

LIABILITY EXPOSURE

south of the 49th parallel



It is the largest product liability verdict so far this year - and one unheard of within Canada's kinder, gentler legal system. A Florida jury this past August ordered a Wisconsin pool-pump manufacturer to pay U.S. \$104 million in compensatory damages to the family of a boy who sustained permanent brain damage after his arm became stuck in a pool drain three years ago. And the whopping \$104 million is just the beginning. Additional punitive damage awards are reported to be pending, as the pool pump company was allegedly aware of a manufacturing defect for years, yet did nothing.



By Mark J. Ram President & CEO,
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To a Canadian, these staggering dollar amounts may sound unbelievable. But they are a tough reality these days in the U.S. court system. Today, it is one thing to insure a customer doing business exclusively in Canada - and quite another thing when, for whatever reason, your client (or your clients' product or service) happens to venture south of the 49th parallel.

"In the unfortunate event that you or your client is sued in the U.S., you

might feel like Dorothy in the Wizard of Oz -

- as though you have just landed in a strange, distant land," says David Duke, a noted U.S. defense attorney with Young, Moore and Henderson P.A. of Raleigh, N.C.

Getting into an accident or dispute in the U.S. means there's a very real chance that you're going to go to court. It's that simple. At fault or not, the U.S. legal system is a whole differ-

ent ballgame with a unique set of rules.

STARK DIFFERENCES BETWEEN CANADIAN AND US LEGAL SYSTEMS

It is not uncommon to face multi-million dollar judgments south of the border. While personal injury awards (compensation for pain and suffering and other non-pecuniary damages) are capped at less than \$300,000 today in Canada, there is no such ceiling in the U.S.

If you have a tort liability and you are

in south Florida, grab your ankles, it's going to hurt!" says Duke. "New York, South Texas ... these are just some of the most notorious hotbeds for high verdicts." (See Exhibit A) Punitive damage award amounts have increased tenfold in the U.S. In recent years, court award amounts in the U.S. have gone through the roof, to put it mildly. An article in the February 2003 edition of The National Law Journal, "The Largest Verdicts of 2002" cites the total value of 2002's 100 largest court awards as nearly 350% more than the 2001 total. If that isn't shocking enough, consider the fact that punitive damage award amounts have increased tenfold - from \$3.2 billion in 2001 to \$32 billion in 2002 - for the same number of cases.

ANTI-BUSINESS SENTIMENT RIFE IN U.S. COURTROOMS

Why is this happening? Well, a lot points to juror anger. One recent study of jury behaviour shows that in the wake of Enron and other corporate scandals there is more distrust than ever of corporations. These days, aggressive plaintiff attorneys have emerged styling themselves as business "killers" and are wildly advertising their ability to win multi-million dollar verdicts on behalf of "the little guy". In fact, it's gotten so bad that the U.S. Chamber of Commerce has spent \$100 million since 2000 and will spend another \$50 million or more this year to challenge judges supported by trial lawyers and labour unions.

BIAS AGAINST FOREIGNERS

Inherent bias against corporations in the U.S. legal system is widespread. But be aware: if you're a Canadian insurance company with a Canadian insured being sued in the U.S., you now have a second major strike against you, one that US insurers don't face: a strong bias against foreigners in the courtroom overall and among jurors especially. This has been the case for years, but in the current political climate, the average American juror looks upon Canadians with even less regard for our country's failure to support the US in the war in Iraq. So your insured (and you) have the cards stacked even further against them.



Red Alert States

Proceed with even more caution if you (or your insured) are exposed in:

- Southern Texas
- Southern Florida
- North and South Carolina
- New York, especially Bronx County
- Erie County (near Buffalo)
- New Jersey
- Mississippi
- Cook County (Chicago) in Illinois
- Orange County California

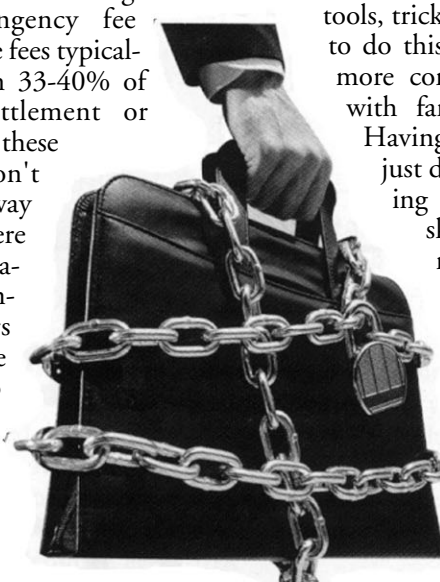
EXHIBIT A

It's far easier being a U.S. insurer in the U.S. than a Canadian insurer with U.S. exposure.

RETAIN EXPERIENCED COUNSEL TO MANAGE CLAIMS

To be successful within the U.S. system you need top flight defense lawyers. Why? Well, let's see what you'll be up against.

For starters, U.S. plaintiff attorneys are most often working on a contingency fee basis. As those fees typically range from 33-40% of the final settlement or court award, these lawyers don't tend to go away too easily. There are also associations of plaintiffs lawyers across the U.S. who have banded together to share strategies and tactics on how to sue specific industry groups, like the one that specializes in suing trucking companies. After all, the average juror has had a scary experience or two with a "big bad truck" bear-



ing down on them on the highway. Throw in a foreign truck, and you have the makings for a real party.

Another major problem is that plaintiff attorneys today are able to get more information -- information that 20 or 25 years ago they would never think of getting. Today, U.S. plaintiff attorneys are able to dig deep, looking for anything they can use to inflame a jury, such as employee hiring, training and disciplinary practices. If they find your insured's actions somewhat negligent in the past with regard to any employee, they will use that to demonstrate overall negligent practices on behalf of the whole company, inferring that those practices must have affected this particular loss somehow. That is why it's so critical to know how to train your U.S.-exposed insureds on best proactive operational practices. The difference between your insured being prepared or not before a U.S. loss occurs can be worth many millions of dollars.

KNOWING WHEN AND HOW TO SETTLE A U.S. LAWSUIT

For all these reasons, it's important to know when (and how) to settle in the U.S. Unfortunately, the tools, tricks and tradecraft required to do this are quite different and more complex than in Canada, with far greater consequences.

Having settled losses in Canada just doesn't come close to giving a claims examiner the skills or confidence they need to navigate the murky U.S. claims waters effectively. It's over before it starts. One could almost compare it to giving a firefighter a water pistol to put out a four-alarm fire.

Another situation an insurer will likely find itself in: losses

where the plaintiff's attorney will be asking for far more than the, say, \$10 million policy limit. While you feel it's likely worth

considerably less than that, the jurisprudence range is so wide that it could, on a bad day in court, go as high as they're asking. However, they're willing to settle for the full policy limits right away. Just say no? Well, it's not that simple. Your insured will likely be sending you a legal letter advising you to settle within policy limits, which, if you don't, would allow your insured to go after you in a "bad faith" action for the amount over policy limits that they'd normally be liable for. In the U.S., that could be in the millions of dollars.

CANADIAN BROKERS: LOOK BEFORE YOU LEAP

For a Canadian broker there's always a very real Errors and Omissions risk present. So ensure you match your U.S.-exposed insured with an insurer who can properly handle the minefield of US risk, one who can also help you learn how to train your insured to be ready for the risks they face in the U.S. Pick carefully: a cheaper price up-front can sometimes be a lot more expensive at the end of the day.

U.S. RESERVE DEVELOPMENT - A LEADING CAUSE OF FAILURE

In the U.S., it can take years for bodily-injury or liability claims to fully develop, far more so than in Canada. There are no magic tables to tell someone how to reserve a U.S. loss. The majority of Canadian insurance personnel, who have no material experience in handling serious US claims, typically under-reserve their existing claims exposures and unfortunately don't find out until it's too late. So don't let the loss experience that you receive from an insured's previous Canadian insurer fool you.

To play in the U.S., you really have to understand and properly estimate your impending claims costs and apply meticulous exposure rating if you have any hope of properly pricing your insurance products. The real deal is in having statistically credible data, knowing the right U.S. laws, jurisprudence and local biases,

and above all else, experience. U.S. claims development has killed so many U.S. insurers; it's just that much harder for Canadians.

THE US-EXPOSURE DEATH SPIRAL - NO MAGIC FORMULA

Too often, Canadian insurers follow the same death spiral when it comes to underwriting U.S. exposure. The extra zeroes in the premiums for a U.S.-exposed line of business can seem rather attractive (especially with the top-line volume and market-share mentality that was so prevalent in the insurance industry up until recently). The spiral starts when they jump into a U.S.-exposed line and start writing business. After the first year or two, they look at the portfolio's loss ratio (almost always dramatically under-reserved at that point, due to the reasons noted in the above paragraph) and mistakenly believe they're profitable, having been lulled into a false sense of confidence through inexperience.

The line now looks deceptively lucrative, to the point where they believe they can cut the prices even further, gain more market share and still generate "excellent" returns. Their appetite increased, they write even more business and cut their

the insurer finds themselves in a bank-breaking, high triple-digit combined ratio mess. Jobs are lost and the departure from the line is made. But worst of all, the effect this can have on the brokers and insureds can be devastating.

One telling example is long-haul trucking insurance which has one of the highest business failure rates of any line of insurance in North America. The estimated average combined ratio, fully developed, for Canadian insurers of long-haul trucking in the soft market years from 1996-2001 was north of 150%! So beware: life expectancy for those companies who dare to price without the knowledge is historically short. The bottom line: there's no magic formula for finding a cheaper way to write US exposed business. If you think you've found it, you're fooling yourself.

Just one glance at Exhibit B below, which as examples of US exposure shows values for long-haul trucking claims in the US versus what they would likely have been in Canada, tells the whole story.

All in all, if you're going to take on U.S. risk, go in with your eyes open, arm yourself with the right expertise and make sure you're willing to make the

long-term investment.

For an insurer, building the infrastructure to properly handle Canadian insureds with true U.S. exposure is critical, costly, and takes time. Remember, the lack of understanding of US exposure has killed the performance of so many Canadian insurers in the past, and it's only tougher today.

We may think of Americans as our friendly cousins to the south, but in today's legal climate we are not likely to be embraced as family if

we are embroiled in an insurance dispute in a U.S. court. Choose your partners and your risks wisely, price carefully, pay attention to safety, compliance and hazard management issues and, above all else ... try to stay out of the U.S. courts!

Long-Haul Trucking U.S. Court Decisions on Bodily Injury Claims		
Actual U.S. Incidents	U.S. Verdict (in CDN dollars)	Estimated Settlement ... If it happened in Canada
39 year old man struck by trailer wheels, resulting in reduced vision, impaired speech and concussion. Long term memory severely affected.	\$19.5 Million	\$1.2 Million
Tractor-trailer jackknives, resulting in collision and death of a woman and her 7 year old son. Husband and second son survive with emotional distress and minor injuries.	\$7.7 Million	\$800,000
Tractor-trailer crossed centerline, killing two teenagers.	\$5.5 Million	\$500,000
Box fell on a dockworker's head requiring cervical fusion.	\$2.0 Million	\$250,000
An 18-wheeler improperly passed another vehicle. Third party now requires round-the-clock care.	\$12.7 Million	\$3.5 Million
Two rear tires flew off a trailer and struck a man. Injuries consisted of broken/paralyzed left arm, broken ribs, collapsed lung and degree of brain damage.	\$6.8 Million	\$1 Million

EXHIBIT B

prices further. They think they've found the magic formula. The portfolio gets larger. But then, after a few years, they find the prior-year claims on the books in this line are starting to develop, and settle for 10 times their reserve levels. Multiply that by many, many claims in the U.S.-exposed book of business, and suddenly