

Forrest Sherer Inc.

The Sherer Edge

2003-2004 IIAI Agency of the Year

The Sherer Edge Insurance and Risk Management
Employee Benefits • Financial Services • Loss Control
Surety • Personal Insurance Since 1920



Email: fsi@fsiinsurance.com

Website: www.forrestsherer.com

COMMERCIAL INSURANCE CENTER

24 North 6th St. • P.O. Box 900

Terre Haute, IN 47808

Telephone: (812) 232-0441

Fax: (812) 232-1783

PERSONAL INSURANCE CENTER

1219 Ohio St. • P.O. Box 506

Terre Haute, IN 47808

Telephone: (812) 232-6011

Fax: (812) 232-6013

THE INSURANCE NEWSLETTER

Summer 2004

Is The Hard Market Over?

The answer, briefly, is “Yes and No.” Let us explain.

The “Yes” has qualifications, of course. For property insurance policyholders with good loss records, the “Yes” generally applies. This does not mean that rates will be comparable to the rates in effect in the late ‘90’s. Those rates may never return. (We have to qualify the word “never” with the word “may.”) But in the absence of specially hazardous loss exposures, whether fire, windstorm or whatever, property insurance rates—again, for some clients with good loss records — have peaked and have started to drift downward. They should settle a bit below recent levels. Note that property insurance encompasses 20% of the commercial business lines.

Policyholders with poor loss records will continue to face exigencies of a hard market, with variations by individual accounts. Note that we’re still referring only to property insurance.

Casualty insurance consists of the various forms of liability insurance plus workers comp. Here there’s a wide variety of market conditions. For example:

- Worker’s comp varies very much by state, with comp in California being a horrible situation for many businesses.

Too early to tell if recent legislation there is helping.

In many other states it’s still a hard market.

Aside from the well-known rapid rise in medical costs, several other factors are at work to raise loss ratios for workers’ comp. At least 25% of workers’ comp claims have an element of impropriety. There are misunderstandings and honest mistakes, but also cost shifting from unoccupational medical costs, employee resentment, unscrupulous service providers, and outright fraud. All these amount to over \$5 billion a year, according to the National Insurance Crime Bureau.

- Medical malpractice is very much in a hard market, especially for high risk specialties, nursing homes and hospitals. Other professional liabilities, e.g., for lawyers and accountants, are also tough to get.
- Directors & Officers (D&O) is still in a hard market especially for companies with publicly traded stocks. It may be peaking for privately owned companies and non-profits.
- Auto liability — for both commercial vehicles and private passenger cars — still has a bit of a way to go upward in some areas and

may be peaking elsewhere.

The upward pressure arises mainly from the relentless explosion in health care costs and its effects on the cost of treating injured parties —

This pressure also affects the cost of workers’ comp and other liability coverages dealing with bodily injuries e.g., general liability, products, etc. The market in these sectors remain on the high side, not only because of the health care costs, but due in part to our litigious society.

- EPLI — Employment Practices Liability Insurance — still feels the upward pressure of discrimination and sexual harassment cases.
- Finally, high limit Umbrella and Excess liability. The hard market has manifested itself not only by premium rate escalation but also by curtailing limits and requiring high SIRs — Self-Insured Retentions. The capacity situation has eased somewhat to the extent that previous limits — of several years ago — may often be available by the layering of limits through two or more carriers. Rates are still high, but may be peaking. Don’t bet on it, though.

To summarize, policyholders with zero loss records are in a better position to benefit from softening market

conditions. Property insurance, e.g., fire, windstorm, etc., is becoming more favorable to buyers of insurance while more forms of casualty insurance are still in somewhat of a seller's market.

The moral: do what you can to prevent losses from occurring and to ameliorate the effects of losses that nevertheless do occur.

The Rating Scoreboard

The May issue of "Best's Review", published by the A.M. Best Company, leading insurance rating agency, revealed the following box score for Property/Casualty insurers. In this month's list of companies, there were:

- 36 downgrades
- 5 upgrades
- 7 lower than B+
- 12 non-rated

There is no bargain in a policy with a low premium when the insurer won't be around a few years hence to pay a claim.

Making Adjustments to Changing Conditions

A recent brief history: The previous hard market existed from about early 1985 to mid- or late-1987. Then the soft market — that is, the low-cost buyers' market — lasted until about the 4th quarter of 1999. It ended just before the time that the dot com bubble burst — in March 2000. The rest you remember quite well.

During the past very difficult four years, various business entities — including some of our clients — reacted in an understandably but potentially dangerous way. They cut back on their insurance. Dropped some coverages, reduced amounts on others. "We can't go over budget" was often the rationale.

Of course, some of this was forced on the insurance buyers by the hard-driving insurers. No ques-

tion about it. But some of it was simply taking undue risks with the very viability of the companies that cut back on their insurance purchases.

In our view, the only actions of this sort that made good business sense was the raising of one's deductibles and self-insured retentions. Eliminating coverage at the bottom is sound practice.

The antithesis — lowering limits at the top — can be self-destructive.

Now is the time, when premiums are more affordable and general business conditions seem to be picking up, for those who cut back on coverages to give serious thought to restoring what may have been dropped, reduced or never bought.

We'll be glad to sit down with you and go over your present insurance needs and see what, if any, improvements are in order. Just give us a buzz.

How Long to Keep Policies?

It depends on the type of policy. First for the easy answer. If you have a policy that only covers direct physical damage to your property, e.g., fire, burglary, explosion, etc., then it could be safe to discard it after four or five years. The reason? Losses become known either immediately or after several months at worst. The only need to hold them for a couple of years would be the time a litigated loss situation takes to wend its way through the courts.

The above situation is almost academic, because the over-whelming majority of policies today include coverages that are either solely "third party" liability or combinations of direct damage and liability. It's the liability situation that is the sticking point that requires you to keep those policies forever — either the policies themselves or reliable copies of them, electronic or otherwise.

Take the following true case as an

example. While it happened to be a Connecticut case, adjudicated by the State Supreme Court of Connecticut, it could have been in virtually any other jurisdiction, with the same result.

The policyholder was sued by many claimants, alleging injuries sustained over a period of 45 years. (Long enough?) The defendant claimed it had liability insurance throughout the period with different insurers at various times. Many of the policies were lost or destroyed. And it's fair to assume that some of the insurers the company remembered had their names changed by takeovers, mergers or whatever — a not uncommon situation over a 45-year period, or even over a 10-year span.

One of the five insurers identified by the policyholders contended that it — the insurer — should only be responsible for its share of the cost of the defense, equal to the years it had written the insurance. The policyholder's contention that the insurer was jointly and severally liable for defense costs was rejected by the court.

The clear implication is that no insurer would have to pick up the marbles of insurers that can't be identified because proof of coverage was no longer available.

While 45 years is a long time, the same situation might have occurred if policy information was lost during, say, a 10-year period of claim occurrence.

P.S. A policy covering employee dishonesty falls into the "keep forever" category. Some losses of this type take many years to discover. We remember such a case that was hidden for 24 years!

Too Often Overlooked: Environmental Exposures

Ok, so you're not a chemical manufacturer or an oil refiner and

you don't operate a coal mine or a nuclear facility, so you don't have any environmental exposures. Right? Of course not. The above are the obvious suspects.

But there are so many other innocuous businesses whose owners or operators don't think of their environmental risks and exposures.

Fuels, cleaning solvents and similar hazardous materials may be used in various processing, including waste-handling. Take, for example, a retail hardware store or a car dealership, as two of just a host of businesses of various types with pollution exposures.

You use a third party waste-hauler. Is it in compliance with all federal and state environmental regulations? Even if they are, you could be ultimately liable for improper disposal of toxic waste, both cleanup costs and liability to injured parties.

One big hidden exposure involves what you might inherit by way of merger or acquisition of either a going business or simply a purchase of real estate. You cannot rely on the policy of the company with whom you merged or acquired. It may or may not cover the damage you discover after that policy expired, aside from any other deficiency of that policy or its insurer.

Sometimes the danger is hidden for years after the transaction takes place, and previous parties who may have been liable are either out of business or physically disappeared.

Many types of businesses have underground storage tanks. Aside from the obvious — garages and the like — apartment house complexes have storage tanks for heating oil. Tanks can and do leak .

We haven't covered the whole gamut of business exposures to environmental damage and possible bodily injury therefrom as well as property damage. But the key

insurance factor is that virtually all environmentally related exposures are excluded from standard policies.

Special pollution coverages are needed for several distinct types of damage:

- Damage to your own property, including business interruption;
- Cleanup costs;
- Liability to third parties for bodily injury, damage to their property including business interruption;
- Liability to government agencies, which may include fines.

The coverage available goes by the fancy name of Environmental Impairment Liability Insurance — EIL for short. Major league insurers write it. The underwriting market is selective and careful, but it's not a closed market. Give us a buzz before something serious happens.

Teenagers as Employees

With the cost of college soaring, more and more teenagers are working full time at summer jobs. Many of these jobs require driving. Of course, it's a given that such work is permissible if the teen has a driver's license. Nevertheless, there are restrictions spelled out by the U.S. Dept. of Labor.

First and foremost: 16-year-olds — and younger, of course — may not be allowed to drive as part of their work duties. Even such a trip as driving to a store to pick up supplies or to a gas station to fill up is verboten.

Now we have 17-year-olds. First are the limitations for on-the-job driving:

- Limited to daylight hours only
- The kid's driver's license must be valid for the type of driving involved.
- He or she must have successfully completed a state approved driver ed course and have no moving violations at the time of

hire.

- The auto or truck involved must not exceed 6,000 lbs. gross vehicle weight.
- The employer has to instruct the teen that the seat belts must be used when driving the vehicle.

In addition to these limitations there are a number of absolute prohibitions applicable to 17-year-olds.

- Driving may not involve towing vehicles
- No route deliveries or route sales
- No transportation for hire of passengers, property or goods.
- No urgent time-sensitive deliveries, (Pizzas?)
- No transporting more than three passengers, including co-employees.
- No driving more than 50 miles from place of employment
- No more than two trips a day from place of employment to deliver goods to a customer
- Driving must be occasional and casual to employment duties, i.e., no more than one-third of the time in any work-day and 20% of any workweek

With summer approaching, this type of employment takes on added significance. Of course, the rules apply all year. Violations by the employer that lead to accidents can seriously jeopardize one's insurance — as well as problems with the Dept. of Labor.

A Strange Theft Epidemic

You wouldn't be surprised to learn of rapidly escalating thefts of jewelry or electronic goods of all kinds. But you may be surprised to learn of a 64% increase, from 1995 and 2001, of theft of contractors' heavy equipment, e.g., bulldozers, graders, etc., some of which run to \$250,000 or \$300,000.

The largest percentage of losses

occur at construction sites, rather than at owners' premises. The site foreman leaves the equipment on a Friday night ready for the Monday crew. The stuff is out in the open and has been spotted beforehand. When the coast is clear, the equipment is moved onto a flatbed truck, covered with a tarp and on its way to a customer.

This sort of operation has become epidemic that creates collateral losses, such as loss of short-term rentals, project delay penalties, etc. And of course much higher insurance premiums and difficulties in getting and/or keeping insurance.

There are protection procedures available such as fencing, off-hours security patrols, etc. One of the best is the satellite tracking device LoJack for Heavy Equipment. 87% of LoJack equipped material has been recovered less than 24 hours after reporting to police and 95% of recovered equipment was undamaged. Other obvious safeguards include ignition disabling devices, movement prevention devices, and so forth.

If crooks can steal stuff that weighs 20 tons or so, so they can steal anything. The lesson is that no

matter what kind of merchandise, supplies or equipment you have in your business it is not immune to theft. Nothing is. And, of course, huge sums of money are transferable to the wrong people and places by the click of a mouse. Insurance to the rescue!

Changing World Conditions

After 9/11, direct foreign investments by American companies dried up and the need for political risk insurance pretty much dried up with it. That is changing as both the world economies and the U.S. economy is recovering and international investing is picking up. How might that affect your company's operations?

Let's say that you do some business with a company located overseas, or perhaps you do some contracting work with foreign governments themselves. The foreign company — or government — is a customer for goods or services and thus has to pay you. Any of several obstacles may occur due to political action by the foreign government. It may decree that its currency may not be convertible into dollars; it may lift

exporting or importing licenses; it may actually expropriate your assets in that country. Whatever.

Political risk insurance may be written by any of several companies or by a quasi-government agency, OPIC — Overseas Private Investment Corporation. You probably don't need the insurance if your foreign dealings are solely with Canada, Western European countries, Japan, Australia and New Zealand, and probably Chile as well. But beyond the aforementioned and you could well be at political risk that calls for insurance.

One other aspect would apply to the aforementioned as well. Your customer goes broke and can't pay you. If your customer is an American company, credit insurance from any of several U.S. insurers will protect you. If your customer is elsewhere, whether in the Western Europe or in the third world, credit insurance would have to be obtained from the FCIA, the Foreign Credit Insurance Association.

If you have any foreign exposures we should sit down and talk about political risk insurance. Give us a buzz.

EXCITING TIMES IN LIFE & EMPLOYEE BENEFITS!

Last quarter, we announced the promotion of Leah Fouts to Vice President of our Employee Benefits Department. We now want to let you know about the exciting things taking place in that department.

Forrest Sherer has been successfully providing overall insurance solutions to our clients since 1920. In further strengthening our ability, we are pleased to announce our cooperative marketing agreement for *life and financial products* with Mike and Nancy Farr of the Michael R. Farr Agency in Terre Haute, Indiana. Mike and Nancy have specialized in personal and professional financial services for over 30 years.

Together with the Farrs, our Employee Benefits Department offers an array of financial products and services for individuals and business owners. Products include term life insurance, variable and fixed annuities, estate tax planning, buy/sell agreements, disability coverages, retirement plans and, of course, financial planning services.

Now is the time to make certain your family and business are well protected. Our unique ability to professionally assist you in this – that's the *Sherer Edge!*