from a 1997 price of \$6.4 billion.

"Legislative interest in workers compensation accelerates in direct response to business concerns over escalating costs," says Robert C. Wellman, Jr., partner of Richfield, Ohio-based law firm Crain, Langner & Co. "Heightened interest does not, however, lead to regulatory reform."

Medical Malpractice: The Road To Reform

Now that the states are moving forward with plans to reform the regulatory system, what of the move to cure medical malpractice's ills? By all accounts, it's in desperate need of oxygen.

Some have suggested that the cure for medical malpractice's ailments could be found in the state's reform push. Yet Robert L. Zeman, senior VP of industry and regulatory affairs for the Property Casualty Insurers Association of America (PCI) in Des Plaines, Ill., disagrees. He says comparing the two areas in need of reform is much like comparing apples to oranges.

"There could be some improvements in the medical liability marketplace through some of the reforms that we've talked about. There's a bit of a connection, but the added piece that's needed to get true medical liability reform is the tort reform piece. Medical liability itself has not been part of the Oxley-Baker discussions. There's a separate discussion in Congress for that. There have been medical liability proposals in Congress that have gone nowhere/ It's another example of how reform can be accomplished at the state level. Some of it has been done over the years. Unfortunately, we are not looking at imminent enactment of good federal reform in that area."



Photo: Ryan Morrison

Conference News

June 6-9: Sixth Annual World Insurance Forum, Fairmont Southampton Hotel, Hamilton, Bermuda. Conference highlights include the Industry Leaders' Forum, this year moderated by Michael A. Butt, Chairman of AXIS Capital Holdings Limited; the first Bermuda Market Capabilities showcase of Bermuda's risk-related products and services; and Analysts, Rating Agencies and Regulators in a panel discussion. Contact Susan Pewter, project coordinator, at Tel: 441-292-6386 • Fax: 441-292-6990. Email: worldinsuranceforum@bis.bm

June 8-11: ICAP 2004, The Fairmont Hamilton Princess - Hamilton, Bermuda. \$500 discount for risk managers. Captives conference featuring over 38 of the world's leading experts in alternative risk solutions and captives. Workshops, tutorials and breakout sessions. For more information, visit <http://www.ibcusa.com/icap>

June 21-24: Tenth Annual Risk USA Congress, Seaport Hotel & World Trade Center, Boston. Highlights include: regulatory vs. risk management orientations of risk analysis panel debate, credit risk modeling and valuing interest rate derivatives; seminars on capital allocation techniques for credit, operational and market risk. For more information, contact Aristotle Liu at aliu@riskwaters.com, Tel: +44 (0) 207.484.9700

Lighter Side of Risk

"An insurance salesman sits next to a passenger on a transcontinental flight. Another insurance salesman sits next to a passenger on a cross-country train. Which passenger will jump out the window first?"— Anonymous

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