1. Introduction

Reinsurers have lost many billions of dollars as a result of the industrial use of asbestos since the 1950s. Accordingly they have come to regard this subject as completely unviable for either insurers or reinsurers to deal with, since the time frame over which claims can evolve is unlimited. Their own credit ratings and their discussions with their stock-market analysts have become materially entangled with the issue.

Hence, the major reinsurers have been aiming to implement a total asbestos exclusion since the Autumn of 2002. This is perhaps not unreasonable in principle, but it is certainly complex in practice. We have encountered various arguments for, and against, the implementation of a direct insurance exclusion, and these are discussed below.

This report aims to clarify the core issues at stake, and follows the broad chronology of the discussions in which we were engaged at the end of 2002. Whilst much of this debate was focused upon the UK, Irish and Australian markets, the issues arise much more broadly. Our aim in producing this paper is to foster awareness of the issues in markets outside the USA and Canada.
2. The constraints upon a debate

European Competition Law and equivalent legislation in other countries is extremely clear that explicit "market debate" amongst market practitioners is against the law. This is for well-understood reasons, although it is also appreciated by the law-makers that best practice can often only emerge through the dissemination of ideas and opinions. Accordingly, there are many more constraints upon an open debate today than there were in earlier times.

What has certainly been possible for an intermediary in our position is to listen to opinions expressed by our individual insurer clients, and by individual reinsurers, with a view to negotiating the broadest possible form of reinsurance cover for our clients. We believe that through that process, and through the dissemination of discussions such as this paper, we raise the quality of our clients' awareness of the issues, and thus improve their ability to negotiate appropriate terms with their reinsurers.
3. The debate towards a General Liability Exclusion

(a) Unclear issues before Reinsurers started the process

The first problem with the entire debate has been that some Reinsurers were clear that something had to be done before they had fully analysed the underlying issues. They started to implement moves towards their objectives before they had reached precise conclusions as to how best to implement their objectives.

We can sympathise with their sense of urgency on the issue, in that the entire asbestos problem is something that the whole community needs to address more fully. It naturally falls to the ultimate risk carriers to take a leadership role in this context. It would have been more acceptable to insurers if the process had been given plenty of warning, with appropriate time for open debate. However, with the competition law pressures already noted, one can see how very difficult it has become to lead change in this type of context.

We still feel that the core issues here have not been adequately articulated by Reinsurers. Accordingly this paper endeavours to set them out (see section 6).

(b) The Reinsurers started the process

An early milestone in the debate of Autumn 2002 was the release by one reinsurer of an initial reinsurance exclusion draft text which was very all-embracing. This read:-

“...in consideration of the premium charged for this reinsurance, it is hereby understood and agreed that this contract shall not apply to and does not cover any actual or alleged liability whatsoever for any claim or claims in respect of loss or losses directly or indirectly arising out of, resulting from, or in consequence of, or in any way involving asbestos, or any materials containing asbestos in whatever form or quantity."

We were surprised at the thought that the text should apparently make the presence of a single asbestos fibre, somewhere in the context of a claim scenario, sufficient to enable reinsurers to deny all liability, regardless of whether the asbestos fibre had anything to do with the loss itself. In addition, phrases like “directly or indirectly arising out of” or in any way involving” left enormous scope for reinsurers to refuse perfectly bona fide original claims.

(c) UK Insurers (amongst others) were strongly unimpressed

Accordingly, various UK and other insurers made strong objections to this reinsurance exclusion for a range of good reasons, most obviously the considerations above. There were a number of other alternatives being proposed by other leading reinsurers, all of comparably unpalatable breadth. Accordingly we developed a first draft of a compromise (“ABC 2003”) which was intended to deflate some of the wider licence implicit in these initial drafts:-

“It is hereby understood and agreed that this contract shall not apply to and does not cover any actual or alleged liability whatsoever for any claim or claims in respect of loss or losses directly or indirectly arising out of, resulting from or in consequence of, asbestos, whether or not there is another less critical cause of loss which may have contributed concurrently or in any sequence to a loss.”

This too met with heavy criticism from both sides. Reinsurers at that point were adopting an inflexible line. Insurers on the other hand did not find it appealing either:-

– “directly or indirectly arising out of” - it was felt that this allowed the presence of asbestos to justify a non-payment of a claim no matter how irrelevant to the claim the asbestos might be. In reality we found that Reinsurers were arguing that this phrase had to be used because it is at least arguable that the mesothelioma condition is caused by the cancerous growths, which in turn are caused by the presence of asbestos fibres, hence the problem is arguably always an indirect one.

– “less critical cause of loss” - it was thought that this was excessively open to interpretation, and would provide lawyers with an easy target to aim at in the destruction of the objectives of the clause. This issue was addressed in later re-drafts of the clause.

– There remained the problem of ambiguity at best in whether non-asbestos elements in a loss would be disqualified from recovery by the presence of asbestos elements.

Insurers then raised the question of a mixed smoking cancer / mesothelioma case. This seemed to us to be too complex to address in any clause - we felt that it would always be possible to dream up scenarios which were going to cause trouble with any written text. In practice we feel the parties concerned - or the courts, if need be - usually come to a fair compromise in this type of situation.

Insurers also raised the interesting problem of asbestos brake linings in motor cars - if they fail and an accident arises, insurers face a normal motor loss caused by a product containing asbestos, although there is no asbestosis involved. The answer to this (as a Motor problem) is that reinsurers should be asked to limit the application of any Asbestos exclusion clause to non-Motor classes. This, in turn, gives rise to the thought that in principle one could imagine this problem arising in GTP with brake linings in trains. Here we have some anecdotal evidence that in practice most of the brake linings under discussion were phased out a long time ago. It may be hoped that insurers could create more transparency in the future on this point.
One major UK insurer raised a number of more general objections to the whole process. These included:

– No good solution (it was argued) can be expected to be found while there is inadequate general comprehension of the key issues here. Everyone concerned with this problem needs to **understand the “trigger” problem**, being that the cause of the loss may drive a claim back to some very old policies. The absence of a clearly defined date of loss is becoming an advantage to claimants, rather than a disadvantage. Dates of exposure, dates of developing ill health, and dates of taking medical advice are all possible issues in a possible court case.

– The US experience in this field was that the courts’ response to the problem was to **find a way to make insurers pay**. The early signs (e.g. the Fairchild case) are that the UK system is heading in the same direction. Again, this itself is not an objection, but we certainly concur with the view that awareness of this reality is an essential element in moving towards a good solution.

– We detected a clear belief on the part of this major insurer that inserting draconian exclusions to 2003 and future policies, would be more than likely to **drive courts into precedent-creating “triple trigger” types of judgements**. These (it was argued) could make future liability underwriting environments even harder for insurers to manage.

– A further argument to forestall any exclusionary discussions was made to the effect that, UK Government intervention in the Health and Safety at Work field has developed to such a level over the past fifteen or so years, that it has now become almost impracticable for new asbestos fibre exposures to arise in anything like the cavalier fashion of workplaces in the 1950s through to the late 1970s. Hence (it was argued) there should be no need for reinsurers to apply exclusions, and to do so would amount to the shutting of stable doors long after far too many horses had bolted.

– Lastly, it was forcefully argued by this insurer (amongst others) that we all needed to be very careful to avoid getting involved with any explicit “market debate” for fear of falling foul of the **EU competition laws**. We obviously concurred with this - see the discussion above.

(d) Reinsurers offered “re-drafts” that showed no progress

Deep into December 2002, we were still being offered further “re-drafts” from reinsurers such as:

“This contract shall not apply to and does not cover any actual or alleged liability whatsoever for any claim or claims in respect of loss or losses directly or indirectly arising out of, resulting from, in consequence of, contributed to or aggravated by asbestos in whatever form or quantity.”

Again, phrases like “… or aggravated by asbestos in whatever form or quantity” give reinsurers the right to deny responsibility for a Third Party Fire loss where 99% of the damage was nothing to do with asbestos. The presence of a tiny asbestos removal issue in one corner of a building, even though this might cost 1% of the claim, would be enough (on this reinsurer text) to allow the entire claim to be excluded.

(e) We reviewed the practice in the USA

We studied the **current US practice**, where Reinsurers are generally happy for their clauses to depend upon original insurer exclusions:

“Asbestos liability to the extent excluded in the Company’s original Policies. However, this exclusion will not apply:

a. When a judicial entity having legal jurisdiction invalidates the Company’s exclusion, thereby obligating the Company for liability for asbestos when such liability was intended to be excluded by the Company’s asbestos liability exclusion.

b. In respect of any Policy written in a state whose insurance regulatory authorities have prohibited the Company from including any asbestos liability exclusion in its Policies.”

The underlying insurer exclusions were too broad to be acceptable in Australia, Europe or other international markets. We noticed that the US texts were similar to the original reinsurer drafts proposed for non-US use.
(f) A preliminary compromise - ABC 422

Finally we had a constructive meeting with a major Alpine reinsurer at which we reached agreement on the principles contained in the "ABC 422" clause:

“This reinsurance does not cover any loss cost expense liability for injury loss or damage directly or indirectly arising out of or resulting from the manufacture mining processing distributions testing remediation removal storage disposal sale use of or exposure to asbestos or materials or products containing asbestos whether or not there is another cause of loss which may have contributed concurrently or in any sequence to a loss.

As regards liability for property damage, only that part of any such loss which is directly or indirectly arising out of or resulting from the manufacture mining processing distributions testing remediation removal storage disposal sale use of or exposure to asbestos is excluded by the foregoing.”

This at least proposes language which could sensibly be transferred into direct insurance policies. It also makes clear that for Third Party Property Damage, only that part of original claims where the asbestos is the cause of the problem is affected by the exclusion.

The ABC 422 text is far from perfection. For example, it fails to address the question of what should happen to bodily injury losses which are only partially attributable to asbestos. A further problem exists as regards the risk of the “falling sheet of asbestos", which could cause personal injury, or even property damage. The ABC 422 was simply the best outcome that could have been negotiated at that particular point in the market, which was of course heavily distracted by many other considerations.

Hopefully the market will evolve towards a more satisfactory text over time.

(g) Contemplating a possible “ACOD” solution

There was a proposal from some parties to move the asbestos reinsurance treatment towards the “ACOD” type of structure. This was pioneered by the London "Accident Circle", in the context of Occupational Disease (thus "ACOD") within Employers' Liability policies, with the effect that one person would be treated as one event. We would see this as having many undesirable ramifications, for example:

— The ACOD structure does not address Third Party Property Damage claims - how would these be treated?
— It sets a potential precedent for all other General Third Party and Products exposures - how would the market begin to handle e.g. pharmaceutical exposures if reinsurance of these risks were to be structured on a one-person-one-event basis? This would quickly lead to a collapse of the purpose of the product.

Some insurers adopted this, but we would have strong reservations about recommending it in any general way while the more standard forms of cover continue to be available. If an insurer found this an appealing solution specifically for asbestos issues, then of course one could contemplate drafting an appropriate text, provided it was possible to find a satisfactory text that constrained the clause only to apply to "the asbestos issues", and also addressed the Third Party Property Damage question.
4. Addressing other classes

The foregoing focuses upon the General Liability/Products Liability problem. What are insurers to do with the Employers’ Liability and/or Workmen’s Compensation Act (WCA) problem, where the policy format is statutory? What are Reinsurers likely to be willing to do in this context? One answer here lies in the commercial reality, that almost all international Employers’ Liability and WCA reinsurances carry a deductible which is higher than most conceivable one-person asbestos claim awards - and also is subject to the Index Clause. So, for Employers’ Liability and WCA, the impact of the (standard) ACOD clause makes the reinsurer exposure almost negligible, hence the problem is passed comprehensively back to the insurer to address. Ironically, a very recent UK court award has been made for four million pounds for a single asbestos claimant, but it is well recognised that this is something of a “freak case”. Since the very great majority (if not all) Employers’ Liability/WCA treaty reinsurances in the international (excluding USA/Canada) markets have carried an “ACOD” clause since 1985, the issue effectively has rested with direct insurers for over fifteen years.

Turning to Professional Indemnity and Directors & Officers, we found that we were able to renew most international treaties in these classes into 2003 without the imposition of any Asbestos exclusions. However, leading reinsurers have made clear statements to put us, and our clients, on notice that for 2004, an appropriate exclusion will need to be introduced.

There must be some perfectly fair questions arising from any possible application of this type of exclusion to Professional Indemnity and/or Directors & Officers policies. For Architects and Surveyors, one can see the risk, but it is not clear why this risk should be any less controllable than the main systemic risk involved in building design, or normal structural survey and valuation. For other risks such as the Professional Indemnity peril for lawyers, it is much harder to see the risk. It must be even more heavily questioned by insurers as to what sort of rational justification might be provided by reinsurers to explain to direct insurance customers why an exclusion might be necessary.
5. Timing of incorporating any new exclusions

As regards timing, we believe that most UK/Irish reinsurance programmes starting on January 1, 2003 ended up incorporating a General Liability/Products exclusion, which is to be applicable as far as original policies incepting on/after July 1, 2003 are concerned. The equivalent in Australia was for an April 1 attachment date, although this is still being discussed.

This of course remains problematic in several ways. Insurers are understandably cautious about accepting any reinsurance conditions that might put them at a disadvantage as compared to their competitors. Hence, they argue for as late an implementation date as possible. Reinsurers naturally want to see something happen at the direct level, and negotiate as early a date as possible. Unfortunately, while the core issues underpinning the problem remain opaque, it is very hard for anyone involved to draft a mature text. It also takes several months for even a finally agreed text to see effective incorporation into original insurance policy documentation.

In the absence of any better solution, our view is that it is better to ask original insurance buyers to contemplate a well-considered, mature text with the associated issues for all parties articulated as clearly as possible, than to try to move forward without appropriate preparation.
6. What are the core issues?

After extended discussions with many interested parties, we perceive the following as Reinsurers’ core issues:-

– As regards liability for Personal Injury, we think that Reinsurers generally have lost confidence in society’s ability to manage the asbestos risk. Whilst there have been many good initiatives (usually government-sponsored) to require particularly construction employees to use well-researched precautions in the handling of known asbestos problems, we think that Reinsurers regard these initiatives as being inadequately comprehensive. The exposure to the unknown risk, and the risk of incompetence or inefficiency in the execution of precautionary measures, are such, that Reinsurers simply do not see how they can cover the Personal Injury risk any further.

– There is a limited exception to this, in that some Reinsurers appear willing to contemplate providing cover on a “one-person-one-event” basis. However, this is of very limited use to most insurers, since the deductibles, at which most of the reinsurance involved attach, are sufficiently high to make the real engagement of the reinsurers more or less nominal by comparison with insurers’ burden of the risk involved.

– A further nuance on Personal Injury is that Reinsurers’ real concern appears to be focused upon the “disease” risk and/or long-term health hazard. It should be possible to draft contractual text that would narrow the area of focus down to this element of the exposure, and thus avoid the “falling asbestos tile” problem.

– As regards liability for Property Damage (and liability for other non-injury losses), we think that Reinsurers’ broader perception is of a society with many substantial and valuable buildings and properties, in which incalculable asbestos problems are latent.

– Reinsurers’ perception is that the economic loss inherent in the asbestos in these properties has already happened. They do not believe it makes any sense for insurers or reinsurers to purport to offer coverage against such loss. The loss concerned perhaps may only fall to be accounted at the point where the building concerned suffers a fire (thus exposing the need to address the latent asbestos issues). Reinsurers contend that such a loss should already have been accounted (for example in the write-down of the property’s value).

– A nuance here is that asbestos removal, or clean-up, might be assessable today in relation to today’s “clean-up” standards and costs, but this can vary uncontrollably with changing legislation and fast-moving market conditions.

– Reinsurers perceive that the grand total of the economic values involved may far exceed the entire assets of the insurance industry.

– They also regard it as highly questionable whether it is good use of either insurers’ resources or the resources of the original insureds that, over perhaps some decades into the future, the parties concerned should be entering into contracts that will inevitably be disputed on this issue.

The above may not be exhaustive. In the interests of keeping this paper to a digestible length, we have not attempted to set out in full the possible counter-arguments of insurers or original insurance purchasers. Nevertheless, we find it hard to avoid the conclusion that the broader issues set out above merit some real consideration.
7. Where do we go from here?

It is clear that there is no simple or single answer to this issue. Direct insurance buyers inevitably have strong concerns that they should have as comprehensive cover as possible, and we are certainly not encouraging any form of limitation of cover in raising the issues here. Insurers are rightly resistant to any “solution” where reinsurers intrude inappropriately upon their well-considered business practices. Reinsurers nevertheless have a viewpoint which has to be considered responsibly if insurers and reinsurers are to maintain their mutual co-operation. The question inevitably follows: Where do we go from here? We consider first, the positions from where we start. We then review the scope for progress.

(a) Where are the parties positioned?
Thus far we have:

– the original purchasers are focused upon maintaining exclusion-free cover
– direct insurers in the USA are increasingly clear that their problems are life-threatening
– direct insurers outside the USA are currently resistant to addressing the problem, although the levels of their share prices may or may not be recognised as (at least partly) being linked to this issue
– reinsurers world-wide are adamant that trenchant exclusion language is the way forward.

The biggest gap lies between the insurers’ position and that of the reinsurers. The pattern in the USA has been for insurers to move towards the reinsurers’ position. If this happens outside the USA, we will have more friction between buyers and sellers of a kind we have all been trying to avoid.

This suggests:

(b) What about bridging the gap with some cover?
Nobody appears to be discussing the possibility of offering a professionally underwritten product. This is a pity, because it is quite apparent that this could form an appealing answer to the issue, at least in part.

– First party insurance for asbestos clean-up and removal, following fire and other named perils, merits real consideration. With appropriate surveys and a suitably designed policy form, this should be an insurable risk.
– Third party insurance for various specific forms of liability, e.g. liability for escape of asbestos following fire, could be considered on an occurrence policy form, conditional upon suitably strong reporting conditions
– Third party insurance could be considered more broadly on an appropriately strongly constructed claims made policy form.

If insurers (perhaps working constructively together with reinsurers, if reinsurers can be convinced to address this issue positively) can show that they have researched the possibility of active insurance professionally, then they will stand on much stronger ground to deflect criticism against the exclusionary alternative.

(c) What about a better exclusion?
In the last resort, we may be forced to consider a professionally worded insurance exclusion.

However, we ought to be a long way away from contemplating this. We at Willis certainly believe that the extent of the recent debate’s focus upon the appropriate text for a reinsurance exclusion is a very undesirable distortion away from where the insurance and reinsurance industry’s focus should have been. Hence we do not propose a further alternative for wider discussion. Rather, we would encourage a more constructive approach to the problem.
8. Conclusion

Indubitably, the scale of the problem is larger than admits any ready-made answer here. It must be abundantly clear that all involved might wish to examine their position with great care. It may be appropriate to review corporate strategy in relation to asbestos, and ensure that it is consistent with some of the wider realities alluded to above.

Our own role has to be limited, as we have already discussed. Competition laws make plain how careful all concerned need to be.

At the least, however, we can simply aim to raise awareness of the issues on as broad a basis as possible, and ensure, so far as possible, that our clients’ reinsurance programmes contain the least punitive conditions that are available.
Asbestos Briefing

March 2003

Willis Limited
Ten Trinity Square
London EC3P 3AX
Telephone: +44 (0)20 7488 8111
Website: www.willis.com