

ALASKA LEGISLATURE COMMITTEE FILES 1983-1988 00/2

4160 SLAB INSURANCE INFORMATION 1040

Reinsurers were the first to put the brakes on the cycle. Reinsurers typically receive a percentage of the premium and take a percentage of the risk of the primary insurer. Figures show that reinsurers were hardest hit in the loss ratio column. When they gave primary insurers the ultimatum across the board of more premium or no reinsurance, premiums increased.

✓ Year-end 1984 insurance company results showed severe losses. More importantly the losses decreased policyholder's surplus, the ultimate measure of an insurers ability to write new insurance policies. With the substantial decrease in surplus, insurers were unable to write as much insurance in 1985 as they had in the previous year. Other insurers closed their doors because of insolvency or to pursue other more profitable ventures.

✓ As a result of the insurers' folly in pursuit of investment profits and their unwillingness to increase rates in the face of aggressive competition during the past few years, we are experiencing two distinct problems today: (1) insurance industry capacity falls short of the national demand for insurance, and (2) insurance rates which have been depressed for six years are taking a quantum leap in 1985 in order to be adequate for current year losses. Profit, if any, will go to rebuilding surplus which has the effect of increasing insurance capacity.

HOW ALASKA FITS INTO THE NATIONAL SITUATION

Despite its geographic size, Alaska accounts for an almost insignificant portion of insurance premium in the U.S. marketplace. Even in the period of excess capacity and cut rate premiums, the Division of Insurance ✓ devoted substantial efforts toward attracting insurers to do business in Alaska. High costs relative to the small volume, lack of local servicing and the perception of Alaska in the lower 48 are constant obstacles to attracting new markets. Alaska is the last state market many insurers enter and the first to feel the company's consolidation of business efforts. Generally, insurers fared better in Alaska, on a pure loss ratio basis, than the national average.

The Division of Insurance believes its long-term efforts to encourage insurers to operate profitably has lessened the present insurance crisis to a large degree. Since Alaska business is largely insignificant to many insurers, any move to pressure them into areas they perceive to be unprofitable or potentially volatile may cause them to shift their underwriting to another part of the country. To the extent Alaska cultivates insurers and encourages their participation, capacity may be attracted here from other states. At least for the present time total insurance capacity does not exist in sufficient amount to satisfy the national need. The particular efforts and conditions in each state, therefore, affect the amount of insurance capacity dedicated by insurers to that state.

INSURANCE INDUSTRY RESPONSES

Insurers interviewed by the Task Force staff made recommendations that they considered would improve the availability of insurance in Alaska. The highest priority was related to reforms in the civil justice system that would give stability and predictability to liability claim settlements and judgments. Joint and several liability, caps on awards for wrongful death and pain and suffering, disclosure of collateral source recoveries and prejudgment interest, were high on the insurers' list. The industry was severely impacted by the recent announcement by the chairman of Lloyds of London that Lloyds would not insure casualty risks in the U.S. after this year because of their frustration with the U.S. legal system. Insurers have responded by asking for tort reform and by switching to a "claims made" form of liability policy. "Claims made" policies respond to losses reported during the policy period only as opposed to covering claims which occur during the policy period but are reported years later. The full impact of the new form will only be known after policies have been in effect for several years. ✓

Insurers did not hesitate to point out the seriousness of their efforts to turn massive losses into profit in the short-term. Further losses would put insurers out of business. Participation in guarantee association programs for insolvent insurer bailout would exacerbate the problems for currently marginal insurers.

Insurers stated that they would devote their limited capacity to the best risks and coverages. Any line they felt had potential for unexpected claims or catastrophic loss would be avoided or priced to guarantee profitability. Being forced to unwillingly write coverage for classes of insured that have an unpredictable risk and/or the potential for catastrophic loss or to subsidize the rate, would be cause for the insurer to reevaluate their overall profit potential in that state and to readjust overall company strategy. Insurers are also holding back until they determine the cost and availability of their reinsurance and the exclusions it contains for certain types of risks.

DIVISION OF RISK MANAGEMENT RESPONSE

State insurance programs have also been adversely affected by the present insurance market situation. Public entities, including states and municipalities of all sizes, have been singled out by the insurance industry as difficult risks due to type and variety of exposures and deteriorating claims experience. Risk Management is well aware of the current market problems, and they have empathy for others caught in the same problem.

They see risk management or "management of risk" as a program requiring three elements of attention: (1) insurance, including various levels of self-insurance; (2) claims control to fairly and quickly adjust or adjudicate claims against the State; and (3) loss prevention or loss control programs designed to reduce the number and severity of claims. As we are

forced to higher levels of self-insurance, loss prevention programs become paramount in control of costs. Risk Management is now providing agencies with useful claims reports and analysis on a quarterly basis. This should help locate and identify problem areas that can be corrected. Another important segment of loss control involves State contract insurance requirements. These are necessary to prevent the State from having to pay or defend claims caused by negligent acts of independent contractors unless the State by its own negligent acts is also responsible.

The Division of Risk Management is in complete agreement with Task Force recommendations concerning reassessment and possible revision of State contract insurance requirements.

Risk Management has been working with State agencies on revisions of insurance requirements for a number of months. They have addressed these issues both on an individual contract basis, and, where applicable, on a specific program basis. They are also in the process of revising several elements of Appendix B ("boiler plate" insurance requirements for many agency contracts) to help alleviate the problem where these insurance requirements are in general use.

Due to the great variety of State contracts, it is very difficult to adopt one program or even a series of programs that fit the needs of all contract agreements. They, therefore, look upon "boiler plate" requirements as "guides" and Risk Management will work with any of the State agencies to consider revisions when necessary.

Risk Management services should be looked upon as a resource available to all State agencies or contractors. They are willing and anxious to meet with agency contract officers or other personnel at any time to explain the State program and to understand or assist with agency insurance problems.

They believe it is in the agencies' best interests to remain involved in insurance decisions or deviations because the agencies attest better to the type of work involved, inherent exposures, possible statutory requirements, and the importance of the program or contract "to the best interests of the State."

To reiterate, they cannot emphasize too strongly that "boiler plate" insurance requirements are considered by Risk Management as "guides." While in many cases these requirements have been set for good and sufficient reasons, there are also many types of contracts depending on supervision, type of work, and other reasons that, as a practical matter, call for modification of such requirements. When these cases are called to Risk Management's attention, they have been recommending accordingly.

The present insurance crisis will probably remain with us for another two or three years, especially in the areas of professional or hazardous liability and property exposures. Recognizing this market situation, Risk

Management will continue to respond to the difficulties the private sector has in meeting State insurance requirements. So far, in most instances they have been able to agree on alternatives acceptable to both parties.

MARKET ACCESS PROGRAM

After the first Task Force meeting, many individuals have called the Division of Insurance for assistance in finding insurance coverage.

The division undertook on an experimental basis a market availability program to these displaced persons. In the majority of cases, diligent market search turned up coverage for these people. Although very time consuming and insufficient on a per policy basis, this experiment proved that few reasonable risks are unable to be insured by someone at some price. The division is working on several ideas which may increase the efficiency of this program in order to make it relatively cost effective.

CADIS

(Coordination of Alaska Day Care Insurance Search)

EVOLUTION AND CONCEPT

During February and March 1985, the division became aware of a growing problem for day care operators attempting to purchase or renew day care liability insurance. Numerous articles have been written on the subject in a variety of publications.

Since the time that the division became aware of the problem, we have attempted to identify potential markets and share the information with both insurance producers (insurance agents and brokers) and day care operators. We have also advised operators how to approach the market.

We understood from the beginning that this challenge could not be met with empty rhetoric. It has to be met with a program of active cooperation by all involved parties. We have used this opportunity to create and test a pilot program wherein we attempt to identify markets, identify their needs, and bring the buyer, intermediary and seller together. This approach is also useful in attracting new markets. It has, in fact, already attracted a market that was not generally available prior to the development of CADIS.

Division personnel have spent many hours talking to individual operators, speaking before groups, meeting with other State agencies and discussing the situation with insurers. From this has come an understanding of the problem and the seeds of how the challenge might be approached.

It became clear in talking with operators that, at the very least, underwriters must be suffering from a severe information deficiency. It was also discovered that much information was available from the permitting and licensing agencies. CADIS attempts to get the information flowing to

those needing it to make decisions. It also helps the operator to understand the insurers concerns and needs, and shows how the information gap can be bridged.

MECHANICS OF CADIS

The approach developed in cooperation with the Department of Health and Social Services and the Department of Education starts with the day care operator. Each licensed day care operator has been informed by the appropriate regulatory agency of the existence and availability of CADIS. The operators have been advised how they might participate in CADIS.

If a licensed operator wishes to participate in CADIS, the operator has been told that his or her insurance producer should be supplied with the following documents:

If the licensed day care operator is regulated by the Department of Health and Social Services, a copy of the evaluation report completed by the licensing worker of the Department of Health and Social Services.

If the licensed day care operator is regulated by the Department of Education, a copy of the application for pre-elementary certification, the pre-elementary certificate, and the written on-site review inspection evaluation of the preschool facility, if available (some preschools do not have this report).

In addition, the following must be included in all cases:

A copy of the fire and sanitation inspection report.

Pictures of the facility showing pertinent underwriting features:

1. The front of the facility with fence and fire hydrant, if available
2. General exterior layout
3. Inside of the building showing general layout
4. Kitchen area
5. Playground equipment
6. Any barriers or features designed to prevent children from reaching items that are hazardous to their health or safety
7. Stairs, if any

After the insurance producer receives this packet, the producer can contact this office and request identification of those companies currently accepting the particular kind of insurance under CADIS. The producer can then submit the packet to the companies with the appropriate application. We are asking the producers to advise us of the results as a means to monitor the success of the program.

There is no guarantee that coverage will be granted by the insurer, but such a package will be more attractive than that generally provided before this program was designed. We have already received favorable comments

from one insurer concerning the quality of submissions. It should be clearly understood that this is a purely voluntary program. It is not an assigned risk plan and should not be characterized as one. At this stage, we believe that the program can be endangered by misconception, so we are treading very cautiously. We believe that the program is working, even at this early stage.

EFFECT ON PARTIES

The effect of this effort of the various parties is, in itself, of value.

The licensed day care providers can receive assistance in locating coverage needed to maintain, license and operate their business. Initially, the program will put them in touch with admitted companies through their agent or broker. This has the advantage of having the protection afforded by the Alaska Guaranty Association Act. These will be companies subject to rate and form review, which should reduce the potential for outlandish pricing.

insurance producer has the advantage of being provided the most desirable of situations, an informed buyer with a complete submission package and the markets to approach with that package. This should result in substantial reductions of the time required to put together the materials needed when approaching an underwriter. The producer also has the attraction of using an admitted market with its known protections. That represents one less exposure to the producers surplus lines brokers bond.

The insurance company will receive submissions that will be unusual in quality resulting in less effort in putting together the information needed to underwrite properly this class of business. This approach will make the resulting portfolio of risk more attractive to the insurers/reinsurers. Hopefully this should stabilize the market somewhat. It will give them insureds that have a better understanding of the risk the insurer is taking and one who is willing to reduce the hazards that could result in loss. This will certainly be attractive to an insurer willing to look at this line of insurance.

WHAT NEXT

At this time, the program is limited to licensed day care operations. To some degree it can help preschools regulated by the Department of Education. We are exploring expansion of the program to operators not subject to licensure. We are also looking to the surplus lines market for a broader base of coverage availability. The program will undoubtedly be subject to fine tuning for some time.

LEGISLATION

Legislation has been submitted which will require insurers to give longer notice of cancellation to insureds and return unearned premium prior to the effective date of cancellation. This will allow additional time to find replacement coverage and provide funds to the insured to apply to the new policy.

ALTERNATIVES FOR INSURANCE

✓ Within staff time and personnel limitations, the Division of Insurance has provided assistance to entities seeking alternatives to commercial insurance such as self-insurance, formation of captive insurers or pools and risk avoidance through loss control.

The Task Force believes that continuation of these ongoing responses is appropriate.

LICENSE AND CONTRACT REQUIREMENTS

✓ We encourage all State agencies to review insurance criteria they impose on others as license requirements or contract requirements, to determine that they are reasonable and appropriate.

Liability awards have increased at a much greater rate than the cost of living or inflation rate and at a greater rate than anticipated by insurers. The civil justice system has gradually expanded theories of liability so that more acts or failure to act are found to be negligent conduct. As insurers are asked to accept this transfer of negligence from individuals, they must anticipate the probable future expansion of legal theories in order to properly charge for the insurance product.

Insurers are also responding to expansion of legal theories with new policies and language which limit coverage for some exposures, in some cases limiting the time in which claims may be covered, and limiting the cost of defense and attorney fees. In effect, they are refusing to accept the transfer of certain types of risk that they feel are unpredictable or unreasonable at this time.

Individuals find that they are less able to transfer the cost of their own negligence to insurers. The punishment afforded by punitive damages is more likely to be assumed by the negligent person than by an insurer in the future.

✓ Insurers having hit their financial low in 1985 have adjusted their practices and anticipate some profits in the future. This has caused insurance stocks to increase in value over prior year lows. As insurers build up their surplus through profitable underwriting, insurance capacity will increase.

THE TASK FORCE RECOMMENDS THAT THE DOCUMENTS COLLECTED DURING THE TASK
FORCE RESEARCH BE READ BY ANYONE WHO INTENDS TO PROPOSE A SOLUTION TO THE
COMPLEX PROBLEM WE ADDRESS AS THE INSURANCE CRISIS.

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Tort Reform:

**A Comprehensive Solution
To The Crisis in
Civil Justice and Insurance**

733 1-7-2018

**The Citizens Coalition for Tort Reform
738 H Street, Suite 100
Anchorage, Alaska 99501**

Civil Justice: Unnecessarily Inefficient and Costly

A tort is literally a wrong. Tort actions seek to redress wrongs in a court of law. A close look at how the tort reparations system works in 1986 reveals that it's not working. The system is mired in inefficiency, punctuated with greed and demonstrably unable to deal with the great bulk of its caseload in a timely and fair manner.

It often takes three to five years to settle a case. Only 30 to 40 per cent of the costs of reaching a settlement go to victims, and that does not include costs of the court system.

The economic costs to society are staggering and difficult to precisely quantify. It is clear that the hefty increases in insurance rates affect the price of nearly every product or service we purchase. *It is a tax—a tax imposed by default, without full political and social evaluation of its impact.*

A society that can send men to the moon ought to be able to settle liability claims in a more effective way. Most other western countries do.

The Comprehensive Solution

The tort reparations system needs a thorough overhaul. Alaska can no longer afford the luxury of having its courts administer a giant lottery where a victim may win a fortune, but more likely will find the pot at the end of the rainbow empty.

Alaska and other states have been dabbling in tort reform for ten or 15 years and there is adequate evidence major changes in the tort reparations system are essential. The fundamental goal of tort reform is to restore predictability to the tort system.

All manner of solutions to the insurance crisis have been proposed including tighter regulation of insurance companies, state-backed insurance funds and reform of the tort system. More regulation may be useful and a state-supported fund may provide temporary relief to some. However, *without stopping the flagrant abuses of the tort system, liability will continue to be a serious problem for business, government and consumers.*

The following proposals address the major faults of the tort system. They are intended to restructure the process to allow more efficient and effective dispute resolution. These reforms would get a higher proportion of damage payments into the hands of plaintiffs while protecting the rights of defendants and the public which ultimately pays the bills.

Joint and Several Liability

If more than one defendant is found partly responsible for an injury, each can be held "jointly and severally" liable for all damages. This means that if one defendant is unable to pay, the other defendants must pay the entire award. *Responsibility should be apportioned according to the degree of fault and each defendant's requirement to pay damages should reflect his share of responsibility for the injury.*

Noneconomic Awards

Noneconomic awards compensate a victim for intangible losses— loss of consortium, pain and suffering, traumatic experiences and other things for which no established economic value exists. *A limit on this kind of arbitrary award will help establish consistency and fairness in this no-man's land. We suggest a maximum award of \$250,000 per incident. The U.S. Supreme Court has upheld such a law in another state.*

Structured Settlements

Damages awarded for predicted future losses should be computed at their present economic value. The injured party would have an option to accept lump-sum payment at present value or accept structured payments running over a period of years and equal to the total award. *This guarantees financial support and care for a long time, often for life.*

Collateral Income Sources

Insurance payments which have been made to an injured party should be disclosed to the jury and should be protected from recovery in the event the victim receives an award. *Under current rules, juries cannot be told about existing medical or other insurance coverage.* If the injured party receives an award, the insurance companies which have fulfilled their obligations may sue for repayment from the victim.

Sliding Contingency Fees

Plaintiff attorneys today can take upwards of 40 percent of a total award verdict. A sliding scale will increase the proportion of the award which actually goes into the victim's pocket as the size of the award increases. *Where the sliding scale is now in effect, lawyers still work on contingency fees, but victims recover a greater share of awards. The U.S. Supreme Court has upheld this principle.*

Itemized Jury Awards

Jury awards for damages should specify amounts for monetary losses, noneconomic losses, future losses, past expenses and other losses. *This will help to eliminate arbitrary awards based upon showmanship or prejudice and introduce an element of rationality in award construction.* An itemized award which is grossly unfair to either the victim or defendant can be more effectively appealed than a lump-sum award.

Rule 82

Rule 82 is unique to Alaska. It is a device to increase attorneys' fees above the agreed level by order of the court. The rule was originally adopted to apply in certain public interest lawsuits, but it has been extended to cover most liability suits. *It simply adds up to 10 percent to the cost of awards without serving the originally intended public purpose.*

Arbitration

Tort litigation is time consuming and expensive. Claims under \$50,000 should be required to go to arbitration before being heard in Superior Court. Either party would be free to appeal the arbitration decision to the courts, however the results of the arbitration could be admitted in evidence at any subsequent trial. *Experience indicates that the effect would be to reduce the number of cases going to court, lower the costs of resolution and ultimately get more money into the hands of victims without great delays.*

Notice of Policy Cancellation

Individuals, businesses and professionals have been suddenly cut off from their insurance programs. *Companies should be required to give 60-day notice of changes in coverage.* This would avoid drastic disruptions in people's ability to earn a living.

Pre-judgment Interest

Interest is often paid on awards. It should accrue from the date an action is filed. Currently, interest accrues in many cases from the date of the occurrence—even if no claim is filed for years. *A defendant should not be required to pay interest covering that period of time when he may have had no knowledge of his liability.*

Wrongful Death Statute

Where there are no dependents, wrongful death monetary awards should be limited to \$25,000. *A wrongful death is always unfortunate, but it is questionable public policy which permits—even encourages—distant relatives and lawyers to reap a windfall at the expense of other policy holders and the public.*

Punitive Damages

Punitive damages is the civil justice system's way of punishing defendants for conduct particularly offensive to society, therefore, punitive damages should be paid to the State of Alaska. *Society as a whole should share the benefits of punitive damages (which are rarely covered by insurance).*

Statute of Limitations

The current statutes of limitation must be clarified to make sure that lawsuits are brought within a reasonable time. Recent court decisions make it possible to file suits in the distant future, making risks totally unpredictable. The alternatives to a functional statute of limitation are insurance devices which effectively establish these limits without benefit of public policy considerations. *These devices (claims-made policies) can cause severely reduced public protection and even reduced availability of some goods and services.*

Frivolous Suits/Untrue Allegations

An Indiana woman purchased a box of Cracker Jacks. The usual prize was not in the box, so she filed suit against the manufacturer. Someone had to defend the suit, even if it was only to ask for dismissal. A responsible legal system should require that plaintiff attorneys certify that the facts have been reviewed and there is reasonable and meritorious cause for filing the action. This certification should be made in writing. *Rules have been adopted by the U.S. Supreme Court and ten states to curb these abuses of our court system.*

Full Disclosure

Essential data should be made available to state regulatory authorities on a quarterly or semi-annual basis, to allow proper regulation of regulated companies regarding reserves, premium rates, loss ratio, investment and other data so as to properly protect people of Alaska.

Comparative Negligence v. Contributory Negligence

When the claimant has contributed to the accident, his or her degree of fault should diminish the award proportionate to the degree. This would reduce damages where the claimant contributed to the mishap. As an example, in single car-auto accidents, cities have been successfully sued by the drivers for faulty road design or maintenance, even where the drivers have been proven to have been drinking or using drugs.

Who is the Citizens Coalition for Tort Reform?

The Citizens Coalition for Tort Reform is an organization composed of representatives from a broad cross section of Alaskan businesses and professions.

They include these companies, associations and agencies:

Alaska Air Carriers	Alaska Visitors Association
Alaska Broadcasters Association	Anchorage Board of Realtors
Alaska Chapter, American Institute of Architects (AIA)	Anchorage Restaurant and Beverage Association (ARBA)
Alaska Dental Society	Cabaret Hotel and Restaurant Retailers (CHAR)
Alaska General Contractors	Childbirth Educators
Alaska Chapter, American Optometric Association	Daycare Operators Association
Alaska Movers Association	Fairbanks North Star Borough
Alaska Oil Marketers Association	Financial Managers
Alaska Rental Association	Hotel and Motel Association
Alaska Section, Fairbanks Branch, American Society of Civil Engineers	Insurance Brokers and Agents Association
Alaska Society of Professional Engineers	Nurse Midwives Association
Alaska State Health Association (Hospitals)	Pension Consultants
Alaska State Medical Association	Professional Physical Therapists Association
Alaska Support Industry Alliance	Risk Management Association
Alaska Truckers Association	Southern Alaska Association of Life Underwriters

CITIZENS COALITION FOR TORT REFORM, inc.

"voices raised in unison.."

1991 10 29

TO: ALL LEGISLATORS

FROM: CITIZENS' COALITION FOR TORT REFORM

SUBJECT: ENCLOSED DATA FOR YOUR USE AND REVIEW

Thanks,

Al Tamagni, Sr.
Chairman

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TORT REFORM -- A COMPREHENSIVE SOLUTION TO THE INSURANCE CRISIS

Introduction

THE TAX THAT SKIRTS THE TAX COLLECTOR

A tort is literally a wrong. Tort actions seek to redress wrongs in a court of law. A close look at how the tort reparations system works 1986 reveals that it's not working. The system is mired in inefficiency, punctuated with greed and demonstrably unable to deal with the great bulk of its caseload in a timely and fair manner.

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THE CITIZENS COALITION FOR TORT REFORM
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(907) 276-1135

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(907) 276-4600

A COMPREHENSIVE LEGISLATIVE SOLUTION TO THE INSURANCE CRISIS

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Interest is often paid on awards. It should accrue from the date an action is filed. Currently, interest accrues in many cases from the date of the occurrence - even if no claim is filed for years. *A defendant should not be required to pay interest covering that period of time when he may have had no knowledge of his liability.*

WRONGFUL DEATH STATUTE

Where there are no dependents, wrongful death monetary awards should be limited to \$25,000. *A wrongful death is always unfortunate, but it is questionable public policy which permits -- even encourages -- distant relatives and lawyers to reap a windfall at the expense of other policy holders and the public.*

PUNITIVE DAMAGES

Punitive damages is the civil justice system's way of punishing defendants for conduct particularly offensive to society., therefore, punitive damages should be paid to the State of Alaska. *Society as a whole should share the benefits of punitive damages (which are rarely covered by insurance).*

STATUTE OF LIMITATIONS

The current statutes of limitation must be clarified to make sure that lawsuits are brought within a reasonable time. Recent court decisions make it possible to file suits in the distant future, making risks totally unpredictable. The alternatives to a functional statute of limitation are insurance devices which effectively establish these limits without benefit of public policy considerations. *These devices (claims-made policies) can cause severely reduced public protection and even reduced availability of some goods and services.*

FRIVOLOUS SUITS/UNTRUE ALLEGATIONS

An Indiana woman purchased a box of Cracker Jacks. The usual prize was not in the box, so she filed suit against the manufacturer. Someone had to defend the suit, even if it was only to ask for dismissal. A responsible legal system should require that plaintiffs attorneys certify that the facts have been reviewed and there is reasonable and meritorious cause for filing the action. This certification should be made in writing. Rules have been adopted by the U.S. Supreme Court and ten states to curb these abuses of our court system.

FULL DISCLOSURE

Essential data should be made available to state regulatory authorities on a quarterly or semi-annual basis, to allow proper regulation of regulated companies regarding reserves, premium rates, loss ratio, investment and other data so as to properly protect people of Alaska.

TRB

FROM WASHINGTON

THE TORT EXPLOSION

A court in Kansas has awarded ten million dollars, including eight million dollars in punitive damages, to a man who got polio after his daughter took the Sabin oral polio vaccine. A jury ruled that it is "outrageous" to sell the Sabin vaccine when the Salk vaccine is safer. The Salk vaccine is safer, in that the Sabin is a live virus that causes about four polio cases a year out of 24 million doses. On the other hand, the Sabin is more effective. Ten or 20 Americans a year get polio now, compared to several thousand

a year during the Salk era. That, among other reasons, is why it is official U.S. policy to prefer the Sabin vaccine. But if this case becomes a precedent, no one will make the Sabin vaccine and that policy will be overruled.

When people fret about unelected judges making important social policy, they usually have in mind the Supreme Court's rulings about the Constitution. But another kind of judicial activism is coming to have an equal or greater effect on life in America. That is the explosion in tort law, set off primarily by state courts. Fear of lawsuits and inability to get insurance are affecting drug companies, municipalities, corporate directors, doctors, rock concert promoters, and others as surely as if the government had issued new laws or regulations. Many of these new judge-made regulations are ones no sane government would ever consider.

A Supreme Court ruling can take effect almost overnight. Tort law, by contrast, operates on a long fuse. A new development can take a couple of decades to percolate through the legal system, drive up insurance rates, and begin to affect everyday life. Little-remarked decisions of the past two decades are

only now coming back to haunt us.

In one sense, the coming tort crisis is just another example of the paradigmatic problem of modern American government: our inability to take action for the general public good if it harms identifiable individuals. Trade protectionism, tax loopholes, and overgenerous entitlements are all part of the same dilemma. But courts add their own special madness. They blithely set policy on complex subjects about which they have no expertise. They are institutionally inclined to focus on the costs of whatever behavior they have under scrutiny, without regard to the benefits.

Under our federal system, the same policy issue can be litigated again and again across the land, with similar or opposite results. However, since the plaintiffs tend to be local and the defendants from out-of-state, there is an inevitable tendency to follow the lead of whatever state has been most aggressive in finding liability.

The idea of tort law is that if my misbehavior causes you harm, I should pay you money to make up for it. Trial lawyers have worked wonders to overcome all these tiresome limitations—fault, causation, harm, damages—in recent years. Punitive damages—payments beyond all compensation for actual loss—used to be reserved for virtually criminal conduct. Now they are almost routine, and can be assessed again and again when a product or incident leads to multiple lawsuits. Courts have become far more imaginative in their definitions of actual harm as well, awarding large sums for emotional distress, fear of getting cancer (as opposed to actually getting cancer), and so on. Where it's impossible to know whether the defendant's activity actually caused the plaintiff's harm—did the victim get cancer from living downwind of a nuclear testing site, or just from living?—courts have held that the defendant must prove it *isn't* responsible, which is impossible.

But the biggest advances have been made in dispensing with the notion that you must have done something wrong in order to be held liable. No human endeavor is risk-free. If you can't plausibly be accused of failing to eliminate all risk, you can be accused of "failure to warn" of the risk that remains.

The first successful suit against the Sabin vaccine, in 1968, turned on the manufacturer's failure to warn recipients of the infinitesimal chance of catch-

continued on page 50

Why did America's business elite fall for a \$200-million scam?

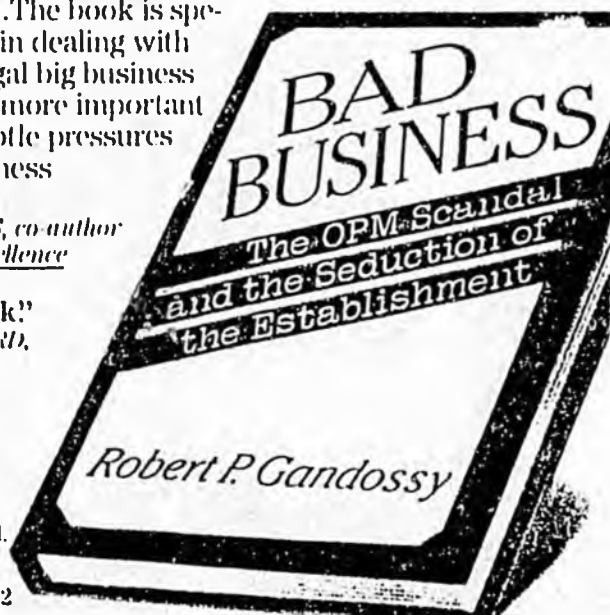
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ing polio from it—as if this would lead any rational person to expose his children to the far greater risk of catching polio from *not* taking it.

More and more, though, any pretense of finding fault is abandoned and manufacturers of inevitably risky products are held “strictly liable” for any harm that comes from them. The theory is that they will absorb the cost and spread it around to all users. Whatever the theory, it is no defense that your product or activity is approved by the government agency that supervises such things. A chemical company recently was held liable for “mislabeling” a can of paraquat poison, even though the wording was not merely permitted but actually required by the Environmental Protection Agency.

In real life, any theory will do as long as it gets the case to the jury, whose natural sympathies will usually produce a large judgment without much concern for the legal technicalities. Fear of juries leads defendants to settle suits, whatever their merits. High settlements lead to skyrocketing insurance rates. And soon so much cost is being absorbed that the activity in question, be it practicing gynecology or manufacturing a vaccine or being on the city council, is no longer economically practicable.

Members of the Reagan administration who are alarmed about this trend regard it resentfully as backdoor government activism. In an era when new regulatory agencies and new social welfare programs don't have a prayer through normal democratic channels, they see liberal judges and greedy lawyers conjuring up vast schemes for income redistribution and controls on business through the courts. The “tax” that pays for these new programs is huge, but hidden (\$12 for a dose of diphtheria vaccine that cost 15 cents a few years ago), so there is little political resistance. But they fear that the government often will end up footing the bill anyway, by interposing itself between some vital activity and a tort system gone wild. In 1976, for example, the government indemnified all manufacturers of swine flu vaccine. Otherwise, no one was willing to make it.

The irony is that the Reaganites are trapped here by their own dogmatism. The obvious solution to the problem of state courts competing against one another with ever-wackier theories of tort

liability is national legislation setting sensible rules and exempting activities that meet federal standards from the risk of lawsuits. But overruling state law in this way would violate the axiomatic Reaganite belief in “federalism,” while enhancing the power of national regulatory agencies would violate a related taboo. So the Reagan administration supports tort reform, so long as it *doesn't* mandate a uniform national standard.

Meanwhile, the fact that conservatives are alarmed by the tort explosion is no reason that liberals shouldn't be. As it now operates, tort law is more like a lottery than a rational and humane system of justice. Yes, some sufferers receive the balm of money. But people with the identical grievance collect radically different amounts, ranging from nothing if they don't sue (as many don't) to millions if they hit the jackpot with punitive damages. What you can collect depends on all sorts of arbitrary factors such as where you live, the size of the defendant, what judge you get, how much publicity there's been, and so on. It also depends a lot on factors like the amount of your lost earnings and the size of your medical bills. This means that affluent people—who are more likely to sue in the first place—collect more than poor people for the same grievance. Above all, collecting from the tort system depends on having someone to sue. If you just get cancer for no apparent reason, you're out of luck.

Anyway, most of the redistribution in tort law is from everyone else to the lawyers. In all the current litigation over asbestos, for example, the average cost per claim has been \$101,000. Of that, \$37,000 has gone to the defendant's lawyers, \$25,000 to the plaintiff's lawyers, and \$39,000 is left for the plaintiff. These numbers are typical. Studies of different aspects of the tort system always show that lawyers get over half the money.

Worst of all, from the liberal point of view, the tort system teaches a cramped lesson about justice and injustice. Most of the suffering in our society—dreadful diseases, loss of employment, simple poverty, whatever—is part of everyday life, not the result of specific actions that disrupt everyday life. Relief of suffering needn't depend on finding someone to blame. The instinct that says it's wrong for people to suffer unnecessarily should be directed into politics, not into lawsuits.

CITIZENS COALITION FOR TORT REFORM, inc.

"voices raised in unison.."

Hon. Fred Zharoff
Chairman
Senate Labor and Commerce Committee
P.O. Box V
Juneau, AK 99811

Dear Mr. Chairman:

This documentation relating to the testimony of J. Robert Hunter before your Committee on February 26 has just come to our attention. Presumably this information has been turned up by your researchers, but in case it has not, we are offering it to you now.

Briefly, here is a summary of the contents:

A paper refuting the Nader-Hunter challenge on the 1985 profit/loss in the property casualty industry.

An article on the property casualty industry's pre-tax operating loss for 1984 from the March 20, 1985 "Wall Street Journal."

An Insurance Information Institute news release reporting year-end 1984 property/casualty industry operating results.

Sources of data on financial results for property/casualty insurance.

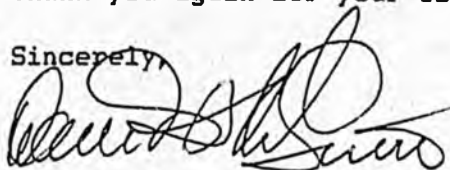
Concepts of profit/loss in the property/casualty insurance industry.

A refutation of the assertion by Mr. Hunter before your Committee that the Canadian Providence of Ontario has had and unsuccessful experience with "tort reform."

The Coalition does not represent the insurance industry nor is it a spokesman for the industry. However, we feel that a sound appreciation of how the industry operates is vital to an understanding of why substantial tort reform is in the public interest. This information from the Insurance Information Institute is presented in that spirit.

Thank you again for your efforts to make sense of this difficult issue.

Sincerely,



David A. McGuire

CITIZENS COALITION FOR TORT REFORM, inc.

"voices raised in unison..."

DOCUMENTATION ON TESTIMONY OF

J. Robert Hunter

Before the House Labor and Commerce
Committee, Judiciary Committee,
Senate Labor and Commerce Committee
and Senate Judiciary Committee
February 24, 24 and 25, 1986

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"voices raised in unison..."

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- ** A refutation of the assertion by Mr. Hunter before your Committee that the Canadian Province of Ontario has had and unsuccessful experience with "tort reform."



Nader-Hunter Challenge on 1985

Profit/Loss in P/C Industry

At a press conference in Washington, D.C. on January 6, 1986, Ralph Nader and Robert Hunter, president of the National Insurance Consumer Organization (NICO), asserted that the property/casualty industry had a profit of \$6.6 billion in 1985 rather than an operating loss of \$5.5 billion, as reported by the Insurance Information Institute.

In interviews with the media on January 6, Dr. Sean Mooney, senior vice president and economist of the I.I.I., and other I.I.I. staff members refuted the Nader-Hunter assertions. By the end of the day, Hunter had lowered his \$6.6 billion profit figure to \$5.0 billion, as reported by The Wall Street Journal, Jan. 7, 1986, page 12.

At his press conference, Hunter claimed property/casualty insurers would earn \$6.6 billion in this way:

	\$ BILLIONS
Operating Loss	-\$5.5
Capital Gains	+ 6.5
Federal Tax Credits	+ 3.5
Dividends to Policy- holders	<u>+ 2.1</u>
PROFIT	\$6.6

In refuting the Nader-Hunter claims, Dr. Mooney noted:

- 1) Hunter accepts I.I.I.'s report of an operating loss of \$5.5 billion based on underwriting and investment performance;
- 2) Nader's Capital Gains figure includes unrealized gains. This is unacceptable because it violates Generally Accepted Accounting Principles as required by auditors and the Securities and Exchange Commission as well as statutory insurance accounting principles. Unrealized capital gains represent increases in the market value of securities which have not been sold. Therefore, the companies have received no money from them. Hence, they are not included in profit and loss data.
- 3) Nader's Federal Tax Credits figure is one developed by NICO and grossly excessive. I.I.I. figures on page 3 are based on nine months of actual data reported by insurers.
- 4) Nader's Dividends to Policyholders entry is wrong. Under general accounting principles, a return to consumers is a price rebate and must be deducted from sales revenues.

The media asked why the industry reported operating figures and not after-tax income at the end of 1985. The I.I.I. year-end press release is based exclusively on data from A.M. Best Company, an independent analytical, rating

and information service organization. These data do not include after-tax income.

When the fourth-quarter data are in, the I.I.I. releases the figures, including after-tax income. (See March 20, 1985, Wall Street Journal story, based on March 19, 1985, I.I.I. release. Copies are attached.)

The I.I.I. reports on after-tax profit or loss on a quarterly basis.

The I.I.I.'s estimates for Profit & Loss in 1985 are as follows:

<u>Profit (Loss) in P/C Industry</u>		
<u>(\$ Billions)</u>		
	<u>1985</u>	
Underwriting Loss	\$(25.2)	<u>Underwriting loss here was supplemented by income from investments (interest and dividends) to produce an operating loss.</u>
Investment Income	19.7	
Net Operating Loss	(5.5)	
Realized Capital Gains*	5.3	However, <u>capital gains</u> primarily from the sale of stocks offset this loss, plus
Tax Credits and Other* Income	1.9	<u>tax credits</u> and other minor income items
		so that
Net After-Tax Income*	1.7	<u>net after-tax income</u> was positive.

*Estimates by Insurance Information Institute.

Why are the I.I.I. figures right and the Nader-Hunter figures wrong? Because with nine months of data available, the net after-tax income was \$1.49 billion. It is totally unrealistic to expect a gain in the last quarter more than three times the size of the gain in the prior nine months.

The Institute is hesitant to estimate the after-tax industry result, but based on nine-month data, the figure should be close to \$1.7 billion -- far below the Nader-Hunter estimate.

Nader and Hunter question whether there has been a litigation "explosion" in the U.S.

There are many facts to demonstrate the increase in litigation in the U.S. over the last few years as well as the increase in the cost of the tort liability system.

-- Million-dollar verdicts awarded in the United States skyrocketed to 251 in 1982 from one in 1962 and to 360 in 1983, the latest year for which figures are available. The lure of jumbo awards in civil suits often contributes to increased litigation.

-- Civil suits filed in state courts rose 22 percent from 1977 to 1981 and appeals climbed 32 percent. Civil case filings in federal district courts soared to 206,000 in 1982 from a mere 35,000 in 1940. Last year there was one private civil lawsuit filed for every 15 Americans.

-- In the 15 years Chief Justice Burger has been heading the Supreme Court, federal court case filings have risen nearly two and a half times as fast as the population.

-- A 1984 Rand study of thousands of asbestos-related lawsuits showed: Cases closed took an average of two years and eight months, with 11 percent taking six years. How much did victims get? Only 37 cents of each dollar paid. The other 63 cents went for legal fees.

Pre-Tax Operating Loss for '84 Is Posted By Property Insurers

By a WALL STREET JOURNAL Staff Reporter

NEW YORK — The nation's property-casualty insurance industry posted a pre-tax operating loss of \$2.9 billion last year, the largest in its history. In 1983, the industry had pre-tax operating profit of \$3.04 billion.

After tax credits and capital gains, however, the industry last year posted net income of \$1.94 billion, down 68% from \$6 billion in 1983.

Such results were expected. Last December, the Insurance Information Institute, a trade group, predicted that the property-casualty industry would post a net loss for 1984. But insurers' tax credits and capital gains both proved to be larger than anticipated, producing net income for the industry rather than a loss, Sean Mooney, the institute's economist, said.

The results released by the institute are based on data from companies representing 97% of the nation's property-casualty premium volume. They were compiled by two other trade groups, the Insurance Services Office and the National Association of Independent Insurers.

Based on the size of the 1984 operating loss, Mr. Mooney said, last year was the property-casualty industry's worst ever. He said the losses surpassed those sustained in 1906, the year of the San Francisco earthquake and fire, which resulted in \$375 million damages.

In the fourth quarter, the industry had a pre-tax operating loss of \$760 million, compared with pre-tax operating profit of \$590 million a year earlier.

After tax credits and capital gains, fourth quarter net income was \$848 million, down 40% from \$1.4 billion in 1983.

For the full year, insurers had pre-tax losses from insurance underwriting of \$20.52 billion, compared with \$12.93 billion in 1983. Investment income, primarily interest on bonds and dividends on stocks, was \$17.62 billion, up 10% from 1983. Capital gains were \$3.17 billion, up 56%.

The industry's poor 1984 performance has been blamed on heavy weather-related claims and lingering effects of a six-year price war in commercial insurance that apparently ended last summer. Still, analysts don't expect earnings to improve until late this year or early 1986.



Insurance Information Institute

The Insurance Information Institute is a nonprofit educational, fact-finding and communications organization for the property and casualty insurance business. The Institute is supported by some 300 insurance companies and provides public relations and communications services to other insurance organizations in the fields of property, casualty, fidelity, surety and marine insurance. Headquartered in New York City, the Institute has offices in other major U.S. cities.

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ISO, NAII REPORT YEAR-END 1984
PROPERTY/CASUALTY INDUSTRY OPERATING RESULTS

NEW YORK, March 19 -- The nation's property and casualty insurance industry reported net after-tax income of \$1.94 billion in 1984, down 68 percent from the 1983 net income of \$6.0 billion.

The industry recorded a pretax operating loss of \$2.9 billion in 1984, compared with pretax operating income in 1983 of \$3.04 billion. The 1984 operating loss consists of a pretax underwriting loss of \$20.52 billion and pretax net investment income of \$17.62 billion.

The industry's pretax underwriting loss of \$20.52 billion for 1984 was \$7.59 billion greater than the loss of \$12.93 billion in 1983. The underwriting loss includes \$2.10 billion of premiums returned to policyholders as dividends in 1984, compared with \$2.16 billion a year ago.

(more)

The \$17.62 billion of net investment income for 1984 (primarily dividends earned from stocks and interest earned on bonds), was up 10.3 percent from a year ago. Net investment income, combined with realized capital gains, which rose 56.1 percent to \$3.17 billion, brings the industry's total pretax net investment gain for 1984 to \$20.79 billion, up 15.4 percent from \$18.01 billion a year ago.

The figures were released by Insurance Services Office, Inc. (ISO) and the National Association of Independent Insurers (NAII), reporting for insurers that account for 97 percent of the country's property/casualty insurance business.

The 1984 underwriting loss of \$20.52 billion was 18.2 percent of the earned premiums of \$112.49 billion. This compares with the 12.4 percent underwriting loss on earned premiums of \$103.89 billion for the year 1983.

Written premiums for 1984 totaled \$115.87 billion, up 9.4 percent from \$105.87 billion in 1983. That growth compares with the 4.6 percent growth of 1983 over 1982 written premiums.

For the fourth quarter of 1984, the industry's net after-tax income was \$848 million, compared with \$1.40 billion for the fourth quarter of 1983, a decrease of 39 percent.

(more)

The industry recorded a fourth-quarter 1984 pretax underwriting loss of \$5.85 billion, compared with the \$4.03 billion loss a year ago. The fourth-quarter 1984 underwriting loss included \$582 million of premiums returned to policyholders as dividends, compared with \$793 million in the fourth quarter of 1983.

The industry's pretax net investment gain in the fourth quarter of 1984 was \$6.20 billion, up 24.5 percent from \$4.98 billion in the fourth quarter of 1983.

The fourth-quarter 1984 loss of \$5.85 billion was 19.6 percent of the period's earned premiums of \$29.91 billion. This compares with the 14.9 percent underwriting loss on earned premiums of \$27.11 billion recorded for the fourth quarter of 1983.

Written premiums in the fourth quarter of 1984 totaled \$29.45 billion, up 14.1 percent from \$25.80 billion in the fourth quarter of 1983. That growth compares with the 6.7 percent growth of 1983 over fourth-quarter 1982 written premiums.

3/19/85: 53TN
March 19, 1985

SOURCES OF DATA ON FINANCIAL RESULTS (Property/Casualty Insurance)

1. Most data published by the Insurance Information Institute are from A.M. Best Company, an independent analytical, rating and information service organization.
2. The A.M. Best Company data are collected from individual insurance companies throughout the United States. Each insurance company is required to report to each state in which it is licensed what is known as the convention statement. A.M. Best Company receives copies of these reports and adds the data up line by line, company by company, to produce a total. This total is then increased by a small factor (less than 3 percent) to produce an overall industry aggregate figure. The incremental factor is used mainly to reflect estimates for companies not required to report to the state insurance departments. In many states, small farm mutual companies are not required to report.
3. The Institute publishes data from a quarterly report issued jointly by Insurance Services Office, Inc. (ISO) and the National Association of Independent Insurers (NAII). These data are collected each quarter from

companies representing about 97 percent of premium volume in the U.S. The data are received by ISO and NAII in the form of answers to questions, e.g., what were your written premiums in the past quarter?

CONCEPTS OF PROFIT/LOSS IN THE PROPERTY/CASUALTY INSURANCE
INDUSTRY

There are several ways of measuring profit and loss in the property/casualty insurance industry, as there are in any other industry. The different concepts used depend on the question being asked and the perspective of the inquirer. For example, a regulator frequently will have a different perspective on data than a shareholder of an insurance company. Some of the common measures of profitability are:

1. Net profit/loss after taxes.

This is the basic concept of bottom-line earnings. This number is the bottom line on the income statement of most U.S. companies. The figure includes losses or gains from underwriting, investment income (interest income and dividends), realized capital gains and federal income taxes. Shareholders are interested in this figure because it provides some indication of whether dividends will be paid and at what rate. However, this figure does include extraordinary items and other factors, which may be of a transitory nature. Of key importance for property/casualty insurance in recent years has been the impact on this figure of federal taxes and realized capital gains.

In the case of federal taxes, what was normally a subtraction from before-tax income has turned into an addition. This is because companies were losing money before taxes and received a credit for taxes paid in the prior three years -- a form of income-averaging for companies. Realized capital gains also increased in importance in the past few years, partly because of the strong stock market, but also because of the need by insurance companies to raise cash to pay losses. In calculating bottom-line profit or loss, the profit or loss from the sale of stock is included regardless of the purpose of the sale.

2. Operating profit/loss.

Because this figure includes the key operating concepts -- underwriting profit or loss and investment income, it is the most reliable indicator of how the property/casualty industry is doing. It excludes realized capital gains or losses and federal taxes.

3. Underwriting profit/loss.

The underwriting profit or loss is calculated by subtracting incurred losses (funds assigned to pay claims) and expenses (e.g., commission to insurance agents) from earned premiums. It does not include income from

investments. This figure tells a regulator how a company is doing in the basic functions of the business -- selling insurance and paying claims.

4. The combined ratio.

The combined ratio is similar to the underwriting profit or loss. The combined ratio is the sum of the ratio of incurred losses to premiums earned and the ratio of commissions and expenses to premiums written. A combined ratio above 100 means that the industry is incurring more in claims and expenses than it is taking in in premiums.



February 13, 1986

Nader's Charge on Ontario, Canada Termed Misleading

The Charge: Insurance Woes Unrelated To Tort Law.
Leah R. Young. The Journal of Commerce.
86/02/11. Page 14A. Ralph Nader told
Washington reporters that the experience in
Ontario, Canada, which has many of the tort
reform measures being proposed in the United
States, "shows that the insurance emperor has
no clothes," since, even with tort reform,
Ontario is also experiencing high premiums
and a shortage of insurance coverage. Jay
Angoff, counsel to the Nader-supported
National Insurance Consumer Organization,
said Ontario already has a cap on
compensation for pain and suffering,
restrictions on punitive damages,
prohibitions on injured parties specifying
the amount they are seeking, restrictions on
attorneys' contingency fees, few jury trials,
and penalties for frivolous suits.

The charge is grossly inaccurate and misleading.

* On a per capita basis, commercial liability insurance premiums are much lower in Canada than in the U.S. In 1985, liability premiums (excluding auto) averaged \$18 (C\$25) per capita in Canada, compared with \$60 per capita in the U.S. The different legal system in Canada is the most likely factor explaining this wide divergence in the cost of insurance.

* There are problems in commercial liability insurance in Canada, but they are not as severe as in the U.S.

* The problems in commercial liability insurance in Ontario, Canada reflect:

- 1) the impact of recent statutes, which increase the incentives to litigate;
- 2) an erosion of traditional common law disincentives to sue;
- 3) the impact of the worldwide contraction in liability insurance capacity.

Commercial liability premiums in Canada are expected to show an increase of 15% for 1985, contrasted with a 72% increase in the U.S.

There are, however, some problems of availability of commercial liability insurance in Ontario. This province is known to be litigious. Specific statutory provisions have increased the number and size of claims in Ontario Province:

- a) The Family Law Reform Act of Ontario Province (1978). This law extended the number of persons who could sue. For example, under this law a person with only passing acquaintance with another relative (say a cousin or nephew) can sue for loss of companionship.
- b) The province of Ontario passed a prejudgment interest act, which adds interest to awards from the date of filing.

Also, judicial procedures in Ontario have tended to increase awards beyond expectations. For example, courts in Ontario have tended to add to the award enough money to cover the taxes on interest earned from the award in future years.

In addition, Canada is affected by the worldwide shortage of liability insurance, caused mainly by severe losses by reinsurers in the U.S. market.

The Province of Ontario did not enact a series of tort reforms as might be inferred from the Nader charges. The reforms mentioned are features of the common law system and are not statutory law. Since they are part of common law, they are subject to change by judicial decision and, in fact, there has been erosion in these areas in recent years.

The following reviews the elements of the legal system in Ontario, Canada, that are highlighted in the Nader charge:

1) Cap on compensation for pain and suffering

In the early 1970s, Canadian courts established through case law a cap of C\$100,000 on pain and suffering awards. The cap has since been eroded and the figure now is C\$180,000. (Since the cap is set by case law, it can be changed by case law.)

2) Restrictions on punitive damages

These restrictions also are set by case law and have been in place for many years. The restrictions in Canada are in general tougher than those used by U.S. courts.

3) Prohibition on injured parties specifying the amount they are seeking.

This prohibition holds that a jury cannot be directly informed or led by evidence to know the amount of damages sought by a plaintiff. This rule is a common law rule and has been in place for decades.

4) Restriction on attorney's contingency fees.

In Ontario, attorneys fees are set by the Law Society. Contingency fees are prohibited.

5) Few jury trials.

Traditionally, Canada has used juries infrequently in civil cases.

6) Penalties for frivolous suits.

Defendants who win suits can collect legal fees and other costs from plaintiffs. This system has been in place for decades.



Nader/Hunter Challenge

The Property/Casualty insurance industry shares the concern of state and federal public officials, business and the general public about developments leading to restricted insurance coverages and the rising cost of commercial insurance protection. The insurance industry is deeply disturbed about the actions it has felt compelled to take in certain lines of insurance and for selected types of coverage. The industry welcomes the commitment of the affected policyholders and public policymakers in restoring the legal and regulatory stability needed to provide a responsive insurance market. The industry already has responded with a number of programs in various states aimed at alleviating the distress in various industries.

The industry recognizes that competitive price cutting by the industry in the first half of the 1980's has been a major factor behind the current large increases in rates for commercial liability insurance. The industry beginning about 1979 entered a period of fierce price competition with two major results:

- commercial businesses throughout the U.S. got bargains in the purchase of liability insurance,

- the insurance industry ended up posting record operating losses in 1984 and 1985.

However, the obvious cyclical factors in the industry tended to obscure a basic phenomenon which had been impacting on the liability insurance system for decades, namely the mushrooming growth in litigation in the U.S., and the associated problem of expanding concepts of liability.

Certain critics of the industry contend that the problems in the availability and affordability of commercial liability insurance are totally due to the competitive nature of the industry and are unrelated to developments in the tort system. The following pages provide brief responses to this and related challenges to the industry.

CHARGE: There is not a tort litigation explosion in this country.

There is a crisis in the civil justice system in America. It is not manufactured by the insurance industry.

* Awards are growing at an alarming rate.

In 1984, there were 401 awards of a million dollars or more in the U.S., up from 372 in 1983. In 1962, in a less litigious era, there was only one award over a million dollars.

The average size of verdicts for three common injuries -- cervical strain, knee injuries and vertebrae fractures -- and for wrongful death of adult males, increased at an average rate of 14.3% between 1974 and 1984, more than double the rate of inflation.

* Cases filed have grown at a spectacular rate.

In federal courts, product liability suits jumped 600% in ten years, from 1,579 in 1974 to 10,745 in 1984.

In state courts, the growth in filings has been at least four times as fast as the increase in population.

* We produce lawyers in this country at a faster rate than we produce babies. The annual rate of growth in the number of lawyers is six times the growth rate in population. Between 1970 and 1980, the number of lawyers in the U.S. increased 68%, while the overall population increased only 11%.

* In the insurance industry our loss data show what's happening. From 1965 to 1985, losses (dollars to be paid out in claims) in commercial liability insurance increased 2,046%, while inflation was up only 242%.

In 1984, losses in commercial liability insurance increased 25%, and in 1985 losses increased 43%.

* The civil justice system is grossly expensive. For example, in Los Angeles a typical trial costs the taxpayers \$11,000.

* The system sometimes delivers meager justice. In asbestos cases, claimants receive only 37 cents of every dollar. The other 63 cents go to pay for litigation costs, according to a recent Rand study.

* The most eminent jurists in the United States believe there's a crisis.

In the words of Chief Justice Burger, the process of going to trial is "not only stressful and frustrating, but expensive and frequently unrewarding for litigants." Other critics of the system include Derek Bok, president of Harvard University and former dean of the Harvard Law School, as well as former Attorneys-General William Smith and Griffin Bell.

Last, but by no means least, is the opinion of the American public. Surveys conducted by the Gallup Organization and Cambridge Reports, Inc. show that the public is fed up with the system.

-- People complain about the excessive delays and outrageous costs of the system.

-- People favor reforms. They favor arbitration as an alternative to going to court.

-- People favor limitations on pain and suffering awards. They favor limits on contingency fees.

Why are people fed up with the system? Because they recognize that what's happening in our society is wrong.

-- In N.J. the Supreme Court ruled that you can't throw a party in your home and serve drinks without running the risk of being sued if someone is injured by an intoxicated guest.

-- Doctors, in addition to taking courses in healing people, are taking courses in how to avoid being sued. According to the AMA, \$17.5 billion is spent in this country on defensive medicine - that's for unproductive tests designed to avoid lawsuits.

-- The threat of lawsuits is discouraging the manufacture of vaccines designed to prevent illnesses.

-- Directors of publicly-held companies are resigning because of the rise in lawsuits.

In sum, this is a basic issue of consumer and human rights. The trial lawyers naturally want the insurance industry to be around, because this is the deep pocket that funds them. But who pays for all this?

The answer is well known. Consumers - the general public - pay through higher insurance premiums. In sum, the insurance industry's current high rates are the symptom not the disease.

The pendulum has swung too far to one side -- we have too many lawyers, too many lawsuits and too many changes in legal doctrine.

Specific Nader-Hunter Challenges:

CHARGE:

The insurance industry is exempted from federal anti-trust law. (The implication being that insurance companies act as an OPEC-like monopoly to gouge consumers).

The insurance industry is not exempted from federal antitrust law. The McCarran-Ferguson Act of 1945 provides that regulation of the insurance industry should occur at the state level. However, federal anti-trust laws apply under McCarran-Ferguson if state regulation is deemed to be ineffective and the Sherman Act always applies in cases of boycott, coercion or intimidation. Federal agencies have exercised regulatory powers. The Department of Justice, for example, has successfully challenged acquisitions in the insurance industry which were viewed as discouraging competition.

(U.S. vs. Chicago Title and Trust Co., et al., 242F. Supp.56, N.D., Ill. 1965.)

CHARGE:

The insurance industry reports only underwriting losses. The industry states that in the ten years 1976 to 1985 insurance companies lost \$81.3 billion. Insurers neglect to mention their investment income over the same period of \$119.8 billion. So overall they made \$38.5 billion.

-- The industry reports data including investment income. I.I.I. reports such data to the trade and general public every quarter. Key sources of data, I.I.I. Fact Book, and Best's Aggregates and Averages, prominently display data on investment income.

-- While \$38.5 billion sounds like a lot of money, it amounts to an average of \$3.85 billion per year. Premiums over this period averaged \$96.8 billion so that profit margin on premiums was only about 4% -- 4 cents on the dollar, a profit margin below the rate achieved by most U.S. corporations. For the ten years 1975 through 1984, the rate of return on net worth in the industry averaged 10.9%, 2.3% points below the 13.2% rate of return for U.S. industry.

CHARGE:

The insurance industry pays little in taxes.

Adding up federal, state and local taxes, the industry pays about the same as the average for U.S. manufacturers.

The property/casualty industry pays relatively low federal taxes because much of its income is from tax-exempt state and local bonds.

CHARGE:

The increase in insurance rates is causing an inflationary jolt to the U.S. economy.

The property/casualty insurance industry makes up only 3.6% of the U.S. economy. A 21% increase (as occurred in 1985) in insurance premiums would not even change the inflation rate by a single percentage point.

Insurance rates have been a deflationary force over the past few years. Between 1978 and 1984, the consumer price index increased 59.2%. Premiums increased only 44.6% over the same period.

CHARGE:

The insurance industry won't tell us what we want to know. I have been asking for data, line by line, state by state showing data as follows:

<u>Column 1</u>	<u>Premiums paid</u>
<u>Column 2</u>	<u>Losses paid</u>
<u>Column 3</u>	<u>Investment income</u>

These data are available by line and by state.

Close to 2,000 insurance companies representing over 97% of insurance premiums report data on premiums, losses and expenses, by line, by state, every year.

They report this information in a document called the "Annual Statement", which is over 60 pages long, and contains details on premiums, losses, expenses, investments and taxes.

Insurance companies report on 28 separate lines of insurance. Data on small lines, such as day-care centers or professional liability for accountants, are included in aggregates and are not reported separately in the Annual Statement.

Investment income is not reported by line, as a company manages its investment portfolio as a whole. However, allocations can be made to lines of insurance and are reported on this basis in Best's Aggregates and Averages. (See, Best's Aggregates and Averages, 1985, pages 78 and 79).

CHARGE:

The insurance industry reports fictitious losses. They refer to incurred losses but don't tell us about paid losses.

Close to 90% of incurred losses are paid losses. Incurred losses represent losses paid, plus dollars set aside to cover losses to be

paid in future years. In many areas of insurance, such as medical malpractice, there is a time difference between when an accident occurs and when a claim is paid. The time difference can be quite long. In liability cases, the process of gathering evidence and court delays can result in a difference of many years between the time an accident occurs and the suit is finally resolved.

CHARGE:

Lloyd's holds the U.S. insurance industry in a vice-like grip. Lloyd's operates without any regulation and is dictating to the United States changes in our civil justice system.

It is estimated that Lloyd's writes only 15% of the reinsurance (insurance for insurance companies) in the U.S., so it can hardly be viewed as controlling the U.S. market. Lloyd's has lost a lot of money in liability insurance in the U.S. Its latest results show that while only 12% of its worldwide premiums were in liability insurance, this line was the source of 100% of its financial losses.

Like any responsible company, Lloyd's began withdrawing from areas where it was losing money, and stated the conditions under which it believes it can write business on a profitable basis.

Lloyd's is an accredited reinsurer throughout the U.S., an eligible excess or surplus line insurer in all jurisdictions as well as a licensed insurer in Illinois, Kentucky and the U.S. Virgin Islands. In addition, a number of federal agencies have also recognized Lloyd's insurance. Each year, Lloyd's files audited

financial statements with the U.S. Treasury Department, many State Insurance Departments and the National Association of Insurance Commissioners.

CHARGE:

Insurance companies say they are losing money, yet their stocks were up over 50% last year.

Every analyst of the industry forecast the property/casualty insurance industry would recover. The stock market practically always rises when it is generally believed that a depressed industry is on the road to recovery.

In general, the stock market is a poor indicator of the financial health of an industry. In 1977, the property/casualty stock index fell 4%. The following year, the industry recorded one of its most profitable years in history, with an 18.1% return on net worth.

CHARGE:

What is needed is a federal insurance office to review the industry and to set standards for state regulators.

What is being proposed is some kind of dual regulatory system. These systems don't work very well, as we know from the banking industry.

The banking industry has a dual system of federal and state regulation. Yet, the failure rate of banks is far higher than that of

the insurance companies. In addition, despite federal regulation and a federal insurance system, bank failures in recent years have cost taxpayers billions of dollars. One bank, Continental Illinois, received a commitment of \$4.5 billion from the federal government to stave off bankruptcy. Failures in the insurance industry do not cost taxpayers, as they are covered by state guaranty funds which are collected from the insurance industry itself.

CHARGE:

What is needed is a federal reinsurance program. Reinsurance is largely concentrated among foreign firms. This would free U.S. business from foreign tyranny just as the goal of energy independence was designed to free U.S. citizens of pressures exerted by oil-producing nations.

A federal reinsurance program could cost the taxpayers of this country billions of dollars. Under a general federal reinsurance program, insurance companies could lay off all their bad risks on the federal government while maintaining only the profitable risks. This also would mean that the losses now being suffered by reinsurers in U.S. markets would be borne by the Federal government, rather than by the private sector.

The foreign tyranny assertion is baseless. About 75% of the reinsurance market is in the U.S. The main advantage of keeping U.S. reinsurance markets open to foreign companies is that the supply is expanded. This means that more insurance capacity is available to

U.S. firms and at a cheaper rate than if reinsurance were restricted to the U.S. companies alone.

Also, pursuing a protectionist policy in insurance markets would have the same negative repercussions of protectionism as in any other industry. Other nations would retaliate, not only against U.S. insurance companies operating abroad, but also against other U.S. exporting industries, such as aircraft manufacturing and agriculture.

In general, the reinsurance industry represents less than 10% of primary premiums. (I.I.I. Reinsurance Monograph, page 60). About 75% of this market is with U.S. companies, and 25% with foreign re-insurers. (I.I.I. Reinsurance Monograph, page 42).

CHARGE:

Thirty-eight states have laws that protect insurance agents by denying groups the right to form their own cooperative insurance coverage.

There are very few restrictions on the formation of groups to purchase insurance or to self-insure. In fact, it is estimated that 25% of commercial lines insurance is in the self-insurance area. Group insurance policies, such as those purchased by employers for their workers or unions for their membership, are allowed in all states. The laws in question deal only with the formation of "fictitious" groups, that is a group of people, who have no formal

relationship with one another. The prohibition on "fictitious" groups is designed to protect consumers who cannot join such "fictitious" groups from paying more for an insurance policy.

CHARGE:

State regulation of insurance is so weak as to be almost non-existent. Only half the states have actuaries on their staff.

The major states have full staffs of qualified actuaries. Small states without actuaries regularly hire actuaries on a contractual basis and consult with experts in other state insurance departments when they have an actuarial problem. In addition, the NAIC publishes actuarial guidelines in its field examiner's handbook and has set up an actuarial task force to deal with problems common to all states. Moreover, insurance companies often are examined by regulators from several states who pool information on companies.



February 18, 1986

NADER'S CHARGE ABOUT ONTARIO TERMED INACCURATE AND MISLEADING

At a press conference in Washington, D.C., on Feb. 10, Ralph Nader told reporters that Ontario, Canada, is experiencing high premiums and a shortage of insurance coverage despite having laws which have many of the tort reform measures being proposed in the United States. Representatives for the National Insurance Consumer Organization said that Ontario already has a cap on compensation for pain and suffering, restrictions on punitive damages, prohibitions on injured parties specifying the amount of the award they are seeking, restrictions on attorneys' contingency fees, few jury trials, and penalties for frivolous suits.

This represents another misleading charge from Nader/Hunter. Here are the facts:

* On a per capita basis, commercial liability insurance premiums are much lower in Canada than in the U.S. In 1985, liability premiums (excluding auto) averaged \$18 (C\$25) per capita in Canada, compared with \$60 per capita in the U.S. The different legal system in Canada is the most likely factor explaining this wide divergence in the cost of insurance.

* There are problems in commercial liability insurance in Canada, but they are not as severe as in the U.S.

* The problems in commercial liability insurance in Ontario, Canada reflect:

1. The impact of recent statutes, which increase the incentives to litigate.
2. An erosion of traditional common law disincentives to sue.
3. The impact of the worldwide contraction in liability insurance capacity.

Commercial liability premiums in Canada are expected to show an increase of 15% for 1985, contrasted with a 72% increase in the U.S.

There are, however, some problems of availability of commercial liability insurance in Ontario. This province is known to be litigious. Specific statutory provisions have increased the number and size of claims in Ontario Province:

- a. The Family Law Reform Act of Ontario Province (1978). This law extended the number of persons who could sue. For example, under this law a person with only passing acquaintance with another relative (say a cousin or nephew) can sue for loss of companionship.

- b. The province of Ontario passed a prejudgment interest act, which adds interest to awards from the date of filing.

Also, judicial procedures in Ontario have tended to increase awards beyond expectations. For example, courts in Ontario have tended to add to the award enough money to cover the taxes on interest earned from the award in future years.

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The Province of Ontario did not enact a series of tort reforms as might be inferred from the Nader charges. The reforms mentioned are features of the common law system and are not statutory law. Since they are part of common law, they are subject to change by judicial decision and, in fact, there has been erosion in these areas in recent years.

The following reviews the elements of the legal system in Ontario, Canada, that are highlighted in the Nader charge:

1. Cap on compensation for pain and suffering. In the early 1970s, Canadian courts established through case law a cap of C\$100,000 on pain and suffering awards. The cap has since been eroded and the figure now is C\$180,000. (Since the cap is set by case law, it can be changed by case law.)
2. Restrictions on punitive damages. These restrictions also are set by case law and have been in place for many years. The restrictions in Canada are in general tougher than those used by U.S. courts.
3. Prohibition on injured parties specifying the amount they are seeking. This prohibition holds that a jury cannot be directly informed or led by evidence to know the amount of damages sought by a plaintiff. This rule is a common law rule and has been in place for decades.
4. Restriction on attorneys' contingency fees. In Ontario, attorneys' fees are set by the Law Society. Contingency fees are prohibited. This system has been in place for decades.
5. Few jury trials. Traditionally, Canada uses juries infrequently in civil cases.
6. Penalties for frivolous suits. Defendants who win suits can collect legal fees and other costs from plaintiffs. This system has been in place for decades.

Sean Mooney, Ph.D., CPCU
I.I.I. Senior Vice President and Economist

THE LANGUAGE OF INSURANCE

The language of the insurance profession can be confusing, obscure and frustrating. Here is a glossary of common insurance terms. As you learn them, you'll be better able to understand the basics of insurance.

A

accident An unforeseen act or result which may cause bodily injury or property damage. In some policies, it is identified as occurring at a specific time and place. In others, it includes continuous or repeated exposure to the same conditions. Refer to the appropriate policy for exact definition. Also see occurrence.

act of God An event caused by the forces of nature, without human intervention and which could not have been prevented by reasonable care; for example, flood, earthquake, hurricane.

actual cash value The present day value of property measured in cash, determined by subtracting depreciation brought about by physical wear, tear and obsolescence from the replacement cost.

additional insured A person, other than the named insured for whom the policy is written, who is protected against loss by the terms of the policy.

additional premium The additional amount of money charged the policyholder which is over and above the original premium charged. This may occur because of endorsement for increase in limits of liability, rate increase or other increase in the exposure of risk.

additions and alterations The fire policy usually extends permission to build additions or make changes or alterations to the dwelling without violating the policy and coverage is extended to include such additions and alterations.

adjacent Lying near to, but not in actual contact with. Nearby. Property near the property insured. Such adjacent property may increase the hazard of loss.

adjuster An individual representing the insurance company in discussions leading to agreement on the amount of a loss and the company's liability.

adjustment The process of determining the cause and amount of a loss; the amount of indemnity the insured may recover.

agent, independent An independent business person who represents insurance companies under contract in a sales and service capacity and is paid on a commission basis.

all risk insurance Coverage for all perils except those specifically excluded in the policy. By contrast, a named peril policy specifically names each peril for which the policy insures.

allied lines Various coverages offered by fire insurers, all of which are closely associated with fire insurance. Examples are extended coverage, and even also malicious mischief and sprinkler leakage.

amount of insurance The maximum dollar amount payable by the insurer under the conditions of the policy. In effect, amount of insurance is synonymous with limit of liability.

appraisal Determination of the value of property, or of the extent of damage, usually by impartial experts. The fire insurance policy provides for appraisal where the company and the insured cannot agree upon the amount of loss.

appurtenant structure Other structural property on and belonging to the insured dwelling including fences, walkways, pools and private garages.

assigned risk A means by which persons unable to purchase automobile insurance through the voluntary market are able to obtain insurance. If eligible, these drivers will be assigned to a licensed company in their state through the Assigned Risk Plan. Also referred to as Auto Plan.

assignment The transfer of the legal right or interest in a policy to another party, generally in connection with the sale of property. It is valid only with the consent of the insurer.

attractive nuisance A dangerous place or device attractive to children. The owner of an attractive nuisance has the legal duty to make particular precautions for children, e.g., swimming pools, animals, construction project.

Auto Plan See assigned risk.

automobile A land motor vehicle. Also see private passenger automobile

automobile non-ownership liability Insurance against loss due to claims for damages arising out of the use of motor vehicles not owned by or hired by the insured but used in the conduct of the insured's business.

B

BI Bodily injury

bailee One who has possession of property belonging to another, for a specific purpose.

bailment Delivery of personal property for a particular purpose with the intent that the property will be returned to the person who originally delivered it.

bailor A person who entrusts goods to another.

basic limits coverage The lowest limits of liability ordinarily written; basic limits are those for which manual rates and minimum premiums are computed.

binder A temporary contract of insurance made with an insured pending delivery of the policy.

bodily injury The impairment of a person's faculties, including pain, suffering, disability and death for which negligence is the proximate cause.

bordereau A memorandum containing detailed information used in passing reinsurance from one company to another under a reinsurance agreement. See reinsurance.

broker An insurance broker ordinarily is a solicitor of insurance who does not represent insurance companies in a capacity as agent but places orders for coverage with companies designated by the insured or with companies of the broker's own choosing.

builders' risk insurance Insurance against loss to buildings in the course of construction. With the value of construction changing during the building process, a fixed amount policy would not properly cover the risk. May be written on a reporting form or on a completed value form.

bureau A national, regional or state organization, supported by participating insurance companies, which may develop standard forms of coverage and policies; develop, publish and file rates to be used by insurers in making premium charges or act as a statistical agency. Bureau frequently is used interchangeably with ISO or WS&RB.

burglary As differentiated from robbery, burglary is the act or intent to take property belonging to another with visible evidence of breaking into or breaking out of locked premises.

C

CIC Certified Insurance Counselors

CPCU Chartered Property and Casualty Underwriter

CSL Combined single limit

cancellation The termination of a policy before its normal expiration date. Cancellation may be requested by the insured at any time. Some restrictions apply to cancellation requested by the insurer in some policies.

captive An insurance company established to insure a specific company or group of companies. The captive is usually owned by the company it insures.

carrier Any organization that "carries" insurance. A carrier may be a company, corporation, association or facility.

casualty insurance A type of insurance primarily concerned with losses caused by injuries to persons and the legal liability imposed upon the insured for such injury or damage.

catastrophe A sudden and severe calamity or disaster. An event which causes a loss of extraordinarily large amount.

certificate of insurance A statement of coverage taking the place of the policy as evidence of insurance and stating the coverages of the policy in general terms.

Chartered Property and Casualty Underwriter (CPCU) A designation conferred by the American Institute of Property and Liability Underwriters to one who has attained certain standards of education and proficiency on property and casualty insurance and has passed a series of examinations.

claim A demand by an individual or organization to recover under an insurance policy for loss which may come within the policy. A demand by an individual against an insured for damages caused by an event. In the latter case, such claims are referred to the insurance company for handling on behalf of the insured.

claimant One who makes a claim.

class rates Fire rates that apply to a group of similar risks. They are obtained from a manual by matching the characteristics of the insured property with the appropriate class described in the manual.

classification The underwriting or rating group into which a particular risk is placed. Pertains to type of business, location and other factors. Classifying persons, property, or operations as a basis for tabulating statistical experience and determining premium rates.

client The customer. The company or person who buys the insurance. See insured.

clause A section of a policy contract, or of endorsements attached to it, dealing with a particular subject in the contract, as the insuring clause or the coinsurance clause.

coinsurance A provision in an insurance policy requiring the insured to contribute a fair and just share of the total premium out of which losses are to be paid. The inclusion of this provision, whether mandatory or optional, usually gives the insured lower rates than would otherwise apply.

coinsurance clause Provision in a fire insurance policy whereby the property owner is to carry insurance up to an amount determined in accordance with the provisions of the policy. This usually is a stated percentage of the value of the property, in return for which the insured pays a lower premium. Failure to maintain limits at the specified percentage causes a reduction in the amount payable to the insured in the event of loss.

coinsurer One who shares the loss sustained under an insurance policy. Usually applied to an owner of property who fails to carry enough insurance to comply with the coinsurance provision and who therefore suffers part of the loss.

collision Insurance against loss to property caused by striking or being struck by a stationary or moving object; includes loss caused by upset.

commission A percentage of the premium paid to an agent or broker in return for business procured.

commissioner of insurance The official charged with enforcement of laws pertaining to insurance in the state.

common law liability The responsibility for injuries or damage imposed upon a party because of his or her actions, by that part of the law based upon custom and usage as established by the courts.

comprehensive Insurance covering the insured's own auto for damages other than collision or upset. It is distinguished from insurance against specific hazards, such as fire and theft.

conditions Provisions of an insurance policy which along with the insuring agreement, coverage forms and exclusions complete the contract. The part which states the obligations of the insurance company and the insured, in such areas as claims, premium payment and cancellation. Also called provisions.

condominium A condominium unit owner owns only the air space inside the unfinished walls, floor and ceiling of the unit. The building and land beneath are owned by the owner's association and unit-owners; have an individual share in the common property.

consequential loss The loss not directly caused by the damage to the property but which arises from the result of such damage. A fire may damage refrigeration equipment and the nonoperation of the refrigerator cause spoilage. Such spoilage is a consequential loss of the fire.

construction class Classification of fire risks, according to type of construction to enable fire insurance rates to be established equitably.

cooperative Multiple family projects owned by a nonprofit corporation. A group owns the building and land; no one individually owns the unit he or she occupies.

countersignature A signature of a licensed domiciled agent required by state law to validate an insurance policy.

coverage The extent of the insurance afforded under an insurance contract. Coverage is frequently used interchangeably with the word protection.

D

daily report An abbreviated copy of pertinent policy information. Identical copies are usually prepared so that insurance companies, agents and brokers may each have one.

declarations The part of the insurance contract which contains information regarding the insurance risk, such as naming the insured, property covered, policy period, limits of liability and premium.

deductible A policy provision under which the insured, in the event of loss, agrees to bear a specified portion of the loss. The company is liable only for the excess.

depreciation Loss in value of property brought about by physical wear, tear and obsolescence. The difference between the replacement cost new and present actual cash value.

deviation Use of a premium rate other than the standard rate filed with a state insurance department.

direct loss A loss which is the immediate consequence of the peril insured against.

direct writer An insurer that uses its own employees to sell insurance.

dividend A refund of part of the premium paid at the beginning of the year that still remains after the company has set aside the necessary reserve and made deductions for claims and expenses.

dwelling The basic structure of a residence which includes walls, floors, roof, attached structures, building equipment, fixtures and outdoor equipment used for the service of the residence.

E

EC Extended coverage

earned premium That portion of the premium which represents coverage already provided. Each day that an insurance policy is in force is a day of earned premium.

effective date The date on which an insurance policy goes into effect and from which time protection is furnished.

endorsement An alteration to an insurance policy by attaching a form bearing the provision or the terms necessary to make the change.

excess insurance A policy which (1) provides limits of liability over and above those of specified underlying primary policies, but which relies on the insuring agreements and conditions of such underlying policies as to definitions of coverage; or (2) provides limits of liability in excess of a self-insured retention for agreed upon exposures.

exclusions The part of the insurance contract which limits, restricts or eliminates coverage under the policy.

expiration date The date upon which an insurance policy will cease to provide coverage unless previously cancelled.

exposure Refers chiefly to the state of being subject to loss from a hazard.

extended coverage A clause or an endorsement of a fire policy which provides additional coverage for other perils, such as wind, hail, explosion, etc.

F

Fair Plan A program, created by law, to make fire and other forms of property insurance available to persons who have difficulty obtaining coverage from insurance companies.

financial responsibility law A statute requiring motorists to furnish, either before or after an accident, evidence of ability to pay damages.

fire Fire must be combustion sufficient to produce a spark, flame or glow, but not an explosion, and must be hostile, as opposed to friendly, i.e., not in the place where it was intended to be. It must be accidental and must be the proximate cause of the damage.

fire protection grading A national system, developed by a predecessor of ISO, which rates cities and towns according to public fire protection and other criteria. The grading scale is 1 (best) to 10 (no effective fire protection). No city is presently graded class 1. See protection class.

floater policy An inland marine policy under the terms of which protection follows movable property, covering it wherever it may be.

full coverage Any form of insurance that provides payment without deduction on all covered hazard losses.

G

glass insurance Insurance to cover the costs of replacing damaged glass, such as door and windows.

H

hazard A specific situation that introduces, or increases, the probability of occurrence of a loss arising from a peril, or that may influence the extent of a loss. Examples of hazards include slippery floors, congested traffic and unguarded premises.

hazard, moral Characteristics of the insured that increase the probability of loss, i.e., dishonesty.

hazard, physical A physical or structural condition of the insured property that makes it more likely a loss will occur.

I

IIA Insurance Institute of America

IM Inland marine

ISO Insurance Services Office. See bureau.

improvements and betterments Additions or changes made by a lessee or renter at his or her own expense which enhance the value of the occupied building. These become part of the realty (and are not legally subject to removal) and require special insurance consideration.

indemnity The insurance concept that enables the insured to be reimbursed for a loss, without either gaining or losing financially, i.e., restored to the condition that existed before the loss.

independent agent See agent, independent.

indirect loss See consequential loss.

inherent vice A condition in property which causes deterioration or damage; for example, the painting of damp wood or spoilage of vegetables.

inland marine insurance Covers property against various hazards or losses while it is being transported from place to place or wherever the property may be located.

insurable interest Any interest in a subject, or any legal relation to it, of such a nature that a certain happening (such as fire) might cause monetary loss requiring insurance.

insurance The business of insuring persons or property. Coverage by contract whereby one party undertakes to indemnify another against loss by a special contingency or peril.

insurance commissioner See commissioner of insurance.

insured A person covered by an insurance policy.

insurer The insurance carrier, or insurance company.

insuring agreement That part of an insurance policy which provides the agreement of the insurance company to protect the insured against loss or damage. This agreement is the basis of the insurance contract.

L

legal liability An obligation enforceable by law most often considered in a monetary sense. Broadly, any legally enforceable obligation.

liability This is a broad term denoting any legally enforceable obligation. An obligation, usually financial.

liability insurance Coverage whereby the carrier agrees to pay damages and to defend against suit, on behalf of the policyholder, for any claim that may occur. It includes coverage for both bodily injury and property damage, where appropriate. Liability coverage is often referred to as third-party insurance.

limit of liability The maximum dollar amount which an insurance company agrees to pay in the event of loss.

loading In inland marine, an amount added to the base rate or premium to cover additional perils.

loss A financial setback or monetary deprivation. A claim or claim payment. The basis for a claim for indemnity or damages under the terms of an insurance policy.

M

McCarran Act See Public Law 15.

manual A book published by an insurer or bureau giving rates, classifications and underwriting rules for some phase of insurance.

manual rates A method for determining the cost of an insurance policy using predetermined rates, usually obtained from a rate book or manual.

medical payments A form of insurance coverage, usually included in automobile and liability policies, under which the insurance company agrees to pay medical, surgical, hospital, ambulance and funeral expenses resulting from an accident covered by the policy, regardless of negligence.

minimum premium The smallest amount that a carrier charges for providing coverage for a given period.

model year To identify the year a car or truck was manufactured. October 1 is considered the start of a new model year.

monoline A policy written to cover a single line of insurance, such as fire alone.

mortgage Legal document obtained as security for money loaned on property. It may apply to either real property or personal property, including autos.

mortgagee The party loaning money toward the purchase of property. Examples would be a bank or lending institution.

mortgagor Borrower who conveys his or her property as security for a loan.

Multiple line policy A policy which is a combination of fire and casualty in a single insurance contract, such as the homeowners policy.

N

named insured That person, partnership or organization for whom an insurance contract is written, and who is specifically designated as being "insured" in the contract.

named peril Named peril policies specify what specific perils are covered or insured against. All risk policies do not specifically name the perils.

negligence Failure to do what a reasonably prudent person would do under the circumstances of a particular case, or doing what a prudent person would not have done.

no fault insurance Provides for payment to persons who sustain bodily injury in a motor vehicle accident, on a first-party basis regardless of negligence. May also include property damage.

O

occupancy Refers to the activity or property of the insured, i.e., what the building is used for or the nature of its contents.

occurrence Any event or happening that may occur gradually over a period of time, or all at once, and which may cause bodily injury or property damage. The exact definition varies by kind of policy. Also see accident.

P

PD - Property damage

PIP Personal injury protection

PUD Planned unit development

peril A cause of damage or loss. Examples include fire, automobile accident, theft, windstorm and explosion. Exposure to the risk of being destroyed or lost.

personal injury coverage An extension of liability coverage to provide for libel, slander, false arrest, invasion of privacy and the like.

personal injury protection This refers to first-party, no fault coverage for damages due to automobile accident.

physical damage coverage Comprehensive and collision coverage for the insured's own automobile.

planned unit development The major difference between a townhouse and a PUD is that the unit-owner in a PUD also owns the land beneath the unit. The common grounds are owned by a nonprofit corporation. See townhouse.

policy A written contract of insurance between an insurance company and the policyholder.

policyholder One who possesses an insurance contract. Often a synonym for insured.

policy period The period during which a policy contract affords insurance.

premises Particular location or portion thereof as stated in the policy.

premium The amount of money paid by the policyholder for insurance coverage.

private passenger automobile A four wheel motor vehicle, other than a truck type.

pro rata In proportion.

property damage Injury to or destruction of property, including (in liability) the loss of use of such property.

property insurance Insurance that provides coverage for direct loss or damage to property such as a home or building. Frequently used interchangeably with fire and allied lines insurance.

protection Used interchangeably with the word "coverage" to denote the insurance provided under the terms of the policy.

protection class A code designating the degree of a property's protection by an adequate fire fighting organization which has sufficient equipment, water supply and alarm transmittal facilities to permit it to extinguish an ordinary fire in the property. See fire protection grading

Public Law 15 A federal statute passed in 1945 declaring that the continued regulation and taxation by the several states of the business of insurance is in the public interest. Its effect is to exempt the business of insurance from federal antitrust laws to the extent that there is state regulation.

R

rate The cost of insurance per unit of exposure used in rating for the determination of premium.

rating The determination of premium to be charged for coverage on a risk based upon risk characteristics and actuarial calculations on the chance of loss.

rating bureau See bureau.

reinsurance The cession by an insurance company (the reinsured) of a stated proportion or amount of risk and the assumption of such cession by another carrier (the reinsurer) in consideration of a premium paid by the reinsured to the reinsurer. The proportion of the risk not ceded is referred to as the retention or net line. Reinsurance is effected under a contract called a reinsurance agreement or treaty.

renewal Continuation of an insurance contract beyond the original date of expiration, by endorsement, certificate or new contract.

replacement cost Replacement cost insurance extends property damage policies to cover the actual cost of repairs or replacement without deduction for depreciation.

rider A form containing special provisions that are not contained in the policy contract and which are added or attached to the policy. See endorsement.

risk The possibility of loss or injury. The chance of loss or the perils of an insurance contract; the degree of probability of such loss.

risk That entity to which coverage attaches. It may be defined by line of business and may take the form of a vehicle, building, physical or geographical location, named person or any object.

S

schedule An enumeration of various properties covered by a policy.

self-insurance A decision made by a company to assume the risk for its own specific loss.

Self-insured retention An amount of liability for a given risk or exposure which is assumed or retained by the insured.

subrogation The legal process by which an insurance company seeks from a third party recovery of an amount paid out by the insurance company to a claimant under the policy.

T

term The period of time for which an insurance policy is issued.

territory Specific areas in cities and counties on which rates are based.

theft Any act of stealing or any unlawful taking.

third-party insurance Protection for the insured against liability arising out of bodily injury to others or damage to their property. Insurance against loss due to liability to third parties. Used synonymously with liability insurance.

tort A civil wrong committed by one person, against another person, for which the law provides compensation.

townhouse Single family dwelling or a multiplex. The occupant of each unit owns either all or a portion of the building structure, including the unit's walls. Owners also have an undivided share in all common grounds, but they do not own the land beneath their unit.

U

umbrella policy An all-encompassing policy providing increased or broader coverage above the basic liability policy.

underinsurance A condition in which not enough insurance is carried to cover the insurable value and especially to satisfy a coinsurance clause.

underinsured motorist coverage Automobile bodily injury protection for loss caused by a motorist without insurance or with inadequate limits of liability or a hit-and-run driver.

Underlying The amount of insurance or reinsurance on a risk which attaches before the next higher excess layer of insurance or reinsurance attaches.

Underwriting The process of selecting policyholders that meet the company's standards of acceptability.

Uninsured Not having insurance on a specific exposure.

Unoccupied Contains furnishings pertaining to operations or activities customary to occupancy of the building, but no one is there at the time.

V

V&M Vandalism and malicious mischief

Vacant Not lived in and void of furnishings.

Valued policy A policy which provides that a special amount shall be paid in event of a total loss of the property. Most fine arts and some other inland marine policies have this provision. In fire insurance in some states there are valued policy laws which require that fire insurance on buildings be treated as valued policies.

vandalism and malicious mischief The willful injury or destruction of property, e.g., throwing stones through the window of a home and damaging home furnishings would be vandalism.

W

WS&RB Washington Surveying and Rating Bureau. See bureau.

warranty The statement of the insured, the truth of which becomes a condition of the validity of the policy. Statement or stipulation in the policy as to the existence of a fact or a condition of the insurance, which, if untrue, will void the policy.

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March 11, 1986

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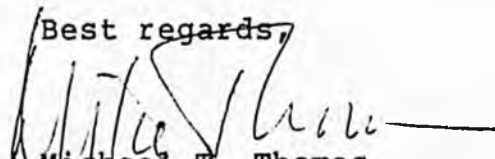
MAR 13 1986

Dear Senator Zharoff:

Enclosed are three documents which may be of some use to you and to the members of your committee as you try to sort out the various proposals for legislation pertaining to insurance and the civil justice system:

1. A "white paper" produced by trade associations in California, relating to their experience.
2. A paper on the financial condition of the insurance industry by the Insurance Services Office.
3. A copy of a statement by Charles Fritzel, an officer of the National Alliance of Independent Insurers before a committee of the U.S. Senate.

Please let us know if there is further information we can provide.

Best regards,

Michael T. Thomas
Counsel for the American
Insurance Association

MTT/kas

Enclosures

January 1986

THE LIABILITY SYSTEM IN CRISIS

The attached resource file is presented to you in the hopes that it will help to explain the current crisis in California's liability system and identify some meaningful measures that will ameliorate the crisis in the short term and solve the underlying problems that created it in the long term.

These papers were prepared in a joint effort by the Alliance of American Insurers, the American Insurance Association, the Association of California Insurance Companies and the National Association of Independent Insurers, who represent 869 insurance companies writing more than half of the property-casualty insurance premiums in California.

It is our hope that you will keep this information on hand throughout the coming months as insurance issues are sure to be among the most newsworthy items during that time.

The causes of the current crisis and the solutions proposed are complex, so a complete review of the situation requires a rather voluminous explanation. Accordingly, we have arranged this material by subject matter and indexed it for easy reference.

We will update the financial data in this report as complete quarterly data become available.

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Prepared by Insurance Services Office
- TAB 9 - Glossary

THE LIABILITY SYSTEM IN CRISIS

An Insurance Industry View

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January 1986

INTRODUCTION

For the first four years of this decade, most buyers of commercial and professional liability insurance enjoyed stable or decreasing insurance premiums. Then, in early 1985, premiums turned upward, often precipitously, and some buyers found it difficult to obtain adequate coverage at prices they regarded as affordable. The liability crisis has been extensively covered by the media, and there have been proposals from many quarters as to what to do about it, ranging from voluntary efforts by insurers and agents to fundamental tort reform.

The insurance industry believes that it is critically important that efforts to solve availability and affordability issues be grounded in a sound understanding of the private insurance mechanism and the impact that the liability system* has on it. Accordingly, this paper describes the reasons for the recent escalation in commercial and professional insurance premiums and sets forth actions, some voluntary and some requiring regulatory or legislative approval, that can lead towards an easing of problems of availability and affordability. The paper also cautions that ill-conceived measures, such as a return to administered pricing or the adoption of involuntary market mechanisms, may impede the return of the insurance industry to financial health and thus operate to the detriment of consumers in the longer run.

*As used in this paper, "the liability system" means the whole panoply of substantive and procedural rules by which losses are transferred from one party to another. It also includes the mechanisms through which disputes are resolved in court or otherwise, including judicial decisions with respect to insurance contracts.