Insurance Buyers' News

Springfield
PO Box 4207, Springfield, MO 65808
Phone: 800-422-5275
417-887-3550 • Fax: 417-887-3252

Rolla
PO Box 1258, Rolla, MO 65402-1258
Phone: 800-364-2212
573-364-8888 • Fax: 573-341-2257

West Plains
PO Box 964, West Plains, MO 65775
Phone: 800-400-3896
417-256-6162 • Fax: 417-256-6165

River City Insurance
PO Box 127, New Madrid, MO 63869
Phone: 800-899-7392
578-748-5215 • Fax: 573-748-5392

Managing Disasters May / June 2024 Volume 35 • Number 3

What's the Insurance Impact of the Key Bridge Collapse?

The Key Bridge Collapse is a Major Blow to Insurance Companies," reads the headline by NPR about Baltimore's Key Bridge disaster on March 30.

The headline is typical of most mainstream news outlets and though the total loss is huge, probably one of the largest maritime insurance losses in history, its impact on the insurance industry will not have the devasting effect suggested by some of the hyperbolic news coverage.

To be sure, its impact will be far-reaching:

Wrongful Death

There will be wrongful death suits filed by the families of the construction workers who were on the bridge when it collapsed.

Aerial view of cargo ship entering port of Hong Kong

continued on next page

This Just In ...

A.M. Best has downgraded the financial strength of State Farm Insurance from "A" (excellent) to "B" (fair) and its long-term issuer credit rating from "a" (excellent) to "bb+" (fair). AM Best said it assesses State Farm General's operation performance as marginal, its business profile as neutral, and enterprise risk management as appropriate. A.M. Best referred to "the challenging regulatory environment within California's marketplace that have constrained the ability of State Farm General (as well as its industry peers) to increase premium rates in a timely fashion."

...An Affirmative Artificial Intelligence (AI) Endorsement has been introduced by Coalition, a provider of insurance and cybersecurity tools. The endorsement clarifies what is covered by its U.S. Surplus and Canada Cyber Insurance policies.

The new endorsement expands the definition of a security failure or data breach to include an AI security

continued on next page

Damage to the bridge, vessel and business interruption insurance

Protection and Indemnity (P&I) Coverage for Grace and Synergy Marine, the owners of the container ship Dali that crashed into the Key when its piloting system failed, is provided by the Britannia P&I Club, one of the twelve members of the International Group of P&I Clubs which insures 90% of ocean cargo vessels.

Clubs in the International Group, such as Britannia, retain $10 million on any claim, with claims more than $10 million to $100 million shared between all the group clubs. The group also buys around $3 billion in group excess of loss reinsurance cover, which is led by Axa XL and spread among 80 reinsurers.

Thus, losses, even though they may be large, will be spread among dozens of well capitalized insurers. The worldwide marine insurance industry has been profitable lately and is in good shape, though incidents like the Houthis rebel attacks in the Red Sea have started to exert some upward pressure.

In fact, shipping losses have declined by 65% in the last decade, according to Rahul Khanna, New York-based global head of marine risk consulting at Allianz Commercial. So, though the Key Bridge loss could cause some rate increases somewhat, the impact is not expected to be dramatic.

"We have seen large incidents in the past being absorbed by the industry without much impact," Khanna told *Business Insurance.*

Force Majeure

The accident will trigger *force majeure* clauses in construction contracts involving projects for which materials were being shipped to or from the Port of Baltimore, though those disputes are often resolved through arbitration, Eric Ruzicka, a Minneapolis-based commercial litigator at Dorsey & Whitney LLP told *Business Insurance.*

Force majeure clauses allow a party to leave a contract temporarily or permanently, in whole or in part, for catastrophes that were not foreseeable. These catastrophes must cause severe disruption to fulfill a contractual obligation. If the event meets the terms of the force majeure clause in the contract, both parties can end the agreement without penalty.

Supply chain interruptions

Supply chain interruptions will be "significant, long-lasting and wide-ranging," according to Washington-based policyholder attorney Michael S. Levine of Hunton Andrews Kurth LLP.

Levine points to the grounding of the container ship Ever Given in the Suez Canal for six days in 2021, which provides a good illustration of the disruption that occurs when operations are interrupted. According to Lloyd's, the grounding interrupted $9.6 billion of trade per day, or $6.7 million per minute.

"What makes things even trickier is that companies affected by supply chain disruptions and contingent business interruptions may not immediately appreciate those losses as being a result of the incident, but over time the cumulative impact will become obvious. Now, is the time for affected policyholders to start quantifying their losses, small as they may be initially," said Levine.

Subrogation claims

Insurers who pay out for replacing the bridge and related losses will look to recover from the responsible parties, mainly Grace and Synergy Marine.

However, Grace and Synergy Marine have jointly filed a petition to limit their liability for the collision that caused the collapse to $43.6 million.

Under the United States Limitation of Liability Act of 1851, parties to maritime accidents can attempt to limit their liability for damage to the value of the vessel and the freight onboard.

Its petition states that the vessel Dali has an estimated value of $42.5 million with $1.17 million of pending freight onboard.

"Break Limitation"

According to Jon Werner, a partner at New York-based Lyons & Flood LLP who represents insurers in maritime coverage disputes, claimants are likely to attempt to break the limitation of the 1851 Act asserted by Grace and Synergy Marine by arguing that their losses resulted from negligence caused by management or that it knew or should have known about the Dali's power issues.

If the claimants can break the limitation cap, they can access the full amount of P&I coverage available.

"If limitation is not broken, however, the claimants will have to split a limitation fund which is probably under $50 million," Werner told *Business Insurance.*

This Just In

event, where artificial intelligence technology caused a failure of computer systems' security. The new Affirmative AI Endorsement language also expands the trigger for a funds transfer fraud (FTF) event to include fraudulent instruction transmitted through the use of deepfakes or any other artificial intelligence technology.

…Active Assailant Insurance rates are on the rise because of increased frequency and higher court awards, according to Tim Strong, London-based head of crisis management for Aspen Insurance Holdings Ltd. Tracking annual data, the organization says there were 656 mass shootings in 2023, 646 in 2022, and 689 in 2021. Mass shootings jumped from 414 in 2019 to 610 in 2020. "We do keep seeing an increase in the frequency and severity of mass casualty events, which does need to be reflected in the underlying rates of clients," he told *Business Insurance*.

Is it Time to Set Up Your Own Captive Insurance Company?

Last year property insurance rate increases, and rising health insurance costs led more companies to form captive insurance companies.

In addition to health insurance, workers compensation and automobile physical damage have typically been good prospects for self-insurance or even creating one's own captive insurance company. The large number of exposure units in these lines makes it easier to meet the probability threshold needed to predict losses with some level of confidence.

To get an idea of the basic framework for self-insurance, including setting up a captive insurance company, let's look first at workers compensation self-insurance.

What are the advantages and disadvantages of self-insuring workers compensation?

Most companies purchase workers compensation coverage from traditional providers, either through a private insurance company or from a state-owned insurance company. You pay your premiums and your insurer takes care of handling and paying all claims, and it bears all financial risk.

Self-insurance unbundles those functions with the primary goal of reducing costs.

What are the Benefits?

- Taking a pay-as-you go approach to claims rather than paying high premiums frees up cash flow
- Claims management expenses are usually lower when managed in-house or by a service company or third-party administrator (TPAs)
- Administration costs are usually lower because you are not paying for insurance company profits and the insurance company's higher overhead costs.

What are the Disadvantages?

Most companies have no expertise in claims handling and loss control.

However, there are very workable solutions to these problems. In fact, most self-insureds don't manage their own claims. They use service companies or TPAs for these and related services. For example, depending on the industry, specialized medical and legal knowledge may be required, along with negotiation skills, risk management, safety, and loss control expertise. All these services can be outsourced to reputable and dependable providers.

Severity and Frequency Issues

The other disadvantage to self-insurance is that while most claims are small, a single large injury claim can wipe out whatever reserves you've allocated to fund your workers compensation losses in a particular year. Two or more such losses could be devastating. In addition, there could also be an explosion of small claims that add up to breaking the bank as well.

The simple solution to both scenarios is to purchase insurance — or, as it's also called, reinsurance (since the primary insurer is the self-insured business). This is not typical workers compensation insurance, however. It's money to pay the workers compensation losses that you, as a self-insurer, have taken on for yourself if your losses exceed your budget.

continued on next page

Primary Reasons for Employers to Consider Self-Insuring Workers Comp

- You have good claims experience and think you're paying too much.
- There's a lot of money held up in claims reserves that you are not getting cash flow benefit from.
- You would like to be more involved in the claims handing experience.

Property Captives

Besides the potential to lower overall costs, setting up a property captive can also achieve certain tactical objectives:

- When one part of a firm's risk portfolio presents problems for the marketplace (rates are too high because risk is high), one solution is to create a separate cell for it and self-insurance it so that it doesn't affect the insurance pricing for the rest of the portfolio. (This is a tactic often used in managing health insurance.)
- Using a captive can also be a way to access reinsurance when additional capacity is needed. "Property risks also can be covered on a quota share basis in a captive to build more capacity," according to Michael O'Malley, managing director at Concord, Massachusetts-based Strategic Risk Solutions Inc.

Capitalization

The challenge for setting up a property captive is capitalization. Regulators require higher limits for property captives than for health insurance or workers compensation. "If you're not talking $5 million and above, you're probably not making any sort of dent in your commercial market placement," Jason Palmer, Burlington-based head of U.S. captive management at Willis Towers Watson PLC., told *Business Insurance*.

Another problem is when a captive needs to be fronted by an insurance company. Often banks and financial institutions won't accept coverage without a fronting insurer.

Of course, self-insurance is not a practical alternative for most businesses, simply because they are not large enough to scale to the level needed to make self-insurance really work. But even then, it's good to know about it. Because even if you aren't big enough now, you may be someday.

Please give us a call if you'd like to explore your self-insurance options. ■

Billboard Attorneys Are Driving Up Insurance Rates

Excessive litigation is compounding the problem of rising auto insurance costs, according to a new report by the Insurance Information Institute.

Legal System Abuse – State of the Risk examines the tactics used to initiate more lawsuits, to drive up a defendant's litigation expenses and settlement payouts, and to secure outsized monetary awards after jury verdicts. Plaintiff attorneys often use aggressive marketing and advertising techniques to attract potential plaintiffs. These practices are prevalent nationwide as plaintiff's attorneys hint at the promise of a financial windfall for their clients through multiple channels – highway billboards, television advertisements, and social media.

"There are real costs behind what we all know and see plaguing our roads with promises of settlement dollars, as billboard attorneys are racking up fees, and consumers are found to be getting less and less. The price of insurance is the effect, not the cause of risk, and there must be more work done to curb legal system abuse, as auto insurers – both personal and commercial – are seeing significant increases in claims costs when attorneys enter into the picture," stated Sean Kevelighan, CEO, Triple-I. "What's more, there are multimillions of dark money investor dollars entering into the fray to try and get their share. Some of these investors are sovereign funds, which may very well pose increased national security risks."

Third-party litigation funding (TPLF), a multi-billion-dollar global industry where hedge funds and other financiers invest in lawsuits in exchange for a percentage of any settlement or judgment, allows plaintiff's attorneys to finance more litigation through dark money.

continued on next page

Few states outside of either Montana or Indiana even require the disclosure of a third-party litigation funder's involvement in a civil lawsuit. An effort to implement TPLF regulations in Florida this year appears to have stalled in the state's legislature due to efforts of the trial bar. This lack of transparency makes it difficult to hold plaintiff attorneys and their clients accountable to good faith standards, the issues brief explained.

"We're seeing publicly traded and private third-party litigation funders getting more than 20% in investment yield. Where else can you get that kind of return?" said Dale Porfilio, FCAS, MAAA, chief insurance officer, Triple-I.

Distracted Driving Accidents Driven Mostly by Cellphones

Cellphone use by individuals operating a motor vehicle continues to be the largest contributor to distracted driving in the U.S., according to the latest Issues Brief from the Insurance Information Institute (Triple-I).

The U.S. personal auto insurance industry saw its costs soar, paying out approximately $1.12 in claims and expenses for every $1 collected. The rising cost of replacement parts, inflation, and legal system abuse also contributed to this trend.

Cellphone use — which includes dialing, texting, and browsing–were among the most prevalent and highest-risk behaviors found in governmental and private sector studies, Triple-I's report explained.

A total of 2.5 percent of drivers stopped at intersections were talking on hand-held phones at any moment during the day in 2021, according to a 2022 national observational survey from the National Highway Traffic Safety Administration (NHTSA).

Solutions: Telematics and UBI

Telematics and UBI (usage-based insurance) are technologies that can potentially help insurers—and their policyholders—to better understand a driver's risk profile and tailor auto insurance rates based on individual driving habits.

An Insurance Research Council survey in 2022 found 45 percent of drivers said they made significant safety-related changes in how they drove after participating in a telematics program. Another 35 percent said they made small changes in their driving behavior. Policyholders became more comfortable with having their insurer monitor their driving behavior when it resulted in potentially lower insurance costs during the onset of the pandemic.

"If telematics can influence drivers to change behaviors and reduce the number of accidents, the nation's roadways will be safer and auto insurance can be more affordable," Porfilio concluded.

Triple-I's just-released report, Distracted Driving: State of the Risk, examines the effects of distracted driving and how it is contributing to more hazardous roadways and higher costs.

Insurance Buyers' News

The information presented and conclusions within are based upon our best judgment and analysis. It is not guaranteed information and does not necessarily reflect all available data. Web addresses are current at time of publication but subject to change. This material may not be quoted or reproduced in any form without publisher's permission. All rights reserved. ©2024 Smarts Publishing. Tel. 877-762-7877. http://smartspublishing.com.