

## Notes from the Global Practice Leader

We believe our success in 2003 proves once again that thought leadership, innovation, responsiveness and attention to detail are what matter most to senior executives in today's corporate environment – and these characteristics continue to set Willis apart from our competition.

We expect 2004 to be an even more exciting year, as much of our infrastructure work has now been completed. We put in place initiatives such as our Risk Profile Analysis and other new technologies, designed to assist our clients in their risk differentiation and process management. Our Practice capabilities have been expanded with the addition of Executive Risk regional offices in San Francisco, Philadelphia and Denver, and we have brought on board new Practice Associates in our regional offices in Atlanta, Boston, Chicago and New York. We have also demonstrated our commitment to claims advocacy through the addition of attorneys to Executive Risks regional offices across North America.

These and other actions have positioned Willis well for the coming year, affording us many opportunities to demonstrate our commitment to quality and market leadership through a myriad of services designed to better protect our clients and their corporate assets in this transitional and dynamic marketplace.

We look forward to talking with you in 2004 about executive risk exposures, loss control measures, risk transfer options and changing marketplace realities. We also invite you to hear what our experts have to say in future issues of this newsletter and our topic-specific monthly *Alerts*. – Don Bailey

All signs are that 2004 will be a watershed year for executive risks after three years of rate increases. Most observers expect exposures to revert to lower expected norms. But will they? This newsletter will examine some of the critical risk and exposure issues facing us in the coming year. *(These issues are addressed in more detail in the Willis 2004 Marketplace Realities book available now at [www.willis.com](http://www.willis.com).)*

Because effective risk management is about mitigating and not just transferring risk, this edition will also take the opportunity to hear from one of our strategic partners, D&D Industrial Consultants, on what can be done in the areas of workplace violence and employment practices. Their proven thesis is that organizations can systematically reduce these exposures by identifying and correcting the hidden risk factors that stand in the way of successful risk management.

## Will the Fidelity Bond Market Ever Soften?!

We await the release of 2003 Fidelity underwriting results to tell us if the past three years' premium and deductible increases will be enough to return the insurance carriers to profitability. Either way, we suspect that the underwriting community should start to experience some favorable results, which may, in turn, impact premiums and coverage availability.

For Fortune 1,000 companies, there has been a marked increase in competition within the Fidelity market. This has started to stem the sharp price increases of recent years. While most companies should still anticipate an increase in pricing for the first quarter of 2004, we now believe there will be some leveling off of premium prices in the latter part of the year.



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For Fortune 500 companies, it is worth noting that the number of Fidelity insurers willing to take a lead position remains *limited*, resulting in a relative shortage of capacity for these companies. With less competition for these larger insureds, coupled with their continued flow of large claims, most Fortune 500 companies will continue to be subjected to premium hikes in 2004. As an alternative to continued price hikes, companies might explore the risk management options available in the market for those entities willing to assume more risk.

Those interested in the Fidelity market will also be watching the new loss control testing now being implemented to comply with Sarbanes-Oxley's Section 404. This section requires that public companies include a discussion in their annual reports on the effectiveness of their internal control structure. The impact of these efforts remains to be seen. The big question is whether the result will be an initial increase in fraud claims (Fidelity or D&O).

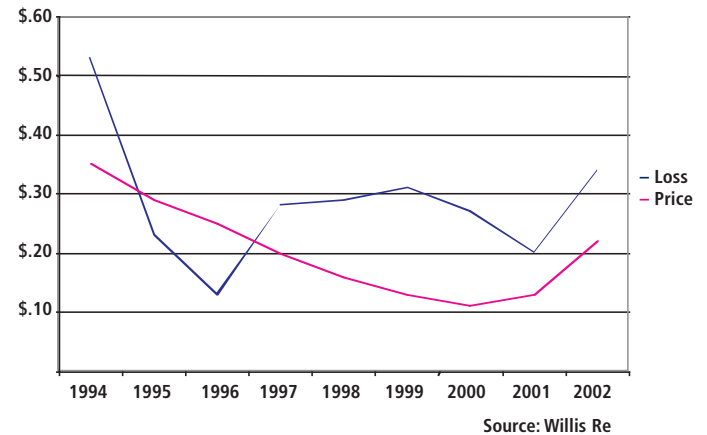
### D&O Market Conditions Improve

We believe that in 2004, D&O premiums will stabilize, depending on the nature of each company's risks, with increases in the range of 20 to 35 percent in most cases but flat renewals in others. The well-documented corporate debacles, financial restatements and under-priced D&O underwriting portfolios of the recent past resulted in some of the sharpest premium hikes and coverage cuts in recent memory. We believe that the D&O market is preparing for a recovery. New capacity is becoming available both domestically and internationally, and carriers are looking to spread their risk portfolios into mid- and small-cap segments. Carriers will still be differentiating risks, but well-run companies that can both define their strengths and outline strategies for addressing their exposures should find receptive audiences in the coming year.

We add a note of caution: Current claims inventories held by D&O insurers suggest that losses are still outstripping earned premiums in spite of rate increases that began in 2001 (*see chart below*). If claims continue to mount in the coming year, then the current softening in D&O pricing may end before it brings any sustainable price relief.

As mentioned above, a decisive factor in the coming year will be how companies fare in responding to Sarbanes-Oxley's 404 requirements on assessing their internal loss control methodology. Already impacting mergers and acquisitions, the revised compliance deadline will be watched closely in the coming months.

### D&O Industry Earned Premium vs. Losses per \$1,000 of Market Cap



### The Hard Market Continues: Fiduciary Liability

Indicators point to a hard market and, to some extent, one that is still hardening for Fiduciary Liability. There is little risk differentiation here, as almost all companies are being hit. Driving the market is a landscape filled with large settlements and adverse judgments with no immediate improvement in sight. Underwriters are concerned with employer security litigation, cash balance plan controversies and ongoing investigations into mutual fund late-trading practices and fee structures. These issues are fueling growing uncertainty about a risk sector where exposures cannot be neatly categorized.

The result is a limited choice of primary insurers, tightly managed capacity and the likelihood of further reductions in limits. Premium levels continue to see upward pressure while retentions on all fronts are "adjusted" upward.

Some good news is that 2004's new FASB requirements for additional pension disclosure in the annual reports of publicly traded companies may relieve some of the pressure on risk managers to produce arcane information as part of the Fiduciary Liability renewal process. However, this could also result in additional carrier unease when the extent of global pension obligations are spelled out.

### The EPL Market - Stabilization is Slow and Strategic

Following two years of reduction in capacity, we see signs of stabilization in 2004. Carrier support will be governed by individual risk components and controls. For larger companies and those with international exposures, the list of primary insurers has been expanded to include Bermuda-based Max Re.

However, as few carriers are willing to compete for the primary layers on large, global accounts, the full benefits of rate competition are not yet expected. On a positive note, excess capacity exists in an array of US and Bermuda facilities, and for medium- to small-cap companies the list of potential primary markets is substantial.

We anticipate the average rate-on-line increases to be in the 15 to 35 percent range for stand-alone Employment Practices Liability insurance. For small- to medium-size and privately held and nonprofit companies that purchase their EPL coverage in combination with D&O, rate increases are expected to be more moderate: flat to 15 percent.

Significant class action developments in 2003 will likely result in continued increases in retentions and some possible tightening of terms in 2004.

## Cyber Risk/Professional Liability

2003 has the dubious honor of being the worst year on record for computer viruses. Not surprisingly – as most of those who renewed their Property and General Liability policies over the past two years know only too well – exclusions for cyber risks are becoming more common. Most companies increasingly rely on computer networks to establish or maintain interconnectivity with clients and business partners (it's how we usually deliver copies of this Newsletter to you). These exposures must be addressed.

The good news is that while the breadth of coverage varies considerably, premium increases in 2004 are expected to average in the 10 to 25 percent range. Capacity is rarely a concern, as nearly a dozen companies are now potentially available to write first- and/or third-party cyber coverage.



## SPOTLIGHT ON: EPL and Workplace Violence

Written by Steven Dranoff, PhD and Wanda Dobrich, PhD,  
D&D Industrial Consulting, Inc.



No employer would knowingly leave flammable materials in an unprotected area, yet when it comes to workplace hostility and aggression, employees are frequently exposed to uncontrolled risk. The chief reason is clear enough. Oily rags or drums of toxins are visible to surface inspection; human risk factors are not. Situations that fuel hostile exchanges that end in bullying, harassment or violence are often not apparent even to the employees themselves involved until it's too late. These factors may be invisible to the risk managers, human resources personnel or others in the company who are responsible for monitoring the work climate and overseeing employee safety.

## Hidden Risk Factors

The failure to prevent workplace aggression is usually **not** due to inadequate policies and risk management practices. The problem lies in human error: when hidden risk factors are ignored and employees fail to use the protections that are in place, individuals suffer. So do companies. Ultimately, hidden risk factors are responsible for increased exposure to litigation and financial loss and to secondary exposures such as negative work climate, employee attrition and reduced worker productivity.

A host of hidden risk factors influencing workplace aggression has long been identified, but until now this information has not been available to employers to use in a systematic way to promote employee safety. For example, we know that:

- Victims typically fail to use their employer's procedural protections, despite training and education.
- Harassers almost never perceive their behavior as harassment.
- Women and men perceive different sets of behaviors as harassment.

- Men sexually harass other men more frequently than they do women, though it is reported significantly less frequently.
- The majority of workers perceive retaliation as a likely consequence of coming forward, regardless of prohibitions against retaliation.
- Jurors make decisions based on the interactions between harasser and victim, not on the harassment acts themselves.

## Getting Ahead of the Curve: Primary Prevention

In the best case scenario, primary prevention tools inhibit harassing or hostile employee behavior before it occurs. Organizational assessment is one tool that systematically, comprehensively and scientifically identifies hidden risk factors in a company. Using quantitative data, an employer can compare its risk profile to normative expectancy and make necessary corrections to prevent worker harassment and aggression.

Training that targets hidden risk factors is another effective tool for reducing employer risk. When employees are given feedback about their perceptions of harassment and hostility in their work environment, they can modify their behavior to be in better alignment with organizational standards. Like basic training in the military, companies can prepare employees. They can offer the skills to avoid harassment or deter its negative impact, if exposed.

## Secondary Intervention: Mopping up the Mess

Despite an employer's best effort, problems with aggression still erupt between workers. Even the employer who takes every "reasonable care" to prevent harassment is not immune to an occasional incident of workplace aggression, harassment or hostility. In this instance, effective risk management intervention is geared to limiting the negative impact of the event. Services such as organizational recovery or harasser assessment reduce the risk of further damage to the employer or employees in the aftermath.

Just as the best prevention practices do not guarantee that all cases of workplace aggression will be eliminated, neither do they preclude an aggrieved employee from litigating. Risk management must address the legal environment. Forensic assessment of the accuser, accused and/or the organization is sometimes needed to build a sound legal defense. Incorporating data on hidden risk factors assists judges and juries in reaching conclusions based on scientific evidence, rather than subjective standards.

## In the Beginning: Your Permanent Record

It is clear that society could benefit if we addressed interpersonal risks in the schools before students enter the adult workforce. As they do in the workplace, hidden risk factors influence students and teachers in their perceptions of bullying, harassment and violence. This is an area of growing concern to school administrators and risk managers. Interpersonal conflicts between students that were once treated as discipline problems are now coming to the attention of legal authorities and even the courts. As we have come to know only too well, the schools themselves can be held liable in some of these outbreaks of peer aggression.

## Tools for Success: Inoculating the Organization

Willis clients now have access to a unique set of prevention tools that reduce exposures all along the risk continuum.

- 1. Compliance Readiness Assessment:** Quantifies the organization's hidden risk factors. A complement to traditional auditing of risk management practices.
- 2. Prevention Training:** Quantifies the employees' hidden risk factors. An internet program that helps employees learn about their personal risk factors, where their perceptions are in misalignment with the company's anti-harassment policy.
- 3. Quick Response Harasser Recovery Program:** Quantifies the accused harassers' hidden risk factors. Individualized assessment and training program to support re-integration.
- 4. Litigation Support:** Quantifies hidden risk factors of litigants. Forensic assessment for legal defense in cases of workplace harassment and aggression.
- 5. School Intervention:** Quantifies hidden risk factors for peer aggression. Curriculum in bullying, harassment and violence prevention for adolescents in grades 6-12.



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## About D&D Industrial Consultants, Inc.

Steven Dranoff, PhD and Wanda Dobrich, PhD are the principals of D&D Industrial Consultants. They are organizational and forensic psychologists, and are on the faculty of the Rutgers University Graduate School of Applied and Professional Psychology. They are co-producers with Rutgers University of a unique interactive internet training program on sexual harassment prevention for corporations worldwide ([esh.rutgers.edu](http://esh.rutgers.edu)). They are also authors and producers of RESPECT, a program for middle and high school adolescents on bullying, sexual harassment and violence prevention. RESPECT is used in major school districts across the United States.

Dranoff and Dobrich are authors of *The First Line of Defense: A Guide to Protecting Yourself Against Sexual Harassment* (John Wiley & Sons); and with Gerald Maatman, Esq., *The Manager's Guide to Preventing a Hostile Work Environment: How to Avoid Legal and Financial Risks by Protecting Your Workplace from Harassment Based on Sex, Race, Disability, Religion or Age* (McGraw-Hill). Both books have received the Book of the Year Award from Willis.