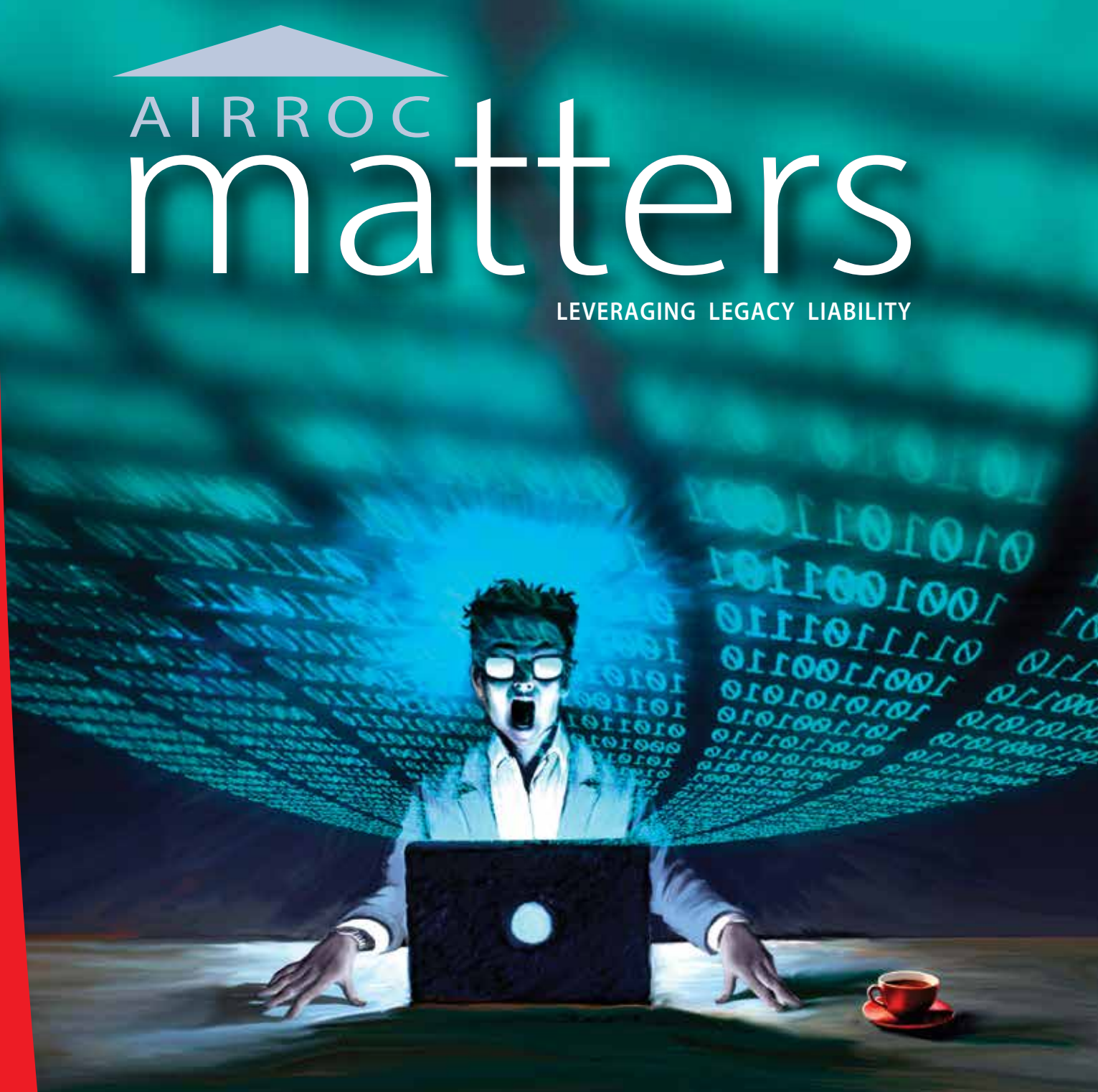
www.airroc.org Vol. 13 No. 2 Fall 2017

AIRROC

matters

LEVERAGING LEGACY LIABILITY



Emerging Cyber Risk: Can Insurers "Hack" It?

CYBERPAIN • MURKY AGREEMENT • MY EYE'S ON YOU • EUROSTABILITY • CASE CLOSED
SHINE ON PAUL, SHINE ON • LAFARGE KNITS • DAM THAT BEAVER • EVENT BECKONS

Saul Ewing LLP

Meeting Your Insurance Needs

FULL SERVICE COUNSEL TO THE INSURANCE INDUSTRY

Saul Ewing's Insurance Practice brings real world insurance industry and regulatory experience to a wide variety of insurance issues, including litigation, regulatory counseling, reinsurance, and corporate matters.

» www.saul.com

Contact us to find out how Saul Ewing's experienced insurance attorneys can help you with your next project.

Paul M. Hummer
Partner & Insurance Practice Chair
215.972.7788 ■ phummer@saul.com

DELAWARE MARYLAND MASSACHUSETTS NEW JERSEY NEW YORK PENNSYLVANIA WASHINGTON, DC

Sounds Like "Cyber"-rattling to me…

Peter A. Scarpato

Unless you've been living under a rock, you know the omnipotence of cyber risk in its many forms, from private corporate to public government hacks. Every day, "black hat" trolls take giddy delight blitzing the net with all forms of cyber-attacks, gaming everything from personal emails to presidential elections. And while certainly not immune from these activities, insurance companies bear the additional burden of providing products and services designed to cover the economic fallout from these pernicious attacks, morphing as fast as the viruses against which they protect.

Thus, we begin with *Emerging Cyber Risk: Can Insurers 'Hack' It?* a roundtable discussion among Eric Cernak, Kirstin Simonson, Karrieann Couture, and moderated by Laurie Kamaiko. In this lively and insightful discussion, the panel explores the challenge of cyber risks from the underwriting, product development and claims handling perspective. There is no insurance topic, big or small, that the group fails to address. Moving forward, this edition of AM presents *Twisting in the Wind: Covered Agreement Left Dangling by Uncertainty and Politics*, Fred Pomerantz's continuing dive into the murky depths of the Covered Agreement, and what it means for the United States.

A familiar presenter to AIRROC Matters, Barbara Murray, returns with useful management advice in "*Eyes-On" Management: Watch Lists for Effective Management of Significant P&C Insurance Risks.* A significant tool in the perennial quest to avoid surprise reserve adjustments, watch lists serve many functions, acting as an early warning signal for potentially large claims, helping to improve the allocation of claims handling and legal resources, and assisting actuaries with pricing and reserving analyses. A must read.

As promised, Eleni Iacovides offers the second in her trio of articles on the legacy market in the UK and Continental Europe, *The Legacy Market: Strength. Stability. Transparency. Certainty. That Order.* Eleni continues to provide useful background, touting Europe's many stable, time-tested vehicles that lead to clean balance sheets and effective finality.

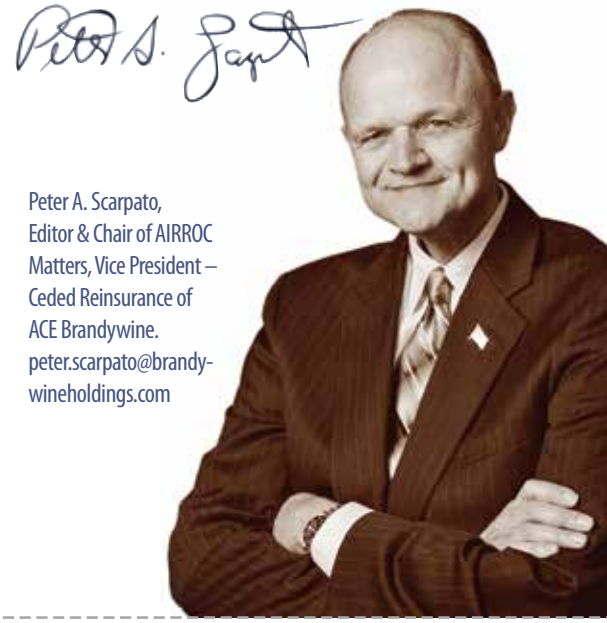
Like the "City," the "Courts" never seem to sleep. In our Legalese section, Robin Dusek and Patrick Frye walk us through the ramifications of the rumored, "courthouse-steps" settlement of the long running case, United States Fidelity & Guaranty Co. v. American Re-Insurance Co. ("USF&G v. Am Re"). The article, aptly named *USF&G v. American Re settles: What does that mean?* is a good retool of the parameters of the prior appealed ruling, which now becomes the law of the case.

Paul Corver has been around – the run off circuit, that is. In fact, he has served with distinction in this arena for 27 of his 32 years in business; and for nine of those years to-date has been the Chairman of IRLA. Our Spotlight segment leans in, revealing Paul's views on everything from second careers to a closer AIRROC/IRLA relationship.

While Madame Fahey quietly sits and knits, we present *A Tale of Three Cities*, summarizing the valuable educational presentations served up in Chicago, Hartford and New York. Pick a hot topic and it's probably on our list. Fortunately, Madame Fahey put down her knitting long enough to pen her Message from the Executive Director, choosing, of all animals, the industrious beaver as the embodiment of all things AIRROC. Wrap it up with Present Value, and we're done.

So, keep it moving, keep it strong, but above all, keep it real.

Let us hear from you,



Peter A. Scarpato,
Editor & Chair of AIRROC Matters, Vice President – Ceded Reinsurance of ACE Brandywine.
peter.scarpato@brandywineholdings.com

AIRROC® Publication Committee

Editor & Chair
Peter A. Scarpato
peter.scarpato@brandywineholdings.com

Vice Chair
Maryann Taylor
mtaylor@damato-lynch.com

Assistant Editor
Connie D. O'Mara
connie@cdomaraconsulting.com

Peter H. Bickford
pbickford@pbnylaw.com

Jenna Buda
jbuda@allstate.com

Bina T. Dagar
bdagar@ameyaconsulting.com

Randi Ellias
rellias@butlerrubin.com

Carolyn Fahey
carolyn@airroc.org

Robert D. Goodman
rgoodman@saul.com

Jeffrey D. Grossman
jgrossman@stradley.com

Nicholas H. Horsmon
nhorsmon@law.gwu.edu

Frederick J. Pomerantz
fpomerantz@goldbergsegalla.com

Francine L. Semaya
flsemaya@gmail.com

Vivien Tyrell
vivien.tyrell@rpc.co.uk

Greg Wyles
greg.wyles@aig.com

Marketing Consultant
Gina Pirozzi
gina@gpirozzi.com

Design & Illustration
Myers Creative Services
nicole@myerscreative.net

The AIRROC® Matters Editorial Board welcomes authors' new and reprinted with permission articles on current topics of interest to AIRROC's membership. The Board reserves the right to edit submissions for content and/or space.

Navigating the new world of runoff.

New regulations in Rhode Island provide for Insurance Business Transfers, an effective restructuring tool that allows US insurers and reinsurers to achieve finality with respect to their commercial runoff businesses. EY's Insurance team can help you navigate the transfer process as well as the challenges related to the optimal use of deployed capital, so together we can establish a foundation for your success.

For more information contact:

Jay Votta
+1 212 773 0509
jay.votta@ey.com

Dave Meyer
+1 513 612 1530
david.meyer@ey.com

John Ferrara
+1 212 773 2835
john.ferrara@ey.com

EY
Building a better working world

© 2017 EYGM Limited. All Rights Reserved. EDNone. 1703-2211547

AIRROC matters

Vol. 13 No. 2 Fall 2017 www.airroc.org

Illustrations / R. Edwards

Copyright Notice AIRROC® Matters is published three times per year to provide insights and commentary on U.S. legacy business, to educate members and the public, stimulating discussion and fostering innovation to advance the industry's interests. Publishing and editorial decisions are based on the editor's judgment of writing quality, relevance to AIRROC® members' interests and timeliness of submissions.

Published articles should not be deemed to reflect the views of any AIRROC® member, unless so stated. AIRROC® endorsement of any views expressed in articles should not be inferred, unless so stated.

AIRROC® Matters magazine is published by the Association of Insurance and Reinsurance Run-off Companies. ©2017. All rights reserved. No reproduction of any portion of this issue is allowed without the publisher's prior written permission.

AIRROC

AIRROC Board of Directors & Officers 2017

Leah Spivey *(Chair)* Munich Re America
Michael Fitzgerald *(Co-Vice Chair)* QBE North America
William Teich *(Co-Vice Chair)* The Hartford
Marianne Petillo *(Treasurer)* ROM Reinsurance Management Company
Jose Martinez, Jr. *(Secretary)** CNA
Karen Amos Resolute Management Services
Andrew Hill Zurich Legacy Solutions
Edward Gibney Vice President, R&Q
William Goldsmith AIG
Ivan Jaffa RiverStone ReSources LLC
David Kenyon Swiss Re
André Lefebvre Arrowpoint Capital
William Littel Allstate
Betsy Mitchell Armour Risk Management Inc.
Peter Scarpato Brandywine Group of Insurance and Reinsurance Companies
Carolyn Fahey *(Executive Director)**
Susan Aldridge *(General Counsel)** Norton Rose Fulbright

*Non-Board member

AIRROC Executive Committees

Governance Committee
Co-Chair William Goldsmith AIG
Co-Chair Bill Littel Allstate

Education Committee
Chair Karen Amos Resolute Management Services
Vice Chair J. Marcus Doran Armour Risk

Finance Committee
Chair Michael Fitzgerald QBE
Vice Chair Marianne Petillo ROM Re

Marketing/Member Recruitment Committee
Co-Chair David Kenyon Swiss Re
Co-Chair Ivan Jaffa RiverStone ReSources

October Event Committee
Chair Edward Gibney R&Q Solutions LLC

Publication Committee
Chair / Editor-in-Chief Peter A. Scarpato Brandywine
Vice Chair Maryann Taylor D'Amato & Lynch

CLIP Committee
Chair Marianne Petillo ROM Re

AIRROC Advisory Council

David Alberts Mayer Brown LLP
Debra Hall Hall Arbitrations and SagePoint Solutions Group LLC
Stephen Johnson Stradley Ronan Stevens & Young LLP
Steve McElhiney EWI Re, Inc.
Connie O'Mara O'Mara Consulting LLC
Sandra Santomenno Towers Watson

AIRROC Board Liaison
Marianne Petillo ROM Re

Emerging Cyber Risk

Roundtable Explores Cyber Insurance Issues

Cyber risks are among the most pervasive risks of our time. They impact all industries that purchase insurance, and all lines of insurance. A panel from the insurance community whose roles in their companies focus on cyber risks (some from the underwriting and product development perspective, and others from the claims handling perspective) discuss key issues and challenges that insurers face from cyber risks.

Panelists:

Eric Cernak – Munich Re US – Cyber and Privacy Practice Leader

Kirstin Simonson – Travelers – Cyber Lead for Global Technology

Karrieann Couture – CNA Specialty Claims – overseeing technology, cyber, and fidelity claims operations

Moderator: Laurie Kamaiko – Sedgwick LLP – Cybersecurity & Practice Group Leadership Team and Co-Chair Cyber Insurance Task Force

Q: *What constitutes a "cyber risk," and what is the range of cyber risks that insurers and their policyholders are dealing with these days?*

Simonson: In the early days, we were focused on whether general liability insurance would respond to cybersquatting or other intellectual property issues. Around 2003, all of that changed when states started enacting breach notification laws requiring notice to individuals when the security of their personal information held by companies was breached and that information was stolen or lost; that was the driver behind a lot of the cyber coverages. Today, there are now really two buckets of risks in play: The first is the data privacy bucket, which involves the privacy of personal information and the protection of confidential information of others that a company holds within the confines of its networks. The second is the network security bucket, which involves how a network is being infiltrated and used to cause some type of harm to one's own company or to others. While there are liability aspects to these and resulting third-party claims, a big chunk of the exposure is the expenses a business faces when an event happens, whether it is a data hacking event that requires forensics and notification costs, or whether it is ransomware with the investigation of that and issues of whether and how the business pays the ransom. It all stems from how everything is connected across the internet, which places everything at risk.

Q: What are some of the types of coverages under traditional lines of insurance, as well as stand-alone cyber policies, that are being impacted by cyber risks?

Cernak: Coverages have evolved from tech E&O, media liability and, ecommerce insurance. Now there is not only data breach coverage for the expenses of responding to and remediating a data breach, but also for the third party actions that can be brought as a result of a breach. There is also systems damage and restoration coverage that is of growing importance, to help businesses restore their systems or data that may have been corrupted or stolen as a result of a computer attack. A corollary to that on the third party side is actions being brought against businesses for transmitting malware, propagating a denial of service attack (even if the company is not aware that it is being used for that), or breaches of sensitive information held by a corporation.

Originally, large organizations were more interested in purchasing cyber coverages as a stand-alone policy.

Originally, larger organizations were more interested in purchasing cyber coverages as a stand-alone policy. Over time, however, it has migrated to smaller organizations that usually access this coverage through endorsements to traditional types of policies. Some coverages may not be as common on an endorsement basis as they are on a stand-alone cyber policy basis, such as fraudulent funds transfer—otherwise known as business email compromise (BEC)—or contingent business interruption, property, and media liability coverages. Part of the reason for this is that for a stand-alone cyber policy, the underwriting process allows one to really dive in and understand the risk.

illustration / Rafael Edwards

Laurie A. Kamaiko & Bina T. Dagar

The primary difference is that you're not going to find a lot of manuscripting or tailored coverages in the endorsement market. The endorsements are standard, with a short (or no) application, and often with prepackaged affordable coverages that can provide as little as $5,000 up to $1,000,000 of coverage. The majority of the coverages provided by endorsement also have services pre-packaged in at pre-negotiated rates for breach response, forensic IT, legal, or extortion specialists. This makes cyber coverage by endorsement a pretty good vehicle for smaller entities, and entities often move up from cyber endorsements to cyber stand-alone coverage over time.

Q: What lines of insurance offer cyber coverage endorsements?

Couture: Cyber endorsements are offered on professional liability policies, and often pick up first party expense for a data breach, with the idea that the main policy may pick up some privacy liability protection if it arises out of professional services. That privacy liability coverage may be broad, but does not include everything, so there may be situations where the endorsement/policy combination may not address all cyber needs. For example, where a business is experiencing a privacy liability situation impacting employees or vendors, there may be no coverage under its traditional professional liability coverage even with a cyber endorsement.

Cernak: There is a movement toward more comprehensive endorsement packages. Early on, the insured would have to guess at what it needed, and a business would get an endorsement for data breach or for a first party computer attack. There is a growing trend for providing the most common cyber coverages under a single endorsement, at a capped annual aggregate. The good news is there is probably some coverage for other cyber incidents in these more comprehensive endorsements, than

From left: Karrieann Couture, Eric Cernak and Kirstin Simonson

Cyber Risk (continued)

what the insured may have initially anticipated and as noted also provide services that provide a lot of value.

Q: How are the cyber exposures from smart products impacting the cyber market and interrelating with traditional lines of insurance, such as general liability, professional liability, product liability and product recall, even homeowners and auto insurance?

Simonson: When we think about all of the devices available now, whether it's a smart home device, autonomous vehicles, wearables, we see everything is interconnected. One of the things that is going to start coming more into play is attempts to attach liability to the manufacturers of these devices, and possibly even the distributers and sellers of the devices. Also, when a device at home doesn't behave the way it's supposed to, or when the device is hacked and it causes something like your HVAC or furnace to turn off while you are gone, and your pipes freeze and your house is damaged, what is the impact on the standard homeowners coverage?

In a commercial setting, what if a refrigeration system with medical samples for a clinical trial is shut off? What are the damages, policies and coverages impacted? There may even be recall of some of these devices and the components within them. The industry will face many challenges and legal tests in the coming years of trying to determine where the liability is, and which kind of policy is going to respond or not respond. It blends into traditional products liability, even with just a failure of security of the device, and leads to downstream impact. From the autonomous vehicle perspective, we hear discussions right now about who is responsible and whose insurer is going to pay if there is an accident. Currently, auto is heavily regulated and there is a no-fault system as well as a tort system. But when is an accident the fault of the human behavior of the driver or the autonomous vehicle, or the fault of another vehicle that is human driven? There's a lot that we need to think about when we look at insurance coverage for these accidents.

Couture: With regard to professional liability policies, typically those are designed for situations where a professional such as a lawyer or accountant provides inappropriate advice and does not contemplate injury that might arise out of disclosure of private or confidential information. But these policies tend to have broad definitions of "professional services"; and if there is an impact to the insured's client, there is a chance that the policy is going to be picking up the third party claim. However, it's not likely to pick up the first party response costs to a data breach, and that's where attorneys and other professionals really need to focus, because they may have legal obligations to respond to such a breach; and if they don't have coverage for it, they will be funding that themselves.

Q: *Are there cyber events which trigger multiple policies, in different lines of insurance?*

Simonson: Denial of service events can impact a property policy and a cyber policy. Each may have business interruption and contingent business interruption coverages, although they can also be very different in how the coverages are going to apply.

For years we've seen the pressure on GL policies to cover data breaches. Now, as we see more business email compromise claims and social engineering claims that involve money transfer, we are seeing more pressure on traditional crime policies.

As purchasers are buying policies that have duplicate coverages, you're going to see interplay between the policies and associated pressures and challenges. The coordination of responses between multiple policies is even more challenging when they are issued by different carriers. The bigger challenge, however, is when someone is trying to find coverage where no coverage was ever intended, whether that's CGL or crime, because they didn't buy something else that would have responded.

Q: What is the "silent cyber" that has been talked about in the industry press recently, and how has it affected traditional lines of insurance?

Couture: "Silent cyber" refers to a policy that had no intention of covering a cyber-type exposure. In the CGL area, there is no intention to cover hacks, but the policy may be pulled into a situation and end up providing a defense. In a CGL policy, there is an ongoing discussion as to whether advertising and personal injury coverage would apply to a hack of personal information or whether a knowing or intentional act of the insured is required and present in a data breach. Then there is the effect of the insured not even being aware of the data security vulnerability at issue. The flip side of the argument is that there's no direct language requiring intentional conduct, so why wouldn't the policy cover something an insured should have protected? There is also an argument as to whether a hacking is the "publication" necessary for advertising and personal injury coverage. A hacker may have access to information, but is that really something that is a publication? Even if a policy has an appropriate exclusion in place today, there may be something new tomorrow that it doesn't address, and so one has to keep abreast of

technology trends and be prepared for the next thing that's coming around.

Cernak: For CGL policies, there has been some exclusionary language produced by ISO, which did two things. One, it made it more difficult to make a claim under these policies. Two, it helped to elevate awareness that people should buy something that provides explicit cyber coverage rather than relying on silent coverage.

Simonson: Silent exposures render every insurer a cyber insurer, whether they think of themselves as one or not. The exposure that a business faces as a result of the internet or other cyber exposures are not limited to coverages that are found under a cyber policy. For example, there can be exposure to Workers' Compensation insurance from the growing number of wearable technology in the workplace, which may generate an uptick in Workers' Comp claims. So whether you issue a cyber policy or not, or whether you intended to cover it or not, you are already in the game.

Q: *Are cyber events impacting D&O Insurance?*

Couture: We've seen shareholders bring derivative lawsuits on behalf of the corporation when there is a data breach. Some allege breach of fiduciary duty, corporate waste, and failure to have the appropriate cybersecurity. There are also situations in which a data breach is announced causing the stock price drop and resulting in a lawsuit. This leads to scrutiny of the security in place at the time and an expectation that the corporation has taken steps to ensure protection of data. We have seen that having a plan and having some cybersecurity and attention to cybersecurity in place has protected many corporations, but not necessarily prevented them from facing a lawsuit. Moreover, the more government agencies that have cybersecurity requirements, the more compliance is a challenge.

Q: *Is there an impact on homeowners' policies?*

Cernak: There are a number of other exposures that present themselves in a home. For example, people may have data breach potential exposure if they volunteer for community activities and collect and maintain information about individuals. Connected devices may be subject to ransomware and extortion threats requiring a coverage response. Thermostats could be held for ransom and cause pipes to freeze, refrigerators could have their temperature be turned up causing spoilage, and connected locks can be opened remotely. In the eyes of a home insurer right now, it doesn't matter if you turn the heat down by walking over to the thermostat or if it is remotely turned down, or if a brick is thrown through a glass window or someone opens the front door remotely to steal your TV. There are also privacy issues, such as TVs and children's toys monitoring activities in the house. People are also using social media to get a sense of when you are home and when you are not, which could lead to increased theft. There is also a need for coverage for cyberbullying, both on the first-party side for resources and costs to help the insured victim of cyberbullying, as well as for cyberbullying liability when someone in the household is perpetrating the cyberbullying. Some of these events can have coverage under a homeowner policy event without explicit coverage, i.e., silent cyber. We haven't seen a great deal of activity yet to carve out those potential coverages from traditional homeowner's policies.

There are a handful of homeowner insurers providing explicit cyber coverage on an endorsement basis. There is also some on-line fraud coverage available. These endorsements look similar to some of the cyber endorsements on commercial lines policies. As homes become more technologically advanced with increased computing power, there is going to be more need for coverage, as seen in commercial lines.

Similar to the commercial side, as people realize the potential exposures and associated lawsuits, you may see activity with insureds seeking coverage under homeowners' policies, and a resulting tightening up of the policy language with either affirmative coverage or affirmative exclusions.

Q: *What about claims by one insurer against another, or between businesses (B2B), arising out of a cyber event? Are you seeing subrogation claims?*

Couture: While we haven't seen a lot of claims between insurers so far, as first-party costs increase there is an expectation that insurers will consider subrogation, for example against vendors who were the conduit to a breached insured's network. Subrogation entails a cost-benefit of available insurance coverage or sufficient assets and whether there is an indemnification agreement. These claims will typically be either for negligence or breach of contract, so the insured will need to prove that the vendor failed to follow a standard of care. That can be a challenge, because not only do the risks and standards of care continue to evolve, but the insured may also be at fault. So if the vendor fails to, for example, update its software or maintain adequate encryption, that scenario may be enough to go against the vendor; but if the insured also fails to train employees on how to avoid a malware intrusion that was a contributing cause to the cyber event, that might be an issue in any subrogation or contribution claim.

Gardere. Solutions tailor-made to fit your legal insurance needs.

Founded in 1909, Gardere Wynne Sewell LLP is one of the Southwest's largest full-service law firms. Serving clients with more than 230 attorneys from three of the largest cities in Texas, as well as Colorado and Mexico, and covering more than 40 different areas of practice, we are noted for our commitment to client service and our ability to assist clients with their most complex and demanding legal and business challenges worldwide.

Gardere's all-encompassing insurance practice offers national and international clients a one-stop shop for all of their insurance needs. From coverage advice to claims litigation to compliance with governmental regulations, our team is uniquely skilled at leading clients safely through the complex world of insurance.

Cyber Risk (continued)

Simonson: Nothing stops claims or suits from determining fault even absent subrogation. For example, I hire a vendor to provide a service, and they do something that causes a breach. I am the one that has to notify those affected and pay notification costs. Nothing stops me from bringing a claim against that vendor myself, apart from my insurer, and hope that they have professional liability coverage in place or the wherewithal to respond. If something happens, and there is breach litigation such as a consumer class action, both the business that breached and its vendor may be named as defendants.

Q: *How are some of the traditional provisions common to insurance policies playing out when applied to cyber risk claims?*

Simonson: Contractual legality exclusions, which are in almost every policy in some form, are an issue. In the payment card industry, liability is assumed by merchants under a chain of agreements that includes a master services agreement with a card brand such as Visa or MasterCard, under which obligations and penalties for a data breach are established via contract. Also, a lot of companies such as vendors are agreeing to pay notification costs on their customer's behalf. So contractual liability exclusions may be problematic in certain situations.

Also, if you look at cyber coverages across the products in the market, you will see varying exclusions relative to internet or other infrastructure outage, failure to have the security protocols that were shown on your application, or failure to meet current security standards. Each carrier may have a different approach to what they consider to be a business risk they may not be interested in covering. So it's really important that purchasers of a coverage pay attention to these provisions.

Q: *How are insurers coordinating their response to cyber-related claims noticed under various lines of insurance?*

Couture: Typically, the cyber claim is the fastest moving of all. Whether the cyber team takes the lead will depend on the facts and lines of insurance available. Regardless of whether they take the lead, they should be helping to coordinate the overall breach response. Overall, the key components are communication, education, and business partnership to get the claim to the right team quickly and ensure engagement of the right resources. With regard to communication, there should be a recognized point of contact for cyber-related matters and issues that everyone in the company should know, to which cyber-related questions and claims get routed. From an education perspective, that includes claim professionals, intake personnel, and pretty much every employee. As we educate employees about basic cyber risks of insurers, it also helps improve the quality of service to the insureds as employees will understand what the risks are. Business partnerships are important, including working with brokers, agents, and insureds to understand the insured's insurance profile when there is a possible cyber incident that could impact multiple policies. Brokers can help when they are reporting a claim by identifying other policies and providing basic information at their disposal.

Simonson: Another challenge is that we can't always predict how the insured will report a claim. So it's important that the insurer recognize certain tag words to identify cyber claims from an insured, who is used to reporting slip and fall claims under a GL policy. How swiftly the insurer distinguishes the cyber claim and involves the cyber group prevents a delay in handling the claim and relieving angst internally and externally.

Cernak: Building on that, another thing an insurer can do is identify examples of types of losses that could eventually turn into, but may not be initially, a cyber loss. For example, someone calls in and reports a claim for stolen computers as a property loss. They may not recognize that they may also have a data breach from personal information on the stolen computers that wasn't encrypted.

Q: *What about aggregation of risk when a cyber risk falls under may different policies or impacts many insureds?*

Cernak: The first step is acknowledging that the potential for aggregation of risk really does exist in cyber and is not as easily addressed as under other lines of business. For example, if you feel you have too much exposure to Atlantic hurricanes, you just stop writing on the Florida coast and start writing elsewhere. For cyber, you don't have that luxury; there is no place to hide from cyber exposure. We saw a small glimpse of what can happen last fall when a DNS provider was brought off-line for a bit. We have seen localized mini-accumulation events where a service provider's clientele list was apparently breached and a vulnerability was discovered in how they set up systems, and the hacker targeted the entire clientele list with the same type of attack.

The struggle, though, is how do you know what an accumulation event will be if you haven't ever seen one? Data on that is limited and the data we are collecting today doesn't reflect the risk five or ten years from now.

We are seeing certain mechanisms that facilitate aggregation, such as denial of service attacks, which are going to become larger and more common. These attacks are going to use larger networks and more computing power and will be increasingly automated. When denial of service attacks are targeted at entities upon which a number of businesses rely,

Morris, Manning & Martin, LLP

A Law Firm with National and International Reach

Moving Forward. Meeting Goals. Progress Realized.

Our lawyers can help you with:

- Regulatory issues applicable to run-off business and associated transactions
- Assumption reinsurance and loss portfolio transfers
- Tax issues associated with run-off transactions
- Litigation and arbitration of insurance, reinsurance and agency matters

Lew Hassett
Co-Chair

404.504.7762
lhassett@mmmlaw.com

Robert "Skip" Myers Jr.
Co-Chair

202.898.0011
rmyers@mmmlaw.com

Ward Bondurant

404.504.9532
wbondurant@mmmlaw.com

Jessica Pardi

404.504.7662
jpardi@mmmlaw.com

Joe Holahan

202.408.0705
jholahan@mmmlaw.com

Tony Roehl

404.495.8477
troehl@mmmlaw.com

Cyber Risk (continued)

that's when you start to get some of that accumulation concern.

Couture: We have some ability to do claim coding to track what's coming in. The key to tracking accumulation is also communication with the different areas within the insurer's claims operation as well as actuary, underwriting, and risk control teams. Finally, one should stay abreast of technology and the areas it impacts. You need to have a commitment to continually educate yourself and those around you.

Cernak: People are starting to talk more and more about a common terminology and coding, but what do you do with that information once you have it? That's where people in the industry are still struggling.

Simonson: We need to develop tools that help us understand our potential aggregation exposure, but how do we do that? We can review our exposure limits and we can review the potential impact of a single event on our book of business, but there is still a lot more work to be done to capture the reality of the risk. We need to plan for the worst case scenario, and walk through "what if this happens, would this policy apply?"

Q: *What about reinsurers, what challenges are they now facing?*

Cernak: Many of the same challenges facing direct carriers also apply to reinsurers, just with a multiplier on it. A lot of the same issues of understanding what is actually being covered, and in how many places apply to reinsurance. A reinsurer can have accumulation vertically on a single risk, or horizontally across multiple risks. As there are ever larger towers of insurance being constructed, there are only so many reinsurers in the market assuming some of this cyber risk, and thus knowing which layer you are on and how many times you are being approached by different carriers on the same tower is key to assessing risk accumulation.

Q: *What do you see as the challenges and cyber risks coming down the road that our current policies may need to face in the next year or so?*

Simonson: The biggest challenge we are going to face is responding to the connectedness of everything. We may not realize the implications of "unlocking our doors remotely," or the risks we are exposing ourselves to when we download a simple app. Who knew my smart TV was always listening? We need to watch the technology trends and anticipate what the risk to insurance companies may be. We hear much more about whether devices that are connected to the internet should be regulated and designed so they are secure, and whether the companies are living up to the security promises they made, the basis for recent FTC investigations. Insureds and insurers that are used to dealing with manufacturing defects may have to deal with these issues, but it's really not the device that fails, but it is also doing something else that impacts people in a way they don't like. While regulations may be increasing, what does full compliance mean in this context? How do we comply with regulatory provisions such as those in the EU's General Data Protection Regulation effective next year that includes a right-to-be-forgotten provision? As regulations shift to protect privacy, there is a whole different type of compliance that a lot of companies in the United States, which aren't used to such provisions, are going to need to address.

Cernak: I think the whole concept of trust, and what and who you trust and how that can be exploited, is an area to focus on in the future. Trust is going to carry more value as things become more connected, and how does one know who to trust? Right now, a lot of the lawsuits relating to breaches are predicated on the promises made by companies to keep data safe and secure, as contained in privacy statements.

Couture: That's a good point, and it is especially timely now with all the devices listening in. Additionally, there is the question of which companies to trust to keep the information they collect safe and private and stored for a limited time.

Q: *Last tips?*

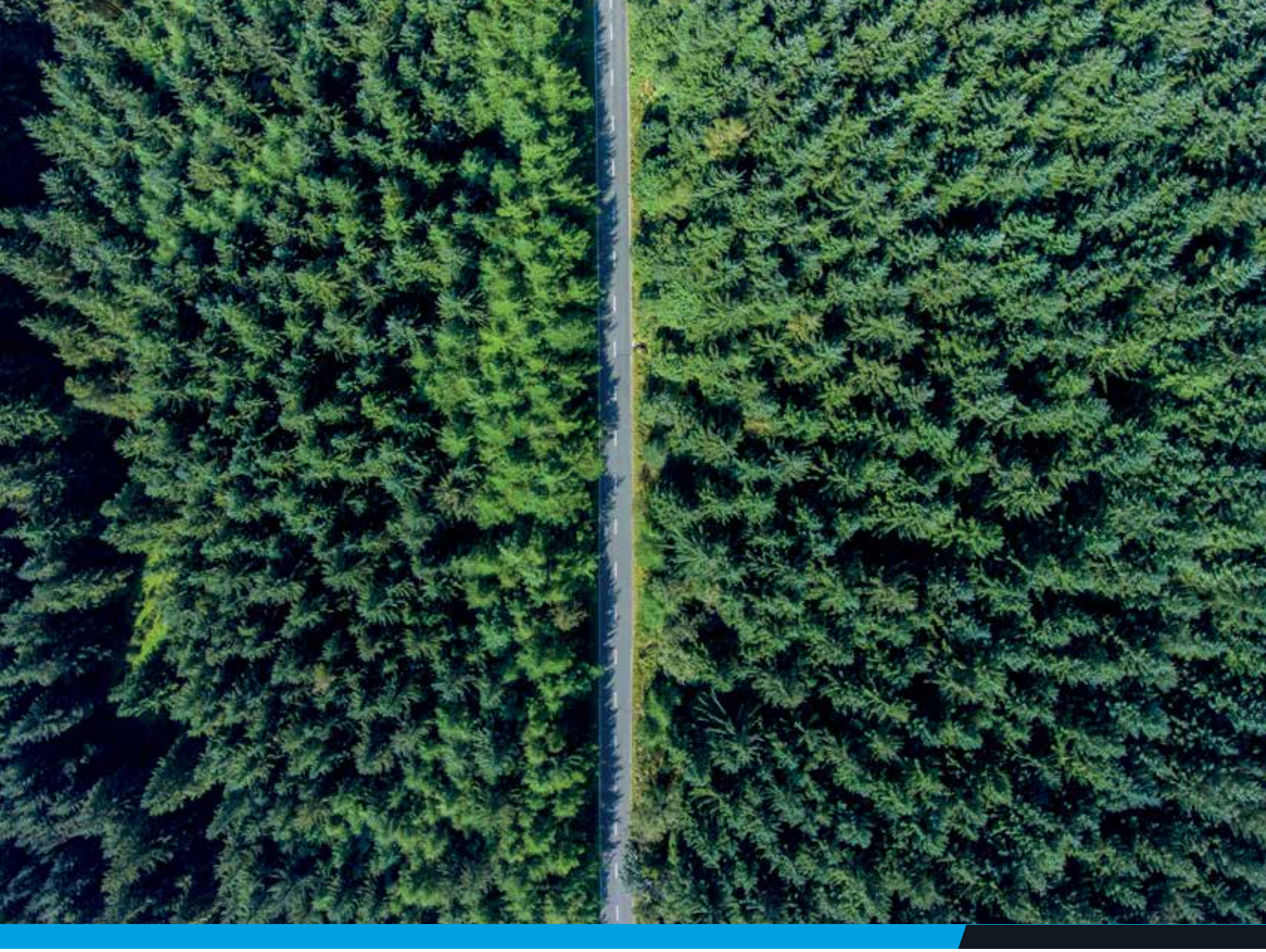
Cernak: Keep abreast of everything, and know your policy language and intent, so you understand what you've written. Be paranoid.

Couture: Have a commitment to continuous education in cyber risks all around.

Simonson: Be involved in one of the numerous information sharing associations focused on cyber risks. ●

Laurie A. Kamaiko is a member of Sedgwick's Cyber-security and Privacy leadership team as well as a member of the Insurance Division. laurie.kamaiko@sedgwicklaw.com

Bina T. Dagar provides re/insurance clients industry best practice solutions and dispute resolution; and also conducts underwriting and claims audits. bdagar@ameyaconsulting.com



/ We simplify the complex

Carroll McNulty & Kull has now merged with international (re)insurance law firm Kennedys. Creating a global reinsurance and insurance coverage and defense practice that will offer clients exceptional coverage and expertise in all our key markets, we've significantly enhanced our presence across the Americas, Europe, Asia-Pacific and the Middle East. Our core business remains (re)insurance: acting for global and domestic (re)insurers, and multi-national corporations.

1,700+
people currently making a difference to our clients

47
offices, associations and cooperations around the world

18
countries in which we have an office

kennedyslaw.com

Kennedys CMK

Twisting in the Wind

Frederick J. Pomerantz

Covered Agreement Dangling by Uncertainty and Politics

On January 13, 2017, the United States and the European Union (EU) concluded negotiations on the first insurance covered agreement after this novel multilateral international agreement, envisioned and promoted by the National Association of Insurance Commissioners ("NAIC") and the U.S. state insurance regulators who are its members, was authorized by Title V of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111-203, signed by the President and effective in July 2010) (the "Act").

The complete title of the document is the Bilateral Agreement Between the European Union and the United States of America On Prudential Measures Regarding Insurance and Reinsurance (the "Covered Agreement").[1]

One of the principal goals of the Covered Agreement is to affirm the authority of the Federal Insurance Office ("FIO"), also established by the Act within the United States Department of the Treasury, to preempt state laws that are inconsistent with the Covered Agreement and may result in less favorable treatment for foreign insurers. Such preemption, however, may not apply to any state insurance measure that "governs any insurer's rates, premiums, underwriting, or sales practices." Although the FIO and the United States Trade Representative ("USTR") must consult with Congress on the negotiations, the Act does not require specific authorization or approval from Congress for the covered agreement to take effect.[2]

FIO's function is primarily designed to gather information, monitor trends in the insurance industry, and provide advice to the industry. While the FIO has no regulatory authority *per se*, it represents the United States in international negotiations with respect to insurance regulation and has a seat on the executive committee of the International Association of Insurance Supervisors.[3]

The U.S.-EU Covered Agreement was submitted to the House Committees on "Financial Services" and "Ways and Means," as well as the Senate Committees on "Banking, Housing, and Urban Affairs" and "Finance" on January 13, 2017 and subsequently both held subcommittee hearings on the Covered Agreement. A 90-day congressional waiting period mandated in the Act has concluded but, to date, the United States has not officially signed the Covered Agreement. The EU's European Council authorized the signing of the Covered Agreement and asked for the European Parliament's consent to adopt it as official policy.

Although the Trump Administration has not indicated whether it favors or disfavors the Covered Agreement, it has alternatively signaled its intention to repeal and replace major portions of Dodd-Frank as a part of its financial services deregulatory push, in particular with respect to the provisions of Dodd-Frank that affect banking, but also insurance to a lesser degree.[4]

…to date, the United States has not officially signed the Covered Agreement.

Less than nine years after the Wall Street meltdown, on June 8, 2017, the House of Representatives voted to pass H.R.10 - 115th Congress (2017-2018): the Financial Choice Act of 2017 (the "Choice Act"). While the Choice Act is widely viewed to be "dead on arrival" in the Senate, some parts of the legislation may end up surviving. The bill's architect, Rep. Jeb Hensarling (R-TX), claimed that it will "end bailouts once and for all" because the legislation would take away the post-crisis powers granted to federal authorities to help them deal with a financial emergency like Lehman Brothers, AIG and parts of the U.S. auto industry.[5]

A portion of the Choice Act, known as Orderly Liquidation Authority, allows regulators to resolve a failing financial firm. It is similar to how the FDIC handles failing banks. Conservatives argue that these emergency powers in Dodd-Frank have made "Too Big To Fail" a permanent policy by implying the federal government will always be ready to bail out financial institutions that, through their own risky behavior, find themselves in existential danger.[6]

According to the United States Trade Representative ("USTR") and Michael McRaith, a former Illinois Insurance Director who was named to the post of Director of the FIO, who together negotiated the terms of the Covered Agreement with their counterparts in the EU, the Covered Agreement most significantly:

1. allows U.S. and EU insurers to rely on their home country regulators for worldwide prudential insurance group supervision when operating in either market;

2. eliminates collateral requirements for EU reinsurers and local presence requirements for U.S. reinsurers meeting certain solvency and market conduct conditions; and

3. encourages information sharing between insurance supervisors.[7]

McRaith resigned his post as FIO Director effective upon the inauguration of President Trump.[8]

However, much to the chagrin of U.S. state insurance regulators and certain insurance trade associations, and unlike the goals expressed to Congress by the NAIC when negotiations began with the EU following an announcement by the NAIC on November 15, 2015,[9] the Covered Agreement does not explicitly call for "equivalency recognition" of the U.S. insurance regulatory system by the

Twisting in the Wind (continued)

EU. Thus, the Covered Agreement's required 90-day waiting period concluded on April 13, 2017 and still is not in effect at this time.

Since January 13, 2017, there have been a number of significant developments, signifying a notable cooling of enthusiasm by some of the trade associations representing different segments of the insurance industry, by state legislators through NCOIL and the state insurance regulators through the NAIC, in some instances openly disagreeing with former FIO Director Mc Raith's interpretation of key portions of the Covered Agreement. In the Center for Insurance Policy and Research newsletter dated March 2017, NAIC President and Wisconsin Insurance Commissioner and NAIC President Ted Nickel openly challenged some of the assurances offered by McRaith:

> State insurance regulators were told by the negotiators the two goals of the process were to gain equivalence for the treatment of U.S. insurers operating in the EU and recognition by EU of the U.S. insurance regulatory system. In my view, neither was clearly resolved in the Covered Agreement.
>
> Fellow regulators and I are concerned with the disparate treatment some EU jurisdictions are imposing on U.S. insurers. State insurance regulators are committed to reaching accord on a system of mutual recognition without any jurisdiction imposing its values and regulatory systems on another. Both U.S. and EU insurers deserve to receive fair and equal treatment. There should be no disadvantage to an EU insurer doing business in the U.S. Similarly, a U.S. insurer should not be disadvantaged when it operates in the EU.[10]

A portion of the Choice Act, known as Orderly Liquidation Authority, allows regulators to resolve a failing financial firm.

To further call the attention of Treasury to those claimed disparities, on March 15, 2017, state insurance regulators and the NAIC wrote a letter on the Covered Agreement asking the Treasury to work with the EU to clarify details of the Covered Agreement and also to offer technical assistance and expertise.[11]

The National Association of Mutual Insurance Companies ("NAMIC") issued a statement immediately following the announcement of the Covered Agreement, as follows:

> The Covered Agreement announced today was conceived in Dodd-Frank as a proposed solution to an invented problem—the question of European regulators deeming our regulatory system equivalent. Because the agreement has the authority to pre-empt U.S. insurance law and regulation, this agreement must meet a very high standard. Setting aside the specific elements of this agreement, which we'll comment on once our analysis is complete, we note that some provisions appear to be temporary and several areas are ambiguous.[12]

Shortly after the Covered Agreement was concluded, NAMIC delivered its verdict:

> "NAMIC has had deep concerns that a covered agreement, a deal made behind closed doors that needs no legislative approval to implement, had the potential to significantly alter or preempt aspects of the state-based system of insurance regulation," Chamness said. "Unfortunately for the vast majority of NAMIC members and their customers, those concerns have been realized."
>
> Equivalency for U.S. regulation was among the chief priorities outlined by the Federal Insurance Office in announcing negotiations for the covered agreement. The FIO was given authority to negotiate covered agreements under the Dodd-Frank Act,

Endnotes

1 Covered Agreement Text

2 F.J. Pomerantz, Uncovering the Agreement, www.insuranceday.com, 29 April 2016

3 F.J. Pomerantz, EU-US Covered Agreement On Reinsurance Collateral: Possible Impact On Surplus Lines?, FORC Journal, , Vol. 27, Edition 1, Spring 2016

4 B. Webel and R. Fefer, What is the Proposed U.S.-E.U. Covered Agreement?, CRS Insight, June 9, 2017

https://fas.org/sgp/crs/row/IN10648.pdf

5 M. Egan, The Most Dangerous Part About Killing Dodd Frank, CNN Money, https://tinyurl.com/y7bola6w, June 12, 2017

6 On June 11, 2017, a report by the U.S. Treasury Department to the President entitled A Financial System That Creates Economic Opportunities Banks and Credit Unions was released. It provides a cabinet level justification for the portions of the Choice Act that eliminate government bailouts of failing financial firms. The Choice Act, however, preserves most of the features of Dodd-Frank that impact the regulation of insurance. Id.

7 Supra fn. iii

8 Federal Insurance Chief McRaith Leaving Post on Jan. 20, Insurance Journal, January 6, 2017

9 http://www.naic.org/newsroom_statement_151120_statement_on_covered_agreement_negotiation.htm

10 http://www.naic.org/cipr_newsletter_archive/vol21.pdf

11 http://www.naic.org/documents/2017_naic_letter_to_treasury_on_covered_agreement.pdf

12 https://www.namic.org/newsreleases/170113nr06.asp

13 https://www.namic.org/newsreleases/170216nr01.asp

14 Q &A: What Britain Wants From Europe, BBC News, Feb. 17, 2016; http://www.bbc.com/news/uk-politics-32695399, cited by the author, supra, fns. 2 and 3.

15 Numerous federal agencies, including the Consumer Financial Protection Bureau and the Financial Stability Oversight Council, are funded solely through fines and fees and receive no annual appropriations from Congress, resulting in almost no congressional involvement in the way these agencies are run.

The Agency Accountability Act seeks to correct this problem by requiring that (with limited exceptions) any fees, fines, penalties, or proceeds from a legal settlement be deposited into the Treasury's general fund. https://tinyurl.com/y75zd4ww

and the agreements do not require congressional approval. In his testimony, [NAMIC President and CEO Charles M.] Chamness noted that even negotiating for mutual recognition represented a concession to the EU.[13]

Finally, the objectives of the United Kingdom in its Brexit referendum and Article 50 notice of intent to withdraw from the EU may clash with the goals of other EU nations, such as France and Germany, possibly leading to referenda in either or both of these original EU nations and, conceivably, the disintegration of the EU, with potential adverse consequences not only to Lloyd's syndicates but also to certified reinsurers from France and Germany.[14]

Thus, with the benefits to U.S. insurers and reinsurers of the Covered Agreement subject to conflicting interpretations, with the FIO facing elimination and with the powers of the Consumer Financial Protection Bureau ("CFPB") set to be diluted by the Choice Act, upon passage,[15] and with the designation of AIG and Prudential as "systemically important financial institutions" already having been eliminated by Presidential Executive Order (and, therefore, no longer applicable to any U.S. domestic insurer) it is easy to see that the viability of the Covered Agreement could be in question for the foreseeable future. ●

Fred Pomerantz co-Chairs the Goldberg Segalla Insurance Regulatory Practice and participates in its Reinsurance and Corporate Transactional practices. fpomerantz@goldbergsegalla.com

AIRROC's 13th Annual

NJ Commutations & Networking Forum

The Heldrich Hotel & Conference Center, New Brunswick, NJ
October 16-19, 2017

Mark your calendars: AIRROC's biggest event of the year will be held from Sunday, October 15 to Wednesday, October 18, 2017.

The AIRROC Board of Directors looks forward to seeing you at The Heldrich Hotel and Conference Center in New Brunswick, New Jersey.

The Heldrich is less than 40 minutes by train from New York City, and boasts a large number of restaurants and shops within walking distance, as well as the full service amenities expected from a fine hotel. "We chose The Heldrich as our host again this year in response to the extremely positive feedback that we received from AIRROC's members and delegates. Not only does it offer beautiful facilities and rooms, but it is an easy commute from Manhattan as well as the major airports," said AIRROC's Executive Director, Carolyn Fahey.

The event offers many features that continue to make it an industry "must -attend." Delegates benefit from two full days of reserved networking tables on Monday, October 16 and Tuesday, October 17. "We already have more than 60 companies represented among the delegates registered," said Fahey.

Monday's schedule is a busy one with a full day of education and a diverse set of faculty and topics of interest to AIRROC's members. On Monday evening, AIRROC will host a reception and dinner at the famous Zimmerli Art Museum, a short distance from The Heldrich. Here, AIRROC will announce the 2017 Person of the Year as well as the recipient of AIRROC's 2017 Trish Getty Scholarship.

Tuesday again provides for the opportunity to schedule meetings all day with other event attendees in order to progress matters between companies. There will also be a two-hour cocktail reception early on Tuesday evening for all meeting attendees.

We will adjourn at noon on Wednesday October 18.

Go to www.airroc.org and register now!!!!!

See you at AIRROC NJ 2017!

Ed Gibney, Event Committee Chair

2017 REGISTRATION RATES

- AIRROC Members get one free registration per company; additional delegates from member companies pay only $695 (after September 15, $795)
- AIRROC Corporate Partners can register at the member rate of only $695
- Non-member rate is $995 (after September 15, $1095)
- Monday Education Sessions only, $295 for members and $495 for non-members
- Monday evening dinner only, $250 for members and non-members
- Meeting table reservation fee is $500 for members and non-members

Sponsorship opportunities are available. Please contact Carolyn Fahey at carolyn@airroc.org for more information.

"Eyes-On" Management

Watch Lists for Effective Management of Significant P&C Insurance Risks

All insurance and reinsurance companies want to avoid public disclosures or headlines regarding significant reserve increases, such as the recent newsworthy reserve adjustments that more than a few companies have taken for asbestos, silicosis, or other large tort liability claims. But how? The secret lies in the early identification of "bad" claims when there is time to alter the claims handling approach and minimize the company's exposure.

Throughout the property/casualty (P&C) insurance industry, prescient companies use watch lists as a tool for the proper management of these claims and to enhance operations from underwriting and actuarial to financial reporting. Most companies would agree that using watch lists is a good approach, but establishing a watch list process, identifying which claims to include and deciding how to handle those claims, once identified, often is a challenge.

What is a Watch List and how do P&C Insurers Use Them?

Merriam-Webster defines a watch list as follows:

"A list of people or things that are being closely watched because they are likely to do or experience bad things in the future."

Similar to the Federal Bureau of Investigation's watch list for terrorists and professional sports teams' scouting watch lists to identify potential team additions, the P&C sector's watch lists identify exposures—claims, claim notifications or potential future claims—to monitor closely. By placing greater focus on these claims, a company can enhance the handling of these claims to mitigate their financial impact, alter underwriting and pricing approaches appropriately, and provide greater transparency in the reserving and financial reporting process.

Watch lists often act as an early warning system to flag potentially large claims, streamline the assignment of claims handling and legal resources with the appropriate level of expertise, and determine appropriate pricing and reserving treatment in the actuarial analyses. For those watch list exposures that arise from an observation of industry events for which claims have not yet been reported, a watch list facilitates a more thorough understanding of a company's exposures, including the potentially impacted lines of business, the limits exposed, and any pending litigation.

Effective use of watch lists can have an impact throughout the organization well beyond the claims department. In fact, the impact can certainly reach the underwriting, actuarial, marketing, ceded reinsurance departments, and —depending on the magnitude of the exposure—even the c-suite. Below are some examples of how insurance companies utilize watch lists to impact strategies, operations and financial results.

What Information does a Typical Watch List Include?

Routine, high frequency claims do not warrant special focus or monitoring and, as such, do not belong on a watch list. Rather, watch lists typically contain claims with unusual exposures or catastrophic potential; specific characteristics may include:

- Significant loss potential, either high severity for an individual claim or an aggregated group of low severity claims, e.g. class action;
- Unusual exposures, or those that are not well represented in the historical data;
- Heavily litigated exposure; and
- Claims with questionable insurance coverage.

Some watch lists include only incurred claims—those that have already been reported and recorded in the claims system; however, a watch list also may include potential claims, which relate to incidents or exposures that may lead to an incurred claim in the future. A company should separately monitor and track potential claims to allow for early identification of incidents that may develop into significant claims. Separate tracking of potential claims affords the actuaries the ability to treat potential

Managing a New Claim Exposure: An Example

An insurer provides excess hospital and medical professional liability coverage to healthcare providers that are utilizing an innovative surgical technique to implant a newly designed pacemaker into patients.

The risk… The new device and procedure introduce the potential risk of claims and complex litigation to the liability insurer of the hospital and medical professionals as well as the device manufacturer.

Mitigating the risk… The insurer adds this claim type to its watch list to increase monitoring of this exposure and enhance its case reserve and actuarial IBNR estimation approach and financial reporting. The watch list approach will aid the insurer in recognizing the associated losses earlier, which facilitates improved litigation strategies that may reduce the company's exposure.

claims differently in the IBNR reserving process.

Common Watch List Exposures

Perhaps the most common exposures included on P&C insurance company watch lists relate to asbestos and environmental pollution exposures. The external environment largely is responsible for driving these costly claims into the forefront for insurance companies who unknowingly insured these exposures at the time the policies were written.

Once thought to be a miracle mineral, asbestos was used extensively in the construction of homes, commercial buildings and ships from the mid-1960s to the mid-1980s. By the mid-1980s, health concerns related to exposure during the installation and removal of asbestos products had come to light. Insurers had unknowingly insured asbestos liability exposures or found themselves with significant occupational disease liabilities stemming from the adverse impact on the health of individuals who had worked with asbestos materials. As such, from the mid-1980s through the 1990s, asbestos claims were, perhaps, the most common exposures on P&C insurer watch lists. Also during this time, the health effects of hazardous wastes became a common headline. Environmental pollution and Super Fund site remediation exposures became common inclusions on P&C watch lists as well.

Another telling and more recent example is the 2008 financial crisis and the increase in professional liability claims that accompanied it. These claims arose from directors & officers (D&O), errors & omissions (E&O) and fiduciary coverage, had complex legal issues, and were a classic example of low frequency/high severity claims that are difficult to estimate. These claims are not uncommon on P&C insurer watch lists today. Further, with the growth of cyber liability coverage and the numerous high profile lawsuits to-date, many P&C insurance companies with such exposures are beginning to monitor cyber liability claims on their watch lists.

Claims Management	Identification of claims with significant loss potential early in the life of a claim allows the claims department to handle the claim proactively and establish an appropriate litigation strategy. Doing so can reduce the loss potential of the claim and avoid unexpected adverse reserve development and stair stepping of reserves.
Industry Trends	Maintaining an awareness of trends in the industry may help an insurer identify potential exposures from existing policies, allowing it to employ targeted claims management strategies and reduce its loss exposure.
Underwriting / pricing / marketing strategy	An insurer may decide to discontinue an unprofitable book of business, add exclusions to its policy language or target a different segment of customers. Correcting underpricing soon after the identification of a significant loss exposure will help to reduce the impact of related claims on the insurer's financials.
Reinsurance	Today's leading practices suggest addressing both gross and net exposures related to watch list claims. This approach is particularly important for companies with complex reinsurance structures. The additional focus facilitates timely notice of loss to reinsurers and appropriate recognition of any reinsurance coverage in the financial reporting process.

Insurers have seen significant improvements in exposure assessment and claims management through the effective use of watch lists for asbestos, pollution, and other health hazard exposures. In large part due to the success of watch list tools utilized for these coverages, insurers have expanded their watch lists to cover a variety of other exposures, such as excess liability, directors and officers (D&O), and cyber risk. Due to the emerging nature of these exposures, time will test the effectiveness of closely monitoring the related claims and exposures.

Insurers seeking to be proactive in mitigating their exposure to significant claims and refining their underwriting and pricing strategy should consider utilizing watch lists to place more focus on monitoring these exposures. Establishing a watch list process and identifying claims to include on a watch list can be overwhelming, and a watch list process requires ongoing review to ensure that the focus remains appropriate as new exposures emerge. Insurers often find that leveraging the expertise of an integrated actuarial and claims consulting team provides useful insights, streamlines the process of establishing an effective watch list process and reduces the burden on internal resources. ●

Barbara K Murray, Director at PwC Actuarial Services. barbara.k.murray@pwc.com

The Legacy Market

Strength. Stability. Transparency. Certainty. That Order.

In a world where "strong and stable" equates to weak and uncertain, the European legacy market remains strong and stable (as defined by the Oxford Dictionary), transparent, and continues to deliver Certainty (the capital C is not a typo!) and a cleaner, leaner and stronger balance sheet to each carrier that engages in the process through the implementation of the most appropriate "finality" solution.

In the Spring 2017 issue of AIRROC Matters, we discussed the various exit and capital release tools available to the European insurance market (and until a hard, soft, or medium exit is finally negotiated, we will continue to include the UK in the European market) with each providing different degrees of finality and capital relief. In this second of three articles, we will discuss the first finality statute available in the U.S. and steps taken by other U.S. states to adopt a similar framework. We will also briefly look at how these compare to what is available in Europe.

The way we are

The continued lack of investment returns, the need to ring-fence exposure, the more stringent regulatory obligations coupled with the additional capital required to simply operate and write the same level of business; each continues to drive the search for ways with which to limit an insurer's exposure to the unknown or uncertain and to deliver value to the shareholders. Large groups with no capital issues or regulatory pressures continue to use the various exit tools we discussed in the Spring issue as a key strategic management tool employed to deliver value to their management and shareholders. At the same time, sadly, there is a continuing perception among smaller carriers and, surprisingly, in large and developed markets that the disposal of a book of business or the transfer of older underwriting years is a sign of weakness or failure or a discussion in which one would engage at the brink of insolvency. We, as a legacy market, still have a lot of work to do to educate the wider insurance community and potential clients across Europe and the U.S. of the fact that we are not quasi-liquidators.

Anything is possible – a contagious state of mind

One cannot underestimate the difficulty of achieving a uniform legal framework where different state systems are involved. In Europe, we know this only too well. The implementation of Solvency II, the years that it took to get there, and the consequent costs have been phenomenal. But it was possible.

In the U.S., an analogous challenge exists where insurance regulation is state-based. In order for concepts such as portfolio transfers to work efficiently and on the same basis (so that they would be supported and accepted rather than challenged) there must be a federal or quasi-federal approach, some level of equivalence, and reciprocity.

The various state economic interests, the fact that some commissioners are elected and some are appointed, the concentration of insurance companies in some states more so than in others, among other reasons, give weight to the position that achieving a federal or quasi-federal legal framework for perhaps some but not all elements of insurance and reinsurance regulation would be impossible.

But for a global industry that proved its ability to maintain strength and stability through various economic crises and adapted its practices and offerings through extraordinary innovation and vision, anything is possible. If 28 EU member states of different economic strengths, languages, religions, and cultures achieved the adoption of uniform (but admittedly, not always perfect) legislation, surely, this could also be possible in the U.S.

USA Today

In August 2015, Rhode Island became the first U.S. state to provide a legal framework, which provides legal and economic finality to a carrier wishing to transfer a part of or its entire portfolio. Rhode Island's Regulation 68 ("Regulation 68") mirrors the UK framework which requires that any portfolio transfer must receive judicial approval before it becomes binding on all affected parties. In all other EU member states, with the exception of the Republic of Ireland (depending on what type of portfolio is subject to transfer) where any transfer must be approved by both the Central Bank and the Irish High Court, the approval of the regulator is sufficient to give the transfer in question a legally-binding effect. Once a portfolio transfer is approved, the transfer is complete and there can be no challenge of the transfer or recourse to the original insurer. And here lies its unique position in our toolbox of finality solutions: it is the only tool that offers complete legal and economic finality.

As insurance regulation in the U.S. is state-based, an important element of any transfer approval is that this receives "full faith and credit" in other states. In simple English, this means recognition and enforceability. The requirement for court approval of any transfer gives the transfer the weight it needs to receive that recognition. Such recognition is not automatic but, as a general statement, there is a presumption that a court decision in a U.S. state is delivered properly and should be recognised and enforced by other states. From an economic point of view, the requirement of an independent actuarial report provides comfort to the court that a thorough review of the economics of the portfolio has taken place.

Under Regulation 68, only commercial P&C books of business are eligible for transfer. Personal lines are excluded; however, reinsurance of personal lines is eligible for transfer. A strict timetable from the date of the provision of the Insurance Transfer Business Plan is provided for and even though the requirement for court approval adds to the time required to complete a transaction, RI's judicial "business calendar" provides some comfort to an efficient process. Once a portfolio is identified for transfer, the transferor should engage its own regulator as early in the process as possible. Early regulatory engagement ensures earlier resolution of any issues and a smoother process. The domiciliary regulators would need to consent to the transfer and the RI regulatory team will need to work closely with the domiciliary regulator (and, depending on where the risk is located, a number of regulators may be involved), in order to address any issues and concerns that may arise in the process.

Once a portfolio is identified for transfer, the transferor should engage its own regulator as early in the process as possible…

Assuming the transfer is approved, an already existing RI carrier can be used to receive the portfolio. Alternately, the portfolio can be transferred to a cell of a Protected Cell Company, which is a mechanism that allows disparate books of business to be acquired. Those books may then be reinsured in whole or in part. This also allows investment by non-insurers into a space which provides steady growth.

At the time of writing, there has yet to be a transfer under Regulation 68, but it is undoubtedly the case that the market on both sides of the pond is excited by the availability of a progressive step that provides the framework to transform a market with enormous potential.

There may be a momentum?

Following RI, two other states introduced their own statutes to provide similar solutions. They both appear to lack certain elements of Regulation 68, which may impact on the willingness of the market to use them as well as their enforceability. However, as these frameworks, including Regulation 68 are new to the U.S. market, all is a matter of speculation and healthy debate.

The Connecticut Act will be effective on October 1, 2017 and does not appear to be limited in scope. An insurer may submit a plan of division (of liabilities and assets) by legal succession to a new legal entity rather than a direct or indirect transfer. The plan of division must first be approved by the dividing insurer and then by the commissioner following a public hearing, if one is felt to be required. Following approval, each resulting insurer is issued a license.

The Oklahoma Bill is expected to become effective on November 1, 2017, but as it is still in draft form, it is subject to change. As it currently stands, the Bill only applies to run-off businesses (excluding life, personal lines, and workers compensation) that wish to submit a Commutation Plan to extinguish their run-off liabilities. It also applies to an Oklahoma-domiciled insurer formed or re-activated for the sole purpose of entering into a voluntary restructuring of its business. The approval process is similar to that applied in the UK in relation to Schemes of Arrangements. The Plan needs to receive the support of 50% of each class of creditors and the holders of 75% in value of the liabilities owed to each class.

Each statute has differences in scope, approval process, and documents to be submitted for approval. However, they all have one core requirement and without which no transfer may be approved: the interests of the policyholders are paramount and the solvency of the transferee insurer will be a key consideration in the approval process no matter which state commissioner is concerned.

You say tomato and I say tomato…

It is undoubtedly the case that the Regulation 68 is a major step in the right direction and that, given the interest shown so far, it is likely that more states will follow with similar statutes. It is also likely that adoption of similar regulations by other states will neither come quickly nor in identical form, as experience has shown so far.

Go-to firm for reinsurance disputes in Philadelphia

- Chambers USA 2016

There's a reason we've been called a go-to firm for reinsurance disputes.
We understand the business of insurance and draw on years of experience applying strategic focus to uncover the nuances in each case.

Our reinsurance group balances aggressiveness and efficiency.
We counsel clients to avoid disputes before they develop, but if that's not possible, we possess the trial and arbitration experience necessary to bring the matter to resolution.

White and Williams LLP

Delaware | Massachusetts | New Jersey | New York | Pennsylvania | Rhode Island

whiteandwilliams.com

The Legacy Market (continued)

Europe (particularly the London market) has been engaged in these transactions for decades and the uniformity across the EU member states ensures that there is a level playing field, a necessary ingredient for business success. Jurisdiction arbitrage would have resulted in unfair competition and pricing. The fact that three out of fifty states offer a framework for exit solutions means that an insurance commissioner of a state without such a framework may see the potential transfer of business from his state to another as disadvantageous from an economic and/or business perspective. Federal legislation would ensure that every state can dispose of and receive legacy business in this way and opportunities would truly go where they are best suited.

Insurance language, terminology, underwriting principles, and claims processing are very similar on both sides of the pond. How we deal with legacy, however, is somewhat different.

The fact that three out of fifty states offer a framework for exit solutions means …

Some food for thought?

- Does the U.S. insurance market need finality solutions that provide the "whole package" of absolute legal and economic finality? Or are the traditional solutions of LPTs and mainstream reinsurance arrangements enough?;
- Is EU-style finality achievable in the U.S. without a federal approach and legislation?;
- Is it likely that the U.S. market will see the need and practicality of a uniform approach across the U.S. to the point that national bodies such as the NAIC will take it upon themselves to make this a priority?;
- In light of pressures on the U.S. market, such as further waves of asbestos and concerns over long-term care, can the market afford to wait for a federal legal framework for portfolio transfers such as the one that the EU enjoys? Or will it have to do the best it can with a disparate system?;
- If the EU, with 28 member states of different cultures, languages, and business practices could reach harmonization for a core pillar of its economic growth, why can't the U.S. achieve this on the federal level? ●

Eleni Iacovides, Group Chief Client Officer at DARAG Group Ltd.
e.iacovides@darag.eu

ACCELERATE
CHANGE
MITIGATE RISK
IMPROVE RESULTS

Drawing on our Restructuring heritage to unlock value for runoff operations.

A&M drives Performance Improvement through strategy, operations and analytics.

We provide Regulatory Support to navigate complex and challenging environments.

Whether an on-going or runoff company, the biggest risks are often what you don't know and can't see. A&M's Insurance and Risk Advisory Services uncovers where potential risks lurk across insurance firms and effectively diagnoses the cause of underperformance. Our multidisciplinary experts apply vast industry experience to create insights and solutions that mitigate the risks and accelerate your transformation or runoff strategy and performance.

Visit us online at **www.alvarezandmarsal.com/insurance** or call **Rudy Dimmling** at **+1 212 328 8541**.

49016

A&M
ALVAREZ & MARSAL

Freeborn

Your Future Is Our Purpose

Strength in Numbers

Meet One of the Largest & Fastest-Growing Specialist Reinsurance Teams:

- Reinsurance Dispute Resolution
- Insurance Coverage Litigation
- Corporate & Regulatory Insurance
- Insurance Insolvency
- Complex Commercial Litigation
- International Arbitration

Chicago | Springfield, IL | New York City | Richmond, VA | Tampa, FL

Visit us at freeborn.com

Joe McCullough | +1 312-360-6327 | jmccullough@freeborn.com

Daniel Hargraves | +1 212-218-8766 | dhargraves@freeborn.com

USF&G v. American Re Settles

Robin C. Dusek & Patrick Frye

What does that mean?

If rumors are to be believed (and there is no reason to think that they should not be), the long running dispute of* United States Fidelity & Guaranty Co. v. American Re-Insurance Co. *("USF&G v. Am Re") settled with trial looming.

As many will remember, in February 2013, the New York Court of Appeals (the state's highest court) issued an important decision that outlined the parameters under New York law for cedents to follow when allocating a settlement to reinsurers. In light of the settlement, the 2013 decision will remain the last and most important analysis of the issues involved in the case and will likely be cited by New York courts (and relied on as persuasive authority in others) where allocation issues intersect with "Follow the Settlements" principles.

Although the decision received attention in the industry press at the time, given its importance since then, it is worth reviewing the key points of the case. The unanimous decision established that reinsurers are only bound by a cedent's reasonable, "'good faith' decisions" in allocating a settlement to its reinsurance covers. Reinsurers had challenged three distinct decisions made by the cedent in allocating a settlement with its insureds that resolved asbestos claims made under general liability policies. The reinsurers challenged them on the basis that each improperly minimized the cedent's net liability for the settlement by maximizing recoveries from the reinsurers. The trial court granted the cedent's summary judgment motion based on the "Follow the Settlements" doctrine, precluding inquiry into whether the allocation to the reinsurers was reasonable or even done in bad faith. The reinsurers appealed the summary judgment, to the first level of appeal, which affirmed in a 2-1 decision, and then to the New York Court of Appeals.

In short, the Court of Appeals ruled that "Follow the Settlements" does not necessarily mean "Follow the Allocations."

The Court found that the "Follow the Settlements" doctrine generally precludes reinsurers from challenging cedents' settlement decisions because the interests of cedents and reinsurers normally are aligned and, therefore, reinsurers should accept the amount the cedent agrees to pay its insured to settle a claim. However, the Court agreed with the reinsurers that the "Follow the Settlements" doctrine should not require a reinsurer to follow the allocation decision of its cedent where the interests of the reinsurer and the cedent conflict. The Court observed that the interests of cedents and reinsurers "will often conflict" when allocation decisions are made. The Court ruled that the "Follow the Settlements" doctrine operates to bind a reinsurer only to the "'good faith decisions" of a cedent. The Court stated that "objective reasonableness should ordinarily determine the validity of an allocation." In addition, the Court ruled that a cedent's allocation decision "must be one that the parties to the settlement of the underlying insurance claims might reasonably have arrived at in arm's length negotiations if the reinsurance did not exist."

> *The Court ruled that the "Follow the Settlements" doctrine operates to bind a reinsurer…*

Although the Court did note that a cedent is not required to disregard its own financial interests in arriving at its allocation methodology, the Court stated that the cedent's "choice [among several allocations] must be a reasonable one." If a reinsurer can show evidence of the unreasonableness of an allocation, it is entitled to a trial to determine whether the facts demonstrate the cedent's allocation decision was "objectively reasonable."

The Court considered the cedent's reliance on the fact that the underlying settlement with the insured supported its allocation decision. The Court held that "reasonableness cannot be established merely by showing the cedent's allocation for reinsurance purposes is the same as the allocation that the cedent and the insurance claimants actually adopted in settling the underlying insurance claims." A cedent's insertion of self-serving language into the underlying settlement agreement will not, standing alone, demonstrate that the allocation was reasonable. The cedent is still obligated to present facts at trial that establish that its allocation decision was one that "might reasonably have [been] arrived at in arm's length negotiations if the reinsurance did not exist."

As the case before the Court involved excess of loss reinsurers whose interests conflicted with the cedent's interests in the cedent's allocation decisions, the reinsurers succeeded in being allowed to challenge two of the cedent's three allocation decisions in dispute. Based on that reasoning, the Court ruled that the validity of (1) the allocation of no portion of the settlement to the insured's bad faith claims and (2) the valuation of certain types of claims needed to be resolved at trial based on the facts underlying those decisions, because the evidence in the appellate record did not indicate that the cedent's allocation decisions could reasonably have been agreed on by the insured and the cedent in the absence of reinsurance coverage. However, the Court did not allow the reinsurers to challenge USF&G's decision to allocate all losses to a single year. Though spiking the one year allowed USF&G to exceed the reinsurance retention that it would not have obtained had it spread the loss over many years, the Court decided that this allocation decision was reasonable because it was consistent with California law on how the asbestos claimants might obtain insurance coverage. As a consequence, the Court reversed in part the appellate court's grant of summary judgment to the cedent and remanded those issues to the trial court (and these issues were ultimately settled).

The takeaways from this decision are:

Founded in 1933, Mound Cotton Wollan & Greengrass LLP is among the oldest and most respected law firms in New York City, offering preeminent legal services in a wide array of practice areas. Headquartered in New York's financial district, MCWG is engaged primarily in the conduct of insurance, reinsurance, and commercial litigation.

Mound Cotton Wollan & Greengrass LLP

www.moundcotton.com

1. By placing an objective boundary on the permissible discretion of a cedent in making an allocation decision, the decision lessens the risk that a reinsurer will be forced to follow an unreasonable allocation decision made by a cedent in an effort to maximize reinsurance recoveries.

2. The allocation of an underlying settlement must be objectively reasonable and consistent with what the cedent and policyholder could have reasonably negotiated if the cedent had no reinsurance. This analysis will, of course, depend on the particular facts of each settlement and allocation decision, and the types of reinsurance covers at issue, particularly the attachment point of the impacted layers. The Court in essence held that a cedent must reach its settlement decision as if it had no reinsurance. While the Court did not refer to the Duty of Utmost Good Faith, its decision may be viewed as an implicit endorsement of that Duty. Importantly, the Court's decision does not require that the reinsurer prove bad faith by the cedent in arriving at the allocation decision.

3. Allocating all losses to one year, rather than across years, may be objectively reasonable under the facts and governing law of a particular case, as was the case in USF&G.

4. The cedent's subjective intent in reaching a particular allocation is irrelevant. The mere fact that the evidence shows the cedent was desirous of maximizing reinsurance recoveries is not enough, standing alone, to defeat its allocation decision. And, in situations

…the Court did not allow the reinsurers to challenge USF&G's decision to allocate all losses to a single year.

where multiple allocations can be shown to be "objectively reasonable," a cedent is not required to prove its allocation was the most reasonable.

5. Where the reinsurer can point to some evidence that the allocation is unreasonable, a question of fact arises and summary judgment should not be granted.

Since the *USF&G* decision came down, courts have looked to its reasoning to evaluate whether a cedent's allocation decisions were justifiable. In finding that a reinsurer had not set forth sufficient bases to challenge a cedent's allocation, the *Northern District of New York in Utica Mut. Ins. Co. v. Clearwater Ins. Co.* cited to the USF&G decision in support of the proposition that a cedent is under no obligation to strictly align its interests with that of its reinsurer. 2016 WL 254770.

The Northern District of New York again considered *USF&G*, this time in more depth, with *Utica Mut. Ins. Co. v. Fireman's Fund Ins. Co*, 2017 WL 743996 (N.D.N.Y 2017). In rejecting both parties' motions for partial summary judgement, the court quoted from USF&G and concluded that "a cedent's motive to reach reinsurance…may invalidate the follow the settlement protection if it causes the cedent to make an unreasonable settlement allocation." Id. at *13-14.

In *New Hampshire Ins. Co. v. Clearwater Ins. Co.*, the New York Appellate Division considered the standards set forth in the USF&G case and affirmed the trial court's refusal to enter summary judgment for the cedent, recognizing that under the USF&G standard, a cedent's allocation decisions are not immune from scrutiny. 129 A.D.3d 99.

Courts have remained faithful to the nuanced approach of the *USF&G* court, and, as expected at the time the decision came down, it has developed into a precedent that offers protections to both cedents and reinsurers. Its legacy is still in the making, but, thus far, its objective standard for determining to what extent a reinsurer is required to follow a cedent's fortunes seems to have provided clarification to an issue that has been, at times, confusing. ●

Robin C. Dusek and Patrick Frye are Partners at the law firm of Freeborn & Peters LLP. They can be reached at rdusek@freeborn.com and pfrye@freeborn.com.

GENPACT
GENERATING IMPACT℠
LEAN DIGITAL™

Putting *digital* to work in reinsurance

With the acquisition of Inpoint Operations, Genpact becomes the premier partner to help you achieve your goals. Whether commuting legacy liabilities, discovering missed cessions, re-engineering your operations, or reducing expenses, Genpact can partner with you at any point on your journey to success.

genpact.com/lean digital

When It Rains.

We've Got You Covered.

Legal Protection. Locke Lord gives insurance and reinsurance companies, and insurance intermediaries the legal guidance and protection they need. Our reputation for providing innovative thinking in mergers and acquisitions, transactions, regulatory compliance, litigation and arbitration is the result of deep experience, and highly skilled people.

Locke Lord LLP

Practical Wisdom, Trusted Advice.

www.lockelord.com

Atlanta | Austin | Boston | Chicago | Cincinnati | Dallas | Hartford | Hong Kong | Houston | London | Los Angeles | Miami
Morristown | New Orleans | New York | Providence | Sacramento | San Francisco | Stamford | Washington DC | West Palm Beach

Attorney Advertising © 2017 Locke Lord LLP

SPOTLIGHT

Paul Corver, R&Q the "IRLA" of Run Off

"Success is not final, failure is not fatal: it is the courage to continue that counts."
— Winston Churchill

Please tell our readers about your work history and lessons you have learned.

Having worked in insurance for 32 years, of which the last 27 years has been in the run-off sector, I learned at an early stage that run-off was an exciting place to be. The innovation and determination of practitioners to find a solution or manage a problem keeps the sector fresh and an enjoyable place to work.

If you could have a second career, what would it be?

I was attracted to art and design in my early teens but sadly these were not academic enough subjects for my parents so were left behind. I have always liked the idea of being a landscape gardener, something most people would be surprised to know about me. I am a very keen gardener, and I would prefer to spend much more time outdoors than is achievable in an insurance role.

What do you like best/worst about your current position?

As IRLA Chairman, I am delighted to see a growth in membership and the continued recognition of the benefits of active run-off management. This manifests in an increasing number of interesting transactions that I see in my M&A role at R&Q. The worst is possibly the disdain with which some people still view the run-off sector but this lessens every year.

How long have you been Chairman of IRLA and how have you seen its role in the Industry evolve?

I am in my ninth year as Chairman and there has been much change in that period. Companies such as Munich Re and QBE have set up dedicated units handling run-off as have a number of other global firms. Membership of IRLA has increased across a wider spectrum of carriers. And, run-off transactions have increased in scale and frequency. The last decade has seen significant change in the insurance industry's recognition of the sector.

What industry publications do you read on a regular basis?

The mainstays are Insurance Insider, Insurance Day, Captive Review and Captive Insurance Times, the latter two because R&Q is very active in M&A across the captive insurance sector. And of course, AIRROC Matters.

What educational sessions or conferences do you attend and why?

The key annual event for me is IRLA Congress. I also attend, and speak at, events related to the captive insurance sector such as AIRMIC and European Captive Forum to educate risk managers and captive owners on the benefits of effective run-off management. I used to attend AIRROC; but since R&Q moved its head office to Bermuda, those events are attended by the Bermudian team.

How would you like to see IRLA and AIRROC continue to work together in the future?

The Associations share similar platforms with common ambitions and plenty of crossover in membership. Education continues as a key deliverable for both organizations. The effectiveness of this education has helped develop active run-off management in many companies. IRLA and AIRROC share speakers at events and support each other's programs where practicable. I look forward to this continuing over the coming years.

Bina T. Dagar, bdagar@ameyaconsulting.com and
Connie D. O'Mara, connie@cdomaraconsulting.com

A TALE OF THREE CITIES

CHICAGO

"It was the best of times, it was the worst of times."

We present AIRROC's Tale of Three cities—Chicago, New York, Hartford —our continued efforts to bring high impact education to our members. Times are good for the runoff industry with business to be accomplished and our association behind us, more challenging as we all seek to adapt in a shifting political, economic, and staffing environment. First to Chicago, co-hosted by CNA and Allstate and held at the CNA offices in iconic "Big Red".

Photos: Jason Gerber

Coverage Issues Relating to Self-Driving Cars

Tony Roehl of Morris Manning & Martin and Chuck Smith of Allstate presented on the technology and risks behind autonomous vehicles.

The future is here as noted by automakers:

- Tesla has said that a driverless Tesla will able to drive from L.A. to New York City "by the end of 2017,"
- GM has said autonomous vehicles could be deployed as early as 2020,
- Volvo has announced plans to start selling cars with autonomous driving technology by 2020, and
- Audi has claimed that its popular A8 model will be capable of self-driving in the 2018 model year.

Key to understanding these claims are an understanding of what is meant by the term "autonomous vehicles."

Roehl noted the levels of vehicle automation:

Level 2: Limited automation
Advanced Driver Assist Systems (ADAS) like automatic braking, warning systems, parking assistance, etc.

Level 3: Limited self-driving automation
Driver can take control in certain situations or when the car indicates to do so

Level 4: Full self-driving automation
Car will perform all driving functions and monitor road conditions from the beginning to the end of a trip. Cars are networked to one another and the environment

Level 5: Performance Equivalent to Humans
Fully-autonomous system that expects the vehicle's performance to equal that of a human driver in every single driving scenario

According to Roehl, as of this year, 41 states and Washington, D.C. have introduced and considered legislation related to autonomous vehicles and 14 state legislatures and Washington, D.C. have enacted legislation related to autonomous vehicles. Additionally, Governors from Arizona and Massachusetts issued executive orders pertaining to autonomous vehicles. This is allowing testing of autonomous vehicles in many states, now with significant sums being spent to advance the technology. In 2013, Google invested $258 million in Uber and GM invested $500 million in Lyft, announcing it will launch its first driverless car on the Lyft platform. Further, GM and Lyft are planning to begin testing a fleet of self-driving taxis on public roads within the next few months, and the two plan on deploying "thousands" of test vehicles beginning in 2018.

Chuck Smith focused on the future of auto insurance in a world of autonomous vehicles and noted that vehicle ownership will change as will needed insurance change. Individual ownership of a car will become the exception. 94% of crashes are currently due to human error. As one of the features of autonomous vehicles is accident avoidance capability, a shift from a negligence standard of liability to a products liability standard will occur, impacting the insurance model and insurance premiums. Accidents will still happen but will occur from things like design defects, weather, road conditions, poor maintenance and hacking rather than from driver negligence. As a result, manufacturers will try to limit their exposure by such approaches as retaining ownership and maintenance of the vehicles they produce.

Throughout this change, the insurance industry will remain a key source of unique skills. Indeed, the insurance industry has more detailed accident data and models than the product manufacturers, greater risk management expertise and the best understanding of liability systems and will be a key contributor to change.

Martin Cillick, mcill@allstate.com

In re Viking Pump, Inc.

Amy Kallal, of Mound Cotton Wollan & Greengrass presented regarding the New York Court of Appeals decision *In The Matter of Viking Pump, Inc. and Warren Pumps, LLC,* Insurance, 27 N.Y.3d 244; 52 N.E.3d 1144; 33 N.Y.S.3d 118; (NY App. 2016). Amy described the complex background of the case involving the Delaware Supreme Court's certification of

the following questions to the New York Court of Appeals:

1. Under New York law, is the proper method of allocation to be used all sums or pro rata when there are non-cumulation and prior insurance provisions?

2. Given the Court's answer to Question #1, under New York law and based on the policy language at issue here, when the underlying primary and umbrella insurance in the same policy period has been exhausted, does vertical or horizontal exhaustion apply to determine when a policyholder may access its excess insurance?

Specifically at issue in the case was the scope of insurance coverage provided to Houdaille (later known as John Crane) while it owned Warren Pumps and Viking Pump, both of which were companies that manufactured pumps that included asbestos components (Collectively "Viking Pump").

The court noted that while its earlier decision in *Consolidated Edison Co. of N.Y. v. Allstate Ins. Co.*, 98 N.Y.2d 208 (2002) applied a pro-rata allocation to claims involving environmental contamination over a number of years and a number of insurance policies, that result was distinguishable since the Consolidated Edison decision was not "a blanket rule" but rather, was based upon "our general principles of contract interpretation and made clear that the contract language controls the question of allocation."

In Viking Pumps, the court found, instead, that the presence of a non-cumulation clause or a non-cumulation clause and prior insurance provision mandates an all sums allocation and concluded that a pro-rata allocation is irreconcilable with non-cumulation clauses.

The second certified question decided by the court was whether horizontal or vertical exhaustion applies under the terms of the excess policies. The court found that vertical exhaustion applied under the terms of the relevant excess policies, "in light of the language in the excess policies tying their attachment only to specific underlying policies in effect during the same policy period as the applicable excess policy, and the absence of any policy language suggesting a contrary intent, we conclude that the excess policies are triggered by vertical exhaustion of underlying available coverage within the same policy period."

Martin Cillick, mcill@allstate.com

Cost of Maintaining Legacy Data Systems for Runoff

David McAndrews, a self-professed "PhD of the Inefficient Processes" discussed the problems, inefficiencies and costs of maintaining legacy data through a patchwork of cobbled together legacy data management systems that he equates to Frankenstein's Monsters. As a result, McAndrews argues that the majority of companies cannot leverage big data. This is because information is spread over multiple systems which cannot communicate and because IT departments tend to "Frankenstein together" work-around procedures. To "manage the monster" McAndrews recommends data migration to a single "interoperable platform" which can easily work alongside continued technological development and also result in greater cybersecurity.

McAndrews provided a description of "p1 runoff" software by HMR Group. p1 helps maintain security and integrates the existing platforms. Noting that redundancy leads to mistakes, McAndrews identified the "Automated Interface Module" or "AIM" by p1 as a capable solution that replicates the entry of duplicative data so the job can be done once and repeated thereafter. Likewise, McAndrews identified the p1 "Service Line" as a way of bridging the gap between outdated legacy systems and the connectivity requirements of today.

Finally, McAndrews offered his top 5 things that can be done to improve insurance data management:

1. Keep it simple;
2. Less is more;
3. Look for Small Wins;
4. Encourage Cross Pollination; and
5. Choose p1.

Martin Cillick, mcill@allstate.com

A TALE OF THREE CITIES

NEW YORK

The Summer Membership meeting took place in the familiar confines of 1301 Avenue of the Americas. While the name on the door has been updated to Norton Rose Fulbright upon its merger with Chadbourne & Parke, the gracious hospitality extended to AIRROC and its members remains the same.

Nanotechnology: Science, Regulation and Emerging Risks

The morning began with a presentation by Thomas Bernier and Lawrence Mason, partners with the firm of Goldberg Segalla on the rapid technological progression, commercialization and pervasiveness of nanotechnology and the associated risks and challenges they pose for the insurance industry.

Nanotechnology is engineering at molecular or atomic level of particles and structures as small as one ten-thousandth the diameter of a human hair, one thousandth the size of a red blood cell, or one thousandth the width of a sheet of paper. The practical application of this technology is diverse and already prevalent in medical technology, environmental, and personal care products. It is poised to transform the manufacturing processes through the development of lighter and stronger materials with new products and applications being developed at a rapid pace.

The revenue trends for nanotechnologies are staggering with approximately 1600 consumer products on the market now. Nanotech revenue has increased six-fold between 2009 and 2016 with an estimated $48.9 billion in sales by 2020 and a compound annual growth rate of 18.7%.

The grave concern of this proliferation and wide-scale use of nanomaterial is that the toxicity and environmental impact of nano is not well known. Nonetheless, there is a growing body of evidence that suggests the potential of adverse health effects stemming from exposures to nanoparticles. By 2020, it is estimated that 6 million factory workers will be handling nanoparticles worldwide with 2 million factory workers handling nanoparticles in the USA.

Calls for tighter regulation and government oversight of nanotechnology have resulted in the establishment of the Nanotechnology Environmental and Health Implications ("NEHI") working group which coordinates and provides an information exchange among Federal agencies that conduct nanotechnology research and are responsible for regulation of nanomaterials and products that contain them. There are, however, huge gaps in the regulatory oversight by the various agencies and the science as to the impact on human health and the environment has simply not kept up with the innovation and the successful commercialization of nanotechnology.

All of this leads to the recognition by insurance industry of nanotechnology as an emerging risk which presents a host of unique issues that insurers must grapple with.

From an underwriting perspective, nano represents a new technology that could significantly impact the risk profile of one or more target markets. Integration with other products coupled with the difficulty to access risk due to lack of historical data on frequency and severity, make it difficult to develop policy exclusions that are marketable.

From a claims perspective, it is difficult to assess coverage due to lack of legal guidance on interpreting current policy language. The likelihood of a claims explosion is real and just one scientific study and lawsuit away because of the wide-spread and wide-ranging applications. The panelist described the eerie and foreboding similarities of nanotechnology to asbestos and the many coverages that may be implicated. If the history of asbestos is any indicator, nanotechnology represents an enormous challenge to the insurance industry.

Maryann Taylor, mtaylor@damato-lynch.com

Talc and Cancer: The Science and the Litigation

The panel, consisting of Ben Blume (Kennedys CMK), Katie Matison (Lane Powell) and Dr. Annette B. Santamaria (Rimkus Consulting) provided context and a critical review of the $300+ million in recent verdicts in cosmetic talc cases, demonstrating the evolution of these cases in a toxic tort continuum related to asbestos litigation. We all know the evolution of asbestos litigation and we now have the impact of both the liability and coverage legacy of that litigation. It influences results surrounding other toxic tort claims. This panel pointed out parallels between asbestos and talc litigation and

Photos: Jean-Marc Grambert

warned of even more problematic exposures for insurance companies faced with potential coverage of talc claims if we do not fail to highlight how they are different from asbestos claims. Whether we decry plaintiffs' lawyers' greed for headlines and jaw-dropping verdicts, or forum shopping to get to Madison County, Illinois, (the "judicial hell-hole" that developed along the asbestos super-highway) or whether we are inured to frequent theories that a given substance is the "next asbestos", talc claims have the potential to present substantial numbers of claims, defense expenses, and verdicts. The panel discussed key areas of dispute.

The core question, of course, is whether talc caused the plaintiff's injuries. Dr. Santamaria went over the science and epidemiology that currently exist with regard to cosmetic talc cases and ovarian cancer (as distinguished from talc cases predicated on exposure to asbestos contaminated talc causing other types of cancer). Clearly, there is debate, but the verdict seems to depend on who hears the evidence. Contrast the jury verdicts in Madison County with a decision last year in New Jersey (*Carl v. Johnson & Johnson*, No. ATL-L-6546-14, 2016 WL 4580145 (N.J. Super. Ct. Law Div., Atl. Cty., Sept. 2, 2016) where Judge Nelson C. Johnson excluded the plaintiffs' experts. After reviewing the scientific literature, he did not find the opinions that supported the theory that the talc caused ovarian cancer to be "sufficiently reliable as being based on a sound, adequately-founded scientific methodology." Many juries, however, when faced with similar evidence on causation have not only awarded damages, but substantial punitive damages to punish talc defendants for their disregard of public safety.

The Panel also reviewed the other critical moving part in cosmetic talc litigation nationwide—the question of personal jurisdiction that surrounds the ability of plaintiffs' law firms to file cases for out-of-state plaintiffs where they believe they will get the best result. The recent U.S. Supreme Court Decision in Bristol-Myers-Squibb (*Bristol-Myers Squibb Co. v. Superior Court*, No. 16-466 (U.S. June 19, 2017), has caused a flurry of motions and arguments on appeal that may cause plaintiffs' firms to spread their talc claims across the nation and promises to prolong the expense and duration of the litigation.

Further, the panel reviewed the plethora of coverage issues raised by talc claims being presented under various types of policies. Given the specific etiology of disease causation and current advances in scientific methods of investigation, the challenge for insurers will be to assess what policies are impacted and how. This will, no doubt, involve extensive use of expert evaluation and the ability to articulate when an injury, if any, took place supported by persuasive medical evidence.

Connie D. O'Mara, connie@cdomaraconsulting.com

Climate Change: An Actuarial Perspective

In a panel moderated by Lewis Hassett of Morris, Manning & Martin, attendees heard from two esteemed actuarial experts on climate change and the impacts on the property and casualty industry. The panel was comprised of Michael Angelina, ACAS, MAAA, CERA, the executive director of the Academy of Risk Management and Insurance at Saint Joseph's University and Steve Kolk, ACAS, MAAA, an independent consulting actuary and active member of the Climate Index Work Group.

The session began with Professor Angelina explaining the origins and goals of the Actuaries' Climate Index ("ACI") and the Actuaries' Climate Risk Index ("ACRI"), both of which were commissioned and sponsored by four major actuarial groups: the American Academy of Actuaries, the Canadian Institute of Actuaries, the Casualty Actuarial Society and the Society of Actuaries. The goal was to create objective and straightforward indices from an actuarial perspective and to use those indices to inform the insurance industry and the general public on the impact of climate change and contribute constructively to the climate change debate. The end result was the creation of one index that measures changes in climate extremes—the ACI; and a second index that relates those climate extremes to economic and human losses—the ACRI.

The ACI focus on the frequency of severe weather based upon historical data of six variables consisting of high temperature, low temperature, heavy precipitation, lengthy drought, high wind and coastal sea level. Indices of the six climate variables are calculated based on separate formulas from data derived from different sources. The data is then constructed for geographic grids, then summarized to regions, countries, and in total. The ACI Index is a composite of six underlying indices. The ACI shows that the frequency of extreme weather has increased with more frequent heat, rain and drought and less frequent cold extremes. Incidents of extreme weather has dramatically increased over the last decade.

Unlike the ACI, the ACRI adjusts for exposure and is based on the historical correlations of economic losses, mortality, and morbidity to monthly ACI data by region. In other words, the ACRI correlates to losses of who gets hurt. For the USA and Canada, the ACRI has been above its average reference period value (which is set to 5) about 96% of the time since 2005. Heat has been the primary driver of the index, although drought and flood have also been high at times.

Panel member Steve Kolk presented on the impact of climate change on insurance risk and the global community, delving first into an explanation of the science, the historical discourse and the genesis of the Climate Change Committee. Measuring climate change requires an understanding of how the climate system operates, which encompasses the entirety of the atmosphere, land surface and oceans over a wide range of time. Changes are occurring, on both a regional and global scale that exceed what is to be expected from natural climate variability alone. Surface temperatures have risen and sea levels are rising. The implications of the wide-ranging and rapid changes in climate for human populations and economic assets are an object of deep concern. The ACI should be thought of as the footings of a new analytical home and the ACRI as the solid foundation of new handles on climate risk. Future ACRI projects will inform risk analytics enabling society to stand firm amidst climate magnified risks.

The ACI and ACRI information will be publicly available on a new website, as a resource for use in further research (www.actuariesclimateindex.org) and (www.indiceclimatiqueactuaries.org).

Maryann Taylor, mtaylor@damato-lynch.com

Tower Insurance Group Tower Insolvency—Mergers, Commutation and Liquidation

Joseph Holloway, the Liquidation Manager for Castlepoint National in Liquidation, described the recent insolvency of Castlepoint as successor to the Tower Group. The Tower Group was made up of 10 insurance companies domiciled in six states that operated on a consolidated financial basis through an intercompany pooling arrangement; their financial issues started to emerge in 2013 when it reported reserve deficiencies of nearly $400 Million. Most of the reserves were attributable to California workers' compensation business so that state's Department of Insurance, working with the other five states, took the lead in formulating a plan for conservation and liquidation. Prior to being put into Conservation, the California Department of Insurance orchestrated the consolidation of all ten companies into a single entity: Castlepoint National Insurance Company, a California-based company that could be put into conservation in a single legal proceeding (rather than multiple proceedings in states where members of the Tower Group were domiciled). By commuting a stop-loss cover that had been in place, the estate derived $200 million in funds for continued payment of claims. Taking the position that no more would be paid on claims during the conservation phase than would be paid by state guarantee funds during liquidation, Castlepoint was able to maintain a payment stream while avoiding preferences; $335 million in claims were paid during the conservation. The liquidation order was effective on April 1, 2017 and now claims are being forwarded to state guarantee funds for handling and payment.

Connie D. O'Mara, connie@cdomaraconsulting.com

Talk to Foley. We're listening.[SM]

Foley's Insurance & Reinsurance Litigation Team provides comprehensive counseling, litigation, and dispute resolution services to the insurance industry.

Our approach is to listen carefully to you in order to understand your specific business concerns and objectives. Armed with that knowledge, we work with you to develop a plan that will help you achieve your specific goals. At Foley, we never forget your business needs.

Tell us about your challenges and let us share how Foley can add value to your business. Contact Partner Neal Moglin in our Chicago office at nmoglin@foley.com or Bart Reuter in our Milwaukee office at breuter@foley.com.

Foley is a proud Corporate Partner of AIRROC.

FOLEY

FOLEY & LARDNER LLP

FOLEY.COM

BOSTON | BRUSSELS | CHICAGO | DETROIT | JACKSONVILLE | LOS ANGELES | MADISON | MIAMI | MILWAUKEE | NEW YORK | ORLANDO
SACRAMENTO | SAN DIEGO | SAN FRANCISCO | SHANGHAI | SILICON VALLEY | TALLAHASSEE | TAMPA | TOKYO | WASHINGTON, D.C.

©2017 Foley & Lardner LLP ■ Attorney Advertising ■ Images of people may not be Foley personnel ■ 17.MC1648

A TALE OF THREE CITIES

HARTFORD

AIRROC traveled to Hartford for the first time to co-host a Regional Education Day with Day Pitney at the historic Society Club. Due to the proximity to some of AIRROC's large member companies (in particular The Hartford and Travelers), we met quite a few individuals from AIRROC members that hadn't yet been able to attend an AIRROC event.

September 11th — A Coverage Retrospective

Day Pitney's Michael Mullins and Jonathan Zelig spoke at AIRROC's Hartford Regional Education day, recapping the contractual controversies resulting from that devastating day and highlighting a few lessons learned for insurers. Their talk centered on the "single or multiple occurrence" question, measuring business interruption, and avoiding long tail losses.

Larry Silverstein, a property developer and investor, sealed a 99-year lease for the World Trade Center complex on July 24, 2001 for $3.2B, just over a month before the attack. On September 11th, two hijacked airplanes hit the Twin Towers, 16 minutes apart.

The $3B question: Seeking two policy limit payments, Silverstein claimed each crash was a separate attack and a separate occurrence. Insurers argued that the plot to hijack and attack on that day represent a single occurrence. The answer: It depends on the definition of occurrence.

A lifelong New Yorker, the Hon. John S. Martin Jr., presided over multiple September 11th policy language cases. Three companies, The Hartford, St. Paul, and Royal, proved they had bound coverage under the WillProp Form, which defined occurrence as attributed "to one cause or to one series of similar causes." Those "cause"-based reinsurers won their single occurrence argument. On the other hand, the Allianz policy language defined occurrence as a "loss or series of losses, disasters, or casualties arising out of one event." Allianz lost its case.

The lesson here: in insurance policy language, the term "cause" is less restricted, while the term "event" represents a particular time, place, or way. To Allianz, the attack was the event that led to a series of losses. The Judge declared that each hijack could also represent an "event" and sent the case to a jury. "Event" and "series" language is often susceptible to counter interpretation. Not surprisingly, the jury seated in Lower Manhattan sided with the insured and authorized a double policy limit payment. Lesson number two: Avoid high-profile and local jury cases.

So how should we measure a business interruption coverage period resulting from an expensive, unique loss? Duane Reade Pharmacy manages about 200 stores in the New York area, 120+ of which are in Manhattan. The World Trade Center store location was the chain's most profitable store. For many years, it was unclear how long it would take to rebuild the location and if the site would become a memorial generating equally profitable store traffic. Duane Reade was a single renter in the complex and had no control over the construction decisions. The complex reopened in 2014, taking 13 years and 56 days to rebuild.

Insurers argued that Duane Reade could have rebuilt and operated at another location, at which time the restoration period should terminate, and that one of the other 120 locations near-by would profit from redirected traffic. Insurers paid $9.8M to the chain. Seeking a larger settlement, Duane Reade took the argument to court. The policy language discussed a "reasonably equivalent store and a reasonably equivalent location," and "rebuild, repair, or replace." Duane Reade held general coverage for all of its store locations. It did not have specific coverage for this most profitable store. The court's intention is to incentivize business to "get back to work" and sided with insurers that the chain could find reasonable equivalence at another location. Lesson learned: Buy specific coverage to protect a unique risk.

Lastly, the pair discussed accounting for the unaccountable – disaster site injuries. Cleanup and rescue workers suffering from asbestos and other injuries sued the Battery Park City authority. In 2009, 600 cases were dismissed because the time limit to file had passed. Political pressures to protect this group resulted in legal changes and extended reporting periods. The final lesson: Reinsurers seeking certainty and avoiding long-tail losses should tie sunset provisions to the applicable state law and include a reporting cap in their policy language.

Lindsay Carter, lindsay.yorkcarter@thehartford.com

Cybersecurity and the Runoff Sector: Increasing Regulatory Pressures

Cybersecurity is a significant and growing exposure: $450B to the global economy in 2016; over 2B personal records stolen globally; the ever-expanding list continues. The question is not **IF** something will happen to the Runoff sector, but **WHEN** something will happen, and whether we will be prepared.

Starting with New York, regulators are making cybersecurity an issue, both for insurance companies and for third parties that handle their data. There is immediate pressure in New York to respond with an established, aggressive timeline. There is also pressure mounting outside of New York, including NAIC's Insurance Data Security Model Law, which is currently in draft form. What does it mean? This is not an IT problem. Companies must: 1) undertake a detailed risk assessment; 2) be prepared to provide prompt breach notification to regulators, consumers and credit reporting agencies; 3) investigate breaches; 4) establish ongoing monitoring and improve security levels; and 5) manage cybersecurity of third-party services providers through contractual terms.

In regards to third parties, for example, consider arbitrators and board members. What information is provided and in what format? How do you control the information so as to reduce or eliminate cybersecurity risk from these parties? The conclusion, there is no need to be afraid, but companies need to take immediate action to control their cybersecurity risk, which largely is driven by human risks and processes, to make them safe.

Questions can be referred to Jed Davis, Partner, Day Pitney LLP jdavis@daypitney.com.

William Teich, William.teich@thehartford.com

Thanks to Our Corporate Partners

BR | BUTLER RUBIN

EY Building a better working world

FOLEY & LARDNER LLP

Freeborn ATTORNEYS AT LAW

GARDERE

Kennedys CMK LLP

MAYER • BROWN

Locke Lord

Morris, Manning & Martin, LLP

Mound Cotton Wollan & Greengrass LLP

NORTON ROSE FULBRIGHT

STROOCK

White and Williams LLP

ADVERTISERS IN THIS ISSUE

Find out how your company can benefit from advertising in AIRROC Matters. Contact Carolyn Fahey: tel 703-730-2808 or email carolyn@airroc.org

Whether advising on entering the run-off market, buying and selling portfolios and entities, resolving disputes, managing discontinued operations or achieving exit strategies, our lawyers get the job done.

MAYER · BROWN

Americas | Asia | Europe | Middle East | www.mayerbrown.com/insurance

Mayer Brown comprises legal practices that are separate entities (the "Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP and Mayer Brown Europe-Brussels LLP, both limited liability partnerships established in Illinois USA; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales (authorized and regulated by the Solicitors Regulation Authority and registered in England and Wales number OC 303359); Mayer Brown, a SELAS established in France; Mayer Brown Mexico, S.C., a sociedad civil formed under the laws of the State of Durango, Mexico; Mayer Brown JSM, a Hong Kong partnership and its associated legal practices in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. Mayer Brown Consulting (Singapore) Pte. Ltd and its subsidiary, which are affiliated with Mayer Brown, provide customs and trade advisory and consultancy services, not legal services. "Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.

© 2017 The Mayer Brown Practices. All rights reserved. Attorney advertising. Prior results do not guarantee a similar outcome.

AIRROC UPDATE

Busy as a Beaver

Carolyn Fahey

Message from the Executive Director

In choosing my animal for this issue the word "busy" popped into my mind and immediately after that the old adage that is the title of my article.

Beavers have many adaptations which help them thrive in their environments —both underwater and on land. While I don't have to live underwater, I have to admit that at times I feel like I am paddling VERY FAST!! Having a beaver flat tail to keep me level might also come in handy!

AIRROC had a busy summer packed with education—from Chicago to Hartford to New York to Philadelphia; we have again presented programs that have topics relevant to our members and partners. More on these programs can be found in this issue. One of the key benefits of AIRROC membership is still the highly rated education. (See more in the box this page).

The preparations for the October NJ Forum are moving at a fast pace. Registrations are coming in, the education agenda is being finalized, and sponsors are lining up. The education sessions will provide in-depth insights on a number of topics: the evolving insurance workforce, legacy employers liability in the UK, In re Viking Pump and allocation, U.S. and UK cyber risk regulatory changes, discovery in an arbitration, to name a few

We have some interesting statistics on last year's October event from our post-event surveys—see the box on this page. If you look at these percentages how can you afford NOT to be present? It is time to sign up, schedule your meetings, and plan your strategy for making the event productive for you and your company. Remember that the delegate rates increase after September 15, so register early.

AIRROC has just had a very successful collaboration with EECMA—the Environmental and Emerging Claim Manager Association. Our organizations worked together on a daylong symposium that looked at the challenges arising from the Mega-Superfund Sites. It was a unique event and hopefully the first of many jointly planned events for us. In a challenging age for non-profits, the AIRROC Board and I feel that it is important that we work together to bolster each other's effectiveness.

There are lots of other "busy beavers" on the Board of Directors and the Advisory Council that are looking at AIRROC's governance, cyber risks, expansion of marketing efforts, and other industry collaborations, exploring a concept to create a database to track company name changes, offering web- based training, and much more! Stay tuned…

We always need other "busy beavers" willing to offer time to help with our initiatives—let me know if you can volunteer!

See you all in New Jersey…

Did You Know? AIRROC By the Numbers

AIRROC NJ 2016 survey results show that:

- **40%** of delegates met with 7-9 companies
- **27%** met with 10 or more companies
- That means that nearly **70%** of the delegates met with 7 or more companies just by attending AIRROC NJ

The end result of the most successful meetings at AIRROC NJ 2017:

- Met counterparty for first time **30.43%**
- Began working on, progressed, or completed a sale/transfer **21.74%**
- Began working on, progressed, or completed a commutation **50.00%**
- Committed to 2017 project list with counterparty **32.61%**
- Arranged a follow-up meeting with counter party prior to year-end **19.57%**

Praise for AIRROC Education:

- Arranged a follow-up meeting with counter party prior to year-end **19.57%**
- In 2016 AIRROC hosted 7 events which were all very highly rated in post-event surveys— **98%** of the attendees rated the events Excellent or Very Good
- A total of 728 individuals attended AIRROC workshops, regional and membership events—653 attendees or **80%** were AIRROC members or Corporate Partners

AIRROC's VISION is to be the most valued (re)insurance industry educator and network provider for issue resolution and creation of optimal exit strategies.

AIRROC's MISSION is to promote and represent the interests of entities with legacy business by improving industry standards and enhancing knowledge and communications within and outside of the (re) insurance industry.

Carolyn Fahey joined AIRROC as Executive Director in May 2012. She brings more than 22 years of re/insurance industry and association experience to the organization. carolyn@airroc.org

BUTLER RUBIN SALTARELLI & BOYD LLP

Count on Butler Rubin

When complex issues arise, count on Butler Rubin to provide trusted counsel.

From underwriting to claims, allocation to insolvency and all areas in between, Butler Rubin's insurance and reinsurance practices are consistently cited for excellence.*

*Chambers USA Guide to America's Leading Lawyers, Leading Lawyers, Best Lawyers, US News and World Report

butlerrubin.com
(312) 444-9660

Helping clients solve complex issues in underwriting, claims, allocation, coverage, agency, insolvency and finite reinsurance as well as the non-litigation aspects of their insurance and reinsurance relationships.

News & Events

Francine L. Semaya & Peter H. Bickford

Regulatory News

Cybersecurity

At the NAIC Summer meeting in Philadelphia (August 5-8), the NAIC focused on Big Data at the Innovation and Technology Task Force. In addition, a significant amount of attention focused on Cybersecurity, where the Working Group discussed and received additional comments on its 5th version of the draft "Insurance Data Security Model Law". Insurers and other insurance entities encouraged the NAIC to follow the footprint of New York's Regulation 3 NYCRR 500, entitled "*Cybersecurity Requirements For Financial Services Companies*", which went into effect on March 1, 2017, to develop consistency across state lines.

Meanwhile, on July 31, 2017 New York continued to develop its model by launching a new online portal to securely transmit in real time all notifications required under its cybersecurity regulation. This portal is available for any notifications required to be filed, including notices of certain cybersecurity events within 72 hours from a determination that a reportable event has occurred.

Covered Agreement Update

On Friday, July 14, 2017, the U. S. Treasury Department and the Office of the U.S. Trade Representative (USTR) announced that the U.S. will sign the "*Bilateral Agreement Between the European Union and the United States of America on Prudential Measures Regarding Insurance and Reinsurance* (the "*Covered Agreement*"). In addition, the Trump administration plans on issuing a policy statement on the implementation of the Covered Agreement. The joint statement issued by the U.S. Treasury and the USTR, provides that:

"This is an important step in making U.S. companies more competitive in domestic and foreign markets and making regulations efficient, effective and appropriately tailored." Furthermore, the bilateral agreement benefits the U.S. economy and consumers by affirming America's state-based system of insurance regulation, providing regulatory certainty and increasing growth opportunities for U.S. insurers."

The initial reaction from the reinsurance and large insurance company industry is extremely positive. The NAIC President issued a brief statement acknowledging the recognition in the joint statement that "affirmed the primacy of state insurance regulation." The NAIC is also hopeful that the policy statement to be issued will "clarify key elements in the Covered Agreement." The question remains whether the Covered Agreement does in fact grant "Equivalency" to the U.S. state insurance regulatory scheme. It is not clear as of this writing what the "policy statement on the implementation of the Covered Agreement" will provide.

Industry News

You know it is a relatively modest M&A season when the more interesting notices are regarding the completion of deals previously announced in our last column. For instance, in July it was announced that the $4.9 billion acquisition by Toronto-based **Fairfax Financial Holdings, Ltd. ("Fairfax")** of Swiss-based **Allied World Assurance Company Holdings, AG** had been completed.

Also, in the Spring Issue we reported on the proposed merger of the **National Association of Professional Surplus Lines Officers ("NAPSLO")** and the **American Association of Managing General Agents ("AAMGA")** into a new wholesale, specialty and surplus lines insurance trade association to be called the **Wholesale and Specialty Insurance Association ("WSIA")**. In July the members of both organizations overwhelmingly approved the merger, which became effective August 1, 2017.

WSIA will be governed by a board of directors that includes both legacy organizations' members. **Corinne Jones**, executive vice president of operations for AmWINS Access Insurance Services, will serve as president. "It is an honor to serve as the first president of WSIA, and I'm looking forward to the work that's ahead," Jones said in a statement. "This merger is not simply a refresh or rebrand of two legacy organizations, but a brand-new association dedicated to developing and strengthening the wholesale, specialty and surplus lines insurance industry."

There were a few acquisitions of note in the second quarter including the following:

In May, **Intact Financial Corp. ("Intact")**, the largest provider of property/casualty insurance in Canada, announced it was purchasing US specialty insurer, **OneBeacon Insurance Group, Ltd.**, for US$1.7 billion. Toronto based **Intact** said that the acquisition will make it a leader in North American specialty insurance with over C$2 billion of annual premiums.

In July, **AXIS Capital Holdings Ltd. ("AXIS")**, which had attempted to purchase PartnerRe in 2015 only to lose out to EXOR SpA, announced that it was acquiring **Novae Group, plc**, a specialty reinsurer that operates through Lloyd's of London, for $604 million. According to **AXIS**, the transaction "adds scale and breadth to the international specialty insurance business of **AXIS**, creating a $2 billion insurer in

Present Value (continued)

the London specialty market anchored as a top 10 insurer at Lloyd's." Based on 2016 results, the combined companies will create a global specialty reinsurer with gross written premiums in excess of $6 billion.

Also in July, Virginia-based **Markel Corporation ("Markel")**, a diverse financial holding company serving a variety of niche markets, announced the acquisition of Texas-based **State National Companies Inc. ("State National")** for $919 million.c According to **Markel's** release on the acquisition, "**State National** is the largest and longest standing pure play U.S. insurance fronting business with approximately $1.3 billion in gross written premium (2016) and more than 60 programs. **State National** is also the leading collateral protection insurance provider in the U.S."

People (and firms) on the Move

Joseph Monahan, who was until recently a member and secretary of AIRROC's Publication Committee for many years, has moved his insurance litigation practice from Saul Ewing LLP to **Vintage Law, LLC** in Ardmore, PA near Philadelphia (www.vintage-law.com), where he will continue to handle insurance coverage and bad faith litigation, as well as other commercial disputes. Joe can be reached at jm@vintage-law.com.

Nick Horsmon, formerly with **Mound Cotton Wollan & Greengrass LLP**, has enrolled in an MBA program at the **University of Oxford's Said Business School** in the United Kingdom. Nick's studies will focus on management and regulatory consulting in the insurance/reinsurance sector as well as Insurtech entrepreneurship. Nick will remain an active member of AIRROC's Publication Committee. Nick can be reached at nhorsmon@law.gwu.edu.

In the Spring issue, we reported that AIRROC partner law firm, Chicago-based **Freeborn & Peters LLP ("Freeborn")**, had expanded into the New York City market through its combination with **Hargraves, McConnell & Costigan P.C.** Now **Freeborn,** which has been a long-standing supporter of AIRROC initiatives over the years, has expanded into the Southwest by opening its first Florida office in Tampa to add litigation strength and geographic capacity. In addition to its headquarters in Chicago, **Freeborn** now has offices in Springfield, IL, Richmond, VA, New York City and Tampa, FL.

While **Freeborn** expands, **Chadbourne & Parke** ended its 115-year run as an independent firm when its merger with global giant **Norton Rose Fulbright** was completed on June 30, 2017. The name also disappeared with the merger. ●

If you are aware of items that may qualify for the next "Present Value," such as upcoming events, comments or developments that have, or could impact our membership, please email Fran Semaya at flsemaya@gmail.com or Peter Bickford at pbickford@pbnylaw.com

MARK YOUR CALENDAR

STROOCK

Tailored Expert Legal Advice to the Insurance Industry

Laura Besvinick
lbesvinick@stroock.com

Beth K. Clark
bclark@stroock.com

Michele L. Jacobson
mjacobson@stroock.com

Robert Lewin
rlewin@stroock.com

Lewis Murphy
lmurphy@stroock.com

Bernhardt Nadell
bnadell@stroock.com

Julie E. Nevins
jnevins@stroock.com

STROOCK & STROOCK & LAVAN LLP
LOS ANGELES • MIAMI • NEW YORK • WASHINGTON, DC
180 MAIDEN LANE, NEW YORK, NY 10038-4982

WWW.STROOCK.COM

Commutations & Networking Forum

October 15-18, 2017

The Heldrich, New Brunswick, NJ

AIRROC

NJ 2017

- *2 Full Days for Meetings*
- *1 Day of Education with CLE*
- *5 Meals and Social Functions*
- *Unlimited Networking Potential*

For further information contact

Carolyn Fahey carolyn@airroc.org

Register Online at www.airroc.org

Full access registration: Prior to Sept. 15th
$695 for AIRROC Members and Partners
$995 all others
(after Sept. 15 $795 member, $1095 others)

www.airroc.org

AIRROC