



JAMES K. RUBLE SEMINAR

Ruble Graduate Seminar

Pennsylvania

March 11-12, 2025

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A Letter from William J. Hold, President/CEO

We know that choosing the right professional development programs to strengthen your career can be challenging. There are many options for you to choose from; so how can you be sure that your time, efforts, and money are being invested and not wasted?

By becoming a committed participant of The Alliance, you can rest assured that you are also making the best educational choice for your career—no matter what step of your learning path you are on.

For the last 50 years, our designations have been regarded throughout the industry as symbols of quality and trust. Our practical courses are taught by active insurance and risk management practitioners, include policies and forms currently used in the field, and guide you through real-world scenarios to give you a deeper understanding of what your clients are facing today. The knowledge and skills you develop in any one of our courses (or designation programs) can be put to use immediately.

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Have no doubt that your success is our priority. Whether you are new to your career, or a seasoned professional, you are about to embark on a wonderful professional development journey. Thank you for choosing the Risk & Insurance Education Alliance as your guide toward a thriving career.

Let's take the first step.

A handwritten signature in black ink that reads 'William J. Hold'. The signature is written in a cursive style and is positioned above a horizontal line.

William J. Hold, M.B.A., CRM, CISR
President/CEO



James K. Ruble Seminar

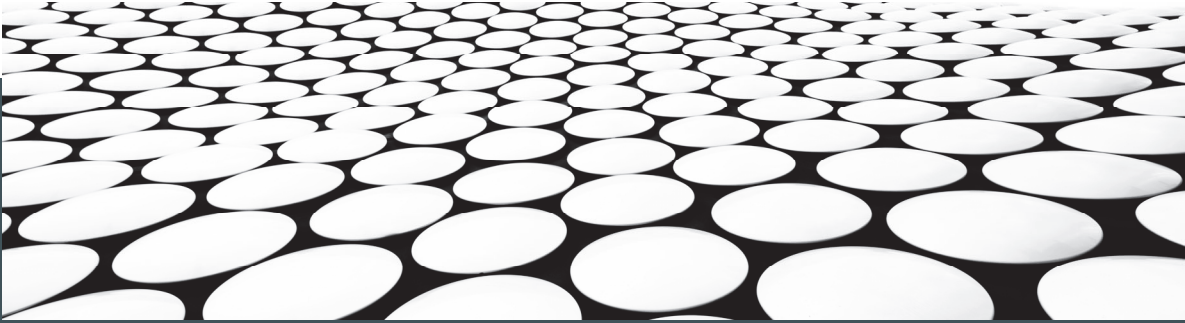
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Section 1

Commercial Insurance Issues That Cause Heartburn



COMMERCIAL INSURANCE ISSUES THAT CAUSE HEARTBURN



TERRY L. TADLOCK, CIC, CPCU, CRIS
CORRELL INSURANCE GROUP
HILTON HEAD ISLAND, SC

1

THE IMPACT OF A HARD MARKET

2

WHEN A HARDENING MARKET BECOMES HARD

By now, everyone has likely noticed the cost of property insurance is increasing at an alarming rate. Unfortunately, these increases are expected to continue through 2024. Although this has happened in the past, it is never welcomed. The following information is designed to explain what is driving the pricing of insurance rates in our industry and let you know what to expect as we move forward together.

3

HURRICANE IAN'S IMPACT

Over the past 6 years we have had an unusually high number of catastrophic losses. Hurricanes Matthew, Irma, Michael and Dorian as well as non-tropical disasters like wildfires in California have an impact on insurance premiums, but none will have the impact of Ian. Hurricane Ian is predicted to be one of the costliest catastrophes in US history. Predictions are between 75 and 100 billion dollars.

INFLATION FACTOR

With inflation at a 40+ year high it will increase the reconstruction cost of hurricane Ian and ultimately your insurance premiums. The cost of materials and labor are rising, as well as major issues we are experiencing with our supply chain. These factors have a direct impact on the cost of insurance.

4

THE COST AND AVAILABILITY OF REINSURANCE

Insurance Companies also buy insurance to protect them when devastating losses take place like Hurricane Ian. As losses continue to rise and the reinsurance market continues to contribute to claims, fewer investors are wanting to invest in this industry. We have seen shrinkage the past two years and are expecting another large reduction this year. With less reinsurance available the cost is increasing which directly effects the rates carrier charge the consumer. This may have the single largest impact we see on pricing and insurer solvency.

5

INSURANCE COMPANY VOLATILITY

We have seen over 20 insurance companies go insolvent or pull out of the market. This is generally due to underfunding and the increase in their price of reinsurance. As such, it has put a great deal of stress on the markets that remain to absorb that business. We want to assure you that we endeavor to place insurance with stable insurance carriers.

6

A FEW ISSUES TO CONSIDER

PROACTIVE EDUCATION

You may want to be proactive in providing education as to why this market shift is happening and what it means for your clients. Bad news in some cases is better than being surprised at renewal.

BEWARE OF SCAMS

When premiums are increasing at 25% to 50% there will be companies offering lower prices than the industry. It will be appealing to place business with them. Beware as coverage may be lower, carrier strength may be sacrificed or even intentional misquoting to secure the business, knowing the error will be caught and the premium changed at inspection.

7

WHAT DOES THE FUTURE HOLD

1. Pricing will increase through 2024. Expect increases of 10 to 25% or higher depending on rating factors such as age of home, distance to coast and upgrades to roofing, plumbing and electrical.
2. Fewer carriers will be available to choose from after the 1st quarter of 2024.
3. Consider re-marketing accounts with other carriers before your renewal to make sure you are providing the service your clients will expect.

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INSURANCE TO VALUE FACTS AND FOLLIES

9

FACT #1 – YOUR BUILDING IS UNDERINSURED!

One of your current clients have purchased a new location. They felt it was a bit overpriced, but the market being a little high they decided to purchase the building anyway as it is a perfect location. The purchase price was \$2,500,000 and they put down \$500,000 and have a mortgage of \$2,000,000.

During the purchase process the building appraisal came back at \$2,300,000 which made your insured feel much better about their new purchase. They have contacted you to insure their building. The building is joisted masonry and was built in 1992. The building has 8,000 square feet for their retail operation and they rent 5,000 square feet to another tenant.

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FACT #1 – YOUR BUILDING IS UNDERINSURED!

Your client feels their building needs to be insured for somewhere between \$2,000,000 (which is the mortgage amount) and \$2,200,000 due to the value of the ½ acre lot it sits on. He has quotes from another agency (the sellers agent) for \$2,000,000, which he was assured was adequate, but your agency has always done a good job and they want to get your thoughts and price as well.

Thoughts about Market Value, Appraised Value, Replacement Cost??? What is the right number?

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FACT #1 – YOUR BUILDING IS UNDERINSURED!

You convince your client the higher number is closer and they choose to insure the building for \$2,200,000 and feel this is an adequate amount. You provide a quote and the client binds the coverage. Now for the BAD news!

7 Months after moving into their new building it is struck by lightning in a terrible thunderstorm and a fire ensued. The business was closed at the time but neighboring properties see the blaze and call the fire department. The clients first call was to you, their agent. Assuring them everything would be fine you report the claim to the carrier and an adjuster was assigned.

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FACT #1 – YOUR BUILDING IS UNDERINSURED!

It looks like the building is going to be almost a total loss if not a complete total loss. The following is an estimate of the repairs that will have to be made.

1. Demolition and site clearing - \$156,000 (Tear down and removal/dumping)
2. Loss adjustment fees - \$48,000 (Independent adjuster cost)
3. Professional fees - \$27,000 (Architects and engineers)
4. Building Permits - \$18,000 (local permits and fees)
5. Reconstruction Cost - \$2,925,000 (Cost of Labor and Materials @225 per square foot)

Total Expense to reconstruct - \$3,174,000. I sure hope you have no ordinance or law issues.

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FOLLY #1 – COST TO BUILD V. RE-BUILD!

It ALWAYS takes more money to rebuild after a loss than it took to build the original building.

I recognize that consumers are cost conscience, and they should be, but don't they deserve to be told the truth?

What happens in an existing economic condition when building materials and labor are skyrocketing. You can't always have your loss at the most convenient time.

Solutions:

Appraisals

Inflation Guards

Square footage analysis

Let the client choose, but give them the facts! If not, an E&O claim may be in your future!

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FOLLY #2 – THE COINSURANCE EFFECT

At the time of the loss (not when the building is insured) it must be insured to a percentage of value or a penalty may be imposed at claim time.

1. Coinsurance

If a Coinsurance percentage is shown in the Declarations, the following condition applies:

- a. We will not pay the full amount of any loss if the value of Covered Property at the time of loss times the Coinsurance percentage shown for it in the Declarations is greater than the Limit of Insurance for the property.

You know the formula as: $DID/SHOULD \times LOSS - DEDUCTIBLE = RECOVERY$

So how would your clients loss be calculated assuming a 90% coinsurance percentage?

$$2,200,000/2,856,600 = .770 \times 3,174,000 = 2,443,980 - 5,000 = 2,438,980$$

Since you only carried 2,200,000 this is all you will be paid. All partial losses under the policy limit would be paid at .770%. (23% reduction)

What will this mean at loss time? 974,000 penalty, Ouch!

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FOLLY #3 – VALUATION OF ROOF SURFACES!

Many companies today will put valuation limitation on roof surfacing once the roof has reached a certain age. For example, if the roof is over 20 years old a company may choose to convert the policy valuation from Replacement Cost (RC) to Actual Cash Value (ACV). What would this mean at claim time?

RC (generally referred to as new for old) will put a new roof on the old home less the deductible.

ACV will subtract the amount of depreciation from the cost of the new roof.

Assume a roof cost of \$125,000. Policy had a \$5,000 deductible.

$$RC = \$125,000 - \$5,000 = \$120,000$$

$$ACV = \$125,000 - \$83,375 - \$5,000 = \$36,250$$

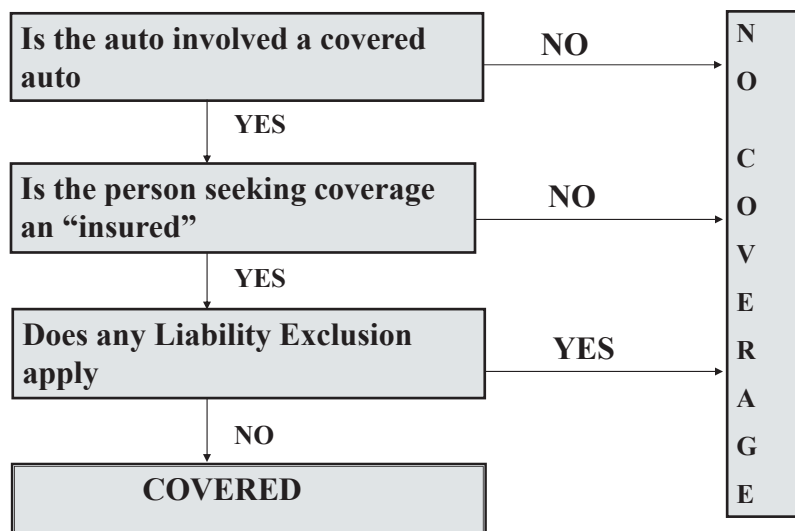
(roof was 20 years old and had a life expectancy of 30 years)

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BUSINESS AUTO – SYMBOLS 2, 8 & 9 DON'T EQUAL 1

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HOW TO DETERMINE COVERAGE



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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

Materials, Inc. is a large concrete company in your city. They have purchased their commercial package through your agency including Business Auto coverage. Liability coverage is written with symbols 2, 8, and 9.

Materials, Inc. has contracted (written agreement) with a local hauling company to assist with a big job. The hauler, while making a delivery on behalf of Materials, Inc. was involved in an at-fault accident killing one passenger and critically injuring another. The estate of the deceased as well as the injured passenger filed suit against Materials, Inc.

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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

SECTION II – LIABILITY COVERAGE

A. Coverage

We will pay all sums an "insured" legally must pay as damages because of "bodily injury" or "property damage" to which this insurance applies, caused by an "accident" and resulting from the ownership, maintenance or use of a covered "auto".

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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

- 2 Owned "Autos" Only
Only those "autos" you own (and for Liability Coverage any "trailers" you don't own while attached to power units you own). This includes those "autos" you acquire ownership of after the policy begins.
- 8 Hired "Autos" Only
Only those "autos" you lease, hire, rent or borrow. This does not include any "auto" you lease, hire, rent, or borrow from any of your "employees", partners (if you are a partnership), members (if you are a limited liability company) or members of their households.
- 9 Nonowned "Autos" Only
Only those "autos" you do not own, lease, hire, rent or borrow that are used in connection with your business. This includes "autos" owned by your "employees", partners (if you are a partnership), members (if you are a limited liability company), or members of their households but only while used in your business or your personal affairs.

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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

- 1. Who Is An Insured
The following are "insureds":
 - a. You for any covered "auto".
 - b. Anyone else while using with your permission a covered "auto" you own, hire or borrow except:
 - (1) The owner or anyone else from whom you hire or borrow a covered "auto". This exception does not apply if the covered "auto" is a "trailer" connected to a covered "auto" you own.
 - (2) Your "employee" if the covered "auto" is owned by that "employee" or a member of his or her household.

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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

- b. Anyone else while using with your permission a covered "auto" you own, hire or borrow except:
- (3) Someone using a covered "auto" while he or she is working in a business of selling, servicing, repairing, parking or storing "autos" unless that business is yours.
 - (4) Anyone other than your "employees", partners (if you are a partnership), members (if you are a limited liability company) or a lessee or borrower or any of their "employees", while moving property to or from a covered "auto".
 - (5) A partner (if you are a partnership) or a member (if you are a limited liability company) for a covered "auto" owned by him or her or a member of his or her household.

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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

Question 1 - Is the vehicle driven by the hauler that caused the accident a “Hired Auto” under Materials, Inc. BAP?

Question 2 - Do you agree the hauler maintained the truck and provided gas and oil. The hauling company paid the driver. Materials did not dictate the route or maintain any control over the driver,

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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

Question 3 - Should Materials, Inc. BAP provide a defense and respond to this claim?

Question 4 - Would your answer concerning this claim change if the policy was written with Symbol 1?

1 Any “Auto”

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“SYMBOLS 2, 8 AND 9 DON’T EQUAL SYMBOL 1”

Question 5 - Do you think this is a common occurrence with business owners today?

Question 6 - How would the retail agent or company know about this exposure?

Question 7 - Can you think of a solution to this problem?

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WHY DOC IS BAD ☹️

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WHY DOC IS BAD ☹️

Bruce Lansing is the owner of Lansing Glass Company, which is a large regional glass installation and cleaning company that your agency insures. Bruce is a very detailed business person and is very thorough before he makes a business decision. He has called your office with the following information:

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WHY DOC IS BAD ☹️

Bruce has been advised by his accountant and his attorney to title his personally owned vehicles in the name of the business and allow the business to pay for all expenses associated. Bruce is concerned that his insurance may not adequately protect him. He currently has a Business Auto policy (Symbol 1 – Liability) for his office, which owns three other vehicles. He also has a Personal Auto policy covering the three vehicles he is considering moving to his BAP. He has been advised by his accountant and his attorney that this is a very common occurrence and that his insurance agency should be able to handle this request with no problems. The attorney even explains to him that this is the way he handles his insurance.

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WHY DOC IS BAD ☹️

Questions you may want to ask:

Who in your agency would handle a request of this nature?

Could he title the vehicles in his businesses name but insure them under a PAP?

If he decides to move his personally owned vehicles to the businesses BAP, what would need to be done?

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WHY DOC IS BAD ☹️

Questions you may want to ask:

What impact, if any, would this have on his Personal Umbrella policy?

What advice, if any, would you give him before making this change?

Let's take a look at a few endorsements that you may want to consider.

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WHY DOC IS BAD ☹️

CA 99 17 Individual Named Insured

CA 99 10 Drive Other Car Broadened Coverage For Named Individuals

PP 03 06 Extended Non-Owned Coverage – Vehicles Furnished Or Available For Regular Use

Will any of these endorsements help?

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PARTS ARE PARTS WHAT DOES “THAT PARTICULAR PART” MEAN

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THAT PARTICULAR PART, WHAT DOES IT MEAN?

A general contractor was hired to repair water damage to a floor. Due to the small size of the job he hired one of his sub contractors to do the work. During the installation the subcontractor put tape on the floor to hold the seams together until the glue dried. The subcontractor did not read the installation instructions which specifically said not to apply any adhesive tape to the flooring. When the subcontractor took the tape off of the flooring it damaged every piece of flooring it touched.

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THAT PARTICULAR PART, WHAT DOES IT MEAN?

The customer obviously wanted the general contractor to pay for the damage, but he told the homeowner that he did not do the work. They would have to file a claim against the subcontractor that actually installed the floors. When the claim was filed the insurance company argued that damage to the flooring was within the scope of work being done and thus constituted the particular part of the real property they were working directly on.

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THAT PARTICULAR PART, WHAT DOES IT MEAN?

The following policy language was cited.

2. Exclusions

This insurance does not apply to:

j. Damage To Property

"Property damage" to:

- (5)** That particular part of real property on which you or any contractors or subcontractors working directly or indirectly on your behalf are performing operations, if the "property damage" arises out of those operations

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THAT PARTICULAR PART, WHAT DOES IT MEAN?

Questions To Consider:

Where do you draw the line on “that particular part”?

What is the intent of the exclusion?

And the court said...

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**TO SERVE OR NOT TO SERVE...
THAT IS THE QUESTION**

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LIQUOR LIABILITY – TO SERVE OR NOT TO SERVE THAT IS THE QUESTION

The insured is a local non-profit organization that raises money for many local charities. In addition they have many social functions at their facility they serve dinner every Friday night and have a cash bar. After being over-served a guest of a member falls down stairs resulting in a serious injury. A suit is filed.

The insurance company issues a ROR letter and investigates the claim. After their investigation they issue a formal denial and site the liquor liability claim. The insured looks to their agent for an explanation.

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LIQUOR LIABILITY – TO SERVE OR NOT TO SERVE THAT IS THE QUESTION

2. Exclusions

This insurance does not apply to:

c. Liquor Liability

"Bodily injury" or "property damage" for which any insured may be held liable by reason of:

- (1) Causing or contributing to the intoxication of any person;
- (2) The furnishing of alcoholic beverages to a person under the legal drinking age or under the influence of alcohol; or
- (3) Any statute, ordinance or regulation relating to the sale, gift, distribution or use of alcoholic beverages.

This exclusion applies only if you are in the business of manufacturing, distributing, selling, serving or furnishing alcoholic beverages.

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LIQUOR LIABILITY – TO SERVE OR NOT TO SERVE THAT IS THE QUESTION

Questions to consider:

What is meant by the Term “in the business of”?

How are courts ruling on this issue?

How do we prevent being the victim?

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**BUT IT IS NOT ON MY TRUCK, IT
MUST BE UNLOADED**

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LOADED OR UNLOADED?

The insured trucking company was hired to deliver truckloads of rock and sand to a road construction site to be used as road base material. A paving contractor was responsible for spreading and leveling the base material after delivery. An employee of the insured dumped a truckload of the base material at the job site and left. An employee of the paving contractor driving a car on the job site collided with the pile of base material and was injured. No trucks or employees belonging to the insured trucking company were present at the job site at the time of the accident. The injured driver sued the insured trucking company.

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LOADED OR UNLOADED?

The trucking company's BAP and CGL insurers disagreed as to which policy covered the loss. The CGL insurer argued that this was an auto loss, because the base material had not yet been spread out and leveled. So the "unloading" of the truck was not complete at the time of the accident. The BAP insurer argued that this was a GL loss, because the "unloading" of the truck was complete when the driver dumped the load at the work site. Special rules have been developed to handle claims happening during the course of loading or unloading a vehicle, a gray area where auto and general liability exposures can sometimes overlap. The basic theory is that the BAP should cover exposures during loading and unloading operations, and that the CGL should cover exposures before loading begins and after unloading is complete.

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LOADED OR UNLOADED?

QUESTIONS:

1. When does loading begin and unloading end?
2. Since the insured is no longer at the premises where the material is unloaded should this be CGL?

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COURT RULING

Here, "the base that the driver delivered and dumped the morning of the collision ... reached its final destination when it was completely unloaded at the road construction site. At this stage of the project, the paving subcontractor was responsible for leveling and smoothing out the base." Because it was not part of the insured trucking company's operation to spread and level the base material, "the BAP did not provide coverage for the other driver's injuries because the base had been completely unloaded and delivered to its final destination."

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MORE LOADING AND UNLOADING

The claim arose when a restaurant employee suffered injuries from a fall that resulted when she was carrying a sack of potatoes. The potatoes had been put in the wrong place when they were delivered to the restaurant. According to the appellate court, the food supplier's motor vehicle liability policy and not its general liability policy provided coverage because the delivery was not completed until the sack was placed in the proper location.

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MORE LOADING AND UNLOADING

The insured driver delivered two sacks of potatoes, each weighing 100 pounds, and deposited both sacks inside the doorway entrance of a walk-in storage cooler. He departed from the restaurant immediately after obtaining a signature on a receipt form. The head cook of the restaurant (who was responsible for taking deliveries) was unaware that the delivery had taken place.

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MORE LOADING AND UNLOADING

When the head cook discovered the two sacks blocking entrance to the storage cooler later that morning, she tried to drag them away from the door to where they were ordinarily kept. As she picked up the second sack, she slipped and fell, injuring herself.

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MORE LOADING AND UNLOADING

To ascertain whether an act constitutes "loading or unloading," courts have adopted two basic tests: the "coming to rest" doctrine, under which "unloading" includes only the actual removing or lifting of the article from the motor vehicle up to the moment when it has actually come to rest, and the "complete operations" doctrine, which holds that "unloading" encompasses all of the operations required to effect a complete delivery. The "complete operations" doctrine, therefore, covers the entire process involved in moving the goods, while coverage under the "coming to rest" doctrine terminates when the deliveryman has finished his handling of the goods.

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MORE LOADING AND UNLOADING

QUESTION:

1. What does “finally delivered” in the exclusion really mean?

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COURT RULING

In this particular case, the deliverymen had been instructed where to place the potatoes. Therefore, following the complete operations doctrine, this delivery was incomplete. The deliverer must have finished his handling of the material and, second, it must have been placed in the hands of the receiver at the designated reception point. In this case, only the first element of the test was satisfied.

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BUT I THOUGHT THIS IS WHAT CYBER COVERAGE WAS DESIGNED TO COVER

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IS IT A CYBER HOAX?

A large materials dealer was curious when notified by one of their largest vendors that they were changing bank accounts. Since the insured processes many wire transfers to this vendor they wanted to make sure everything was above board. They called the vendor and it was confirmed. They were changing banks because they were hacked. During the call the client verified the wire transfer amounts that were due. Later that day, the insured received an email from the vendor with account numbers and wiring instructions as they had discussed.

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IS IT A CYBER HOAX?

I think you know what is coming... The insureds email system had been hacked and the “bad actor” was lying in wait. The email received was fraudulent and the insured wired the money to the wrong account. There were several invoices that matched the information that was received earlier in the day. The insured wired the money thinking all was good. Another email arrived requesting another bank change. The insured got suspicious and called the vendor again and was given the bad news the account numbers don’t match. After calling the bank, the next call was to the agent!

Let’s look at the policy language.

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IS IT A CYBER HOAX?

SECTION I . INSURING AGREEMENTS

Coverage is provided under the following insuring agreements for which limits of liability are shown in the Declarations:

9. Fraudulent Instruction

We will indemnify the "named insured" for loss, in excess of the applicable retention, resulting directly from an insured having transferred, paid, or delivered any "money" or "securities" as a direct result of "fraudulent instructions", provided such loss is first discovered by the insured and reported in writing to us during the "policy period" or as otherwise provided in SECTION VIII – NOTICE AND DUTIES IN THE EVENT OF A CLAIM, LOSS OR CIRCUMSTANCE THAT MIGHT LEAD TO A CLAIM and occurs on or after the retroactive date and before the end of the "policy period".

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IS IT A CYBER HOAX?

25. "Fraudulent Instructions" means a fraudulent written instruction, electronic instruction (including email or web-based instruction) or telephone instruction provided by a person purporting to be a "vendor", "client", or an "authorized employee", that is intended to mislead an Insured through the misrepresentation of a material fact that is relied upon in good faith by such Insured.

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IS IT A CYBER HOAX?

To your surprise you get a call from the adjuster informing you that the carrier is going to deny the claim. They identify an exclusion that you were not aware that existed.

25. With respect to **SECTION I — INSURING AGREEMENTS, 9. Fraudulent Instruction**, for, arising out of or resulting from, either directly or indirectly:

D. any "fraudulent instruction" that was not verified with the requestor using an "out-of-band authentication";

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IS IT A CYBER HOAX?

Your next question is... What in the world is an “out-of-band authentication?”
I’m glad you asked.

40. "Out-of-Band Authentication" means a method of challenge and response to the requestor of a transfer, payment or delivery of "money" or "securities" by an Insured, via a method other than the original means of request, to verify the authenticity or validity of the request.

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IS IT A CYBER HOAX?

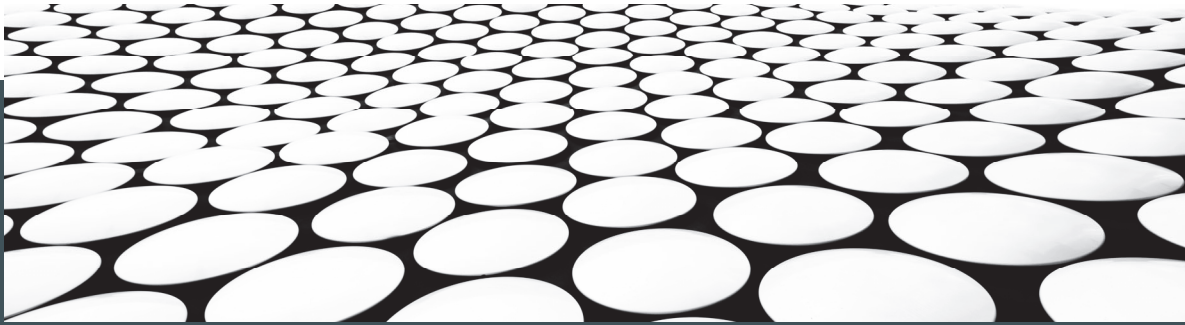
The carrier is standing firm on their denial because the insured did not verify or challenge the information in the email AFTER it was received?

How do you rule?

And the Court said.....

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COMMERCIAL INSURANCE ISSUES THAT CAUSE HEARTBURN



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James K. Ruble Seminar

a proud member of Risk & Insurance Education Alliance

Section 2

Insurance and the Property Lease



INSURANCE AND THE PROPERTY LEASE

Written and presented by:

Terry L. Tadlock, CIC, CPCU, CRIS

INSURANCE AND THE PROPERTY LEASE

LEARNING OBJECTIVES:

1. Identify provisions found in leases of real property that may impact how property insurance should be written.
2. Discuss when and under what conditions subrogation may be waived in the Commercial Property Coverage Forms.
3. Review the impact of a “Mutual Waiver of Subrogation” clause found in property leases.
4. Discuss the coverage provided in the Legal Liability Coverage Form.
5. Identify how “Tenants Improvements and Betterments” should be written and how losses will be valued at the time of a loss.
6. Briefly look at the Leasehold Interest Coverage Form and discuss how it may fix some problems associated when a lease is terminated.
7. Identify how to insure and value personal property that is leased by your insureds.
8. Review other miscellaneous leases such as contractor’s equipment, automobiles and apartments for kids away at college.

Situation #1 - The Real Property Lease:

Bubba's Sporting Emporium is renting space in a local strip center that is owned by Strip Centers, Inc. Bubba has signed a ten (10) year lease at a reduced rate because Bubba is making improvements to the building valued at \$250,000. Bubba (like many of our clients) was so pleased to get this prime location that he signed the lease without reading the fine print. You have written Bubba's insurance on a Building and Personal Property Coverage Form covering his personal property in the amount of \$1,000,000.

Question #1 – Four years into the lease the roof collapses in the strip center and damages \$200,000 of Bubba's personal property. The damage to the roof is \$50,000. Your lease states:

Insurance: Lessor shall pay property insurance premiums on the leased premises including the personal property in a sufficient manner to cover the entire property. Lessee will provide insurance on any personal property that the Lessee moves to the leased premises.

Maintenance: The renter shall during the term of the lease keep and maintain the property in good working condition and repair and shall be responsible for any loss, casualty, damage or destruction to said property notwithstanding how caused and Renter agrees to return said property in its present condition, reasonable wear and tear excepted.

The Insurance Company for Strip Centers, Inc. pays for the damage to the structure and Bubba's insurance company replaces the \$200,000 of damaged personal property. Life is good! Four (4) months later Bubba receives a letter from Strip Centers, Inc. Insurance Company stating: "It has come to our attention that the damage to the roof of Strip Centers, Inc. was due to a water back-up on the flat roof. Our structural engineer has indicated that the collapse was a result of the gutters not being cleaned out in four (4) years. Please find enclosed a bill in the amount of \$50,000. Please pay at your earliest convenience." Bubba's next call is to you, his agent. What is your response?

Question #2 – Strip Centers, Inc. writes a letter after the claim waiving the rights to subrogate against Bubba for the \$50,000. Is this allowed? How do you think the company will respond?

Question #3 – If the following language known as a “mutual waiver of subrogation” was in the lease would it have had an impact on the above mentioned loss?

Lessee shall provide Lessor with a Certificate of Insurance showing Lessor as additional insured. The Certificate shall provide for a ten-day written notice to Lessor in the event of cancellation or material change of coverage. To the maximum extent permitted by insurance policies which may be owned by Lessor or Lessee, for the benefit of each other, waive any and all rights of subrogation which might otherwise exist.

Question #4 – In the absence of a “mutual waiver of subrogation,” is there any Insurance policy we can recommend to Bubba that will cover damage to property of others in an insureds care, custody or control?

Question #5 - After the loss Strip Centers, Inc. sends Bubba a letter asking him to file a claim for the \$50,000 damage to the roof with his insurance company because the lease requires the tenant (Bubba’s Sporting Emporium) to provide insurance on the real property leased for the benefit of Strip Centers, Inc. Does this happen? If so how should this insurance be written?

Lessee shall provide property insurance on the leased premises including the real and personal property in a sufficient manner to cover the entire property for the interest of Strip Centers, Inc. Lessee will also provide insurance on any personal property that the Lessee moves to the leased premises.

Situation #2 – How the Lease Impacts Tenants Improvements and Betterments:

Bubba has installed at his own expense \$250,000 of improvements and betterments that were needed in the strip center to make his business functional. The improvements are a permanent part of the building and cannot be removed at the termination of the lease. Bubba certainly wants his investment protected for the duration of the lease.

Question #1 – What is a Tenant Improvement and Betterment? Who has the right and/or responsibility to insure them? Can the lease affect this issue?

An Endorsement that may help with cost!

Your Business Personal Property - Separation of Coverage - CP 19 10 used to write separate values on business personal property items. If TIB are separated from other personal property items, they are rated as building. Use with caution since this subdivides coverages. When BPP is written with a single limit, the highest rate is used. Property listed here is not part of the Business Personal Property limit on the declarations.

Question #2 – Fire totally destroys the building and Strip Centers, Inc. notifies Bubba’s Sporting Emporium that they plan to rebuild as soon as possible. How will Bubba’s Building and Personal Property Coverage Form respond for his use interest in Tenants Improvements and Betterments?

Question #3 - Fire totally destroys the building and Strip Centers, Inc. notifies Bubba’s Sporting Emporium that they do not plan to rebuild. Strip Centers, Inc. is selling the land. Does Bubba have any recovery for his Tenants Improvements and Betterments?

Question #4 - Fire totally destroys the building and Strip Centers, Inc. notifies Bubba’s Sporting Emporium that they plan to rebuild. Strip Centers, Inc. has filed the claim with their insurance company for payment. How will Bubba’s policy respond for the Tenants Improvements and Betterments?

The following is a quick overview of the coverage under the Commercial Property Coverage Forms.

DAMAGE TO TENANTS IMPROVEMENTS AND BETTERTMENTS	VALUE FOR PAYMENT UNDER TENANT'S CPP
Tenant repairs	ACV (RC if option is activated)
Landlord repairs	Nothing paid
Cannot repair or rebuild	Proportional on original cost

Situation #2 Cont. - Fire destroys one-half of the strip center owned by Strip Centers, Inc. where Bubbas is a tenant. However, Bubba's Sporting Emporium has not suffered any loss. The lease states:

13. Destruction of Premises: In the event of a partial destruction of the premises during the term hereof, from any cause, Lessor shall forthwith repair the same, provided that such repairs can be made within sixty (60) days under existing governmental laws and regulations, but such partial destruction shall not terminate this lease, except that Lessee shall be entitled to a proportionate reduction of rent while such repairs are being made, based upon the extent to which the making of such repairs shall interfere with the business of Lessee on the premises.

...in the event that Lessor shall not elect to make such repairs which cannot be made within sixty (60) days, this lease may be terminated at the option of either party. In the event that the building in which the demised premises may be situated is destroyed to an extent of not less than one-third of the replacement costs thereof, Lessor may elect to terminate this lease whether the demised premises be injured or not. A total destruction of the building in which the premises may be situated shall terminate this lease.

Bubba's property has not been damaged at all. Strip Centers, Inc. has mailed him official written notice of their intention to terminate his lease. How will Bubba's policy respond to the following questions?

Question #5 - Is Bubba entitled to relief of rent payment while repairs are being made? Bubba is concerned that even if he can have access to his store the construction and lack of walk by traffic will reduce his sales.

Question #6 - Bubba is concerned that repairs will take at least 12 months. Can Bubba terminate his lease (based on lease language above)? If so, how will Bubba be compensated for his loss of use interest in his tenant's improvements and betterments?

Question #7 - Bubba is having a disagreement with Strip Centers, Inc over last year's tax and maintenance assessment. Bubba's lease states:

14. Lessor's Remedies on Default: If the Lessee defaults in the performance of any of the other covenants or conditions hereof, Lessor may give Lessee notice of such default and if the Lessee does not cure any such default within 60 days, then the lessor may terminate this lease on not less than 60 days' notice to Lessee.

Bubba is made aware that if he fails to pay the assessment that his lease will be terminated in 60 days. Bubba continues to refuse and formal written notice of termination is issued. What will happen to Bubba's use interest in his tenants and improvements and betterments?

Let's go to the numbers...

ASSUME: Year 1 of policy.

Present rent of \$10.00 per square foot each year on 7,500 square feet. Cost to relocate in a satisfactory location would result in a rental value of \$16.00 per square foot each year. There are 57 months remaining on lease as of the effective date of policy. The insured spent \$90,000 on Tenants Improvements and Betterments at the inception of the lease. Original lease 10 years.

Policy limit will be present value of gross leasehold interest plus unamortized value of the TIB.

$$\begin{array}{rcl} 7,500 & \times & \$10 = \$75,000 \text{ per year} & \$6,250 \text{ per month} \\ 7,500 & \times & \$16 = \$120,000 \text{ per year} & \$10,000 \text{ per month} \end{array}$$

The gross leasehold interest is \$3,750 (\$10,000-\$6250).

Assuming a present value of money at 6% the gross leasehold interest is:

$$\mathbf{\$3750} \quad \times \quad \mathbf{49.6711 \text{ (PVAF 6\% @57 months)}} \quad = \mathbf{\$186,267}$$

Now let's look at the Tenants Improvements and Betterments...

$$\mathbf{\$90,000} \quad \times \quad \mathbf{57/120} \quad = \mathbf{\$42,750 \text{ unamortized interest in TIB's.}}$$

$$\mathbf{\$186,267 \text{ (interest in lease)} + \$42,750 \text{ (interest in TIB's)}} \quad = \mathbf{\$229,017.}$$

Now let's look at how to arrive at the correct premium...

Net leasehold interest for the policy year:

$$\begin{array}{rcl} \$3750 \times 49.6711 \text{ (PVAF 6\%-57 months)} & = & \$186,267 \\ \$3750 \times 40.3249 \text{ (PVAF 6\%-45 months)} & = & \underline{\$151,218} \\ & & \$337,485/2 & = \$168,743 \end{array}$$

Average TIB for the policy year:

$$\begin{array}{rcl} \$90,000 \times 57/120 & = & \$42,750 \\ \$90,000 \times 45/120 & = & \underline{\$33,750} \\ & & \$76,500/2 & = \underline{\$38,250.} \\ \mathbf{Premium basis is \$168,743 + \$38,250} & & & = \mathbf{\$206,993} \end{array}$$

Writing this coverage on the basis of the premium will leave the client underinsured in the first six months of the policy period. Remember the limit and the premium basis are different.

Let's go a little further... Same risk year 2 (renewal).

Present rent of \$10.00 per square foot each year on 7,500 square feet. Cost to relocate in a satisfactory location would result in a rental value of \$16.00 per square foot each year. (In year 2) 45 months are remaining on the lease as of the effective date of policy. The insured spent \$90,000 on Tenants Improvements and Betterments at inception of the lease. Original lease term was for 10 years.

Assuming the present value of money at 6% the value of the gross leasehold interest is:

$$\mathbf{\$3750} \quad \mathbf{x} \quad \mathbf{40.3249 \text{ (PVAF 6\% @45 months)}} \quad \mathbf{= \$151,218}$$

The interest in Tenants Improvements and Betterments is:

$$\mathbf{\$90,000} \quad \mathbf{x} \quad \mathbf{45/120} \quad \mathbf{= \$33,750}$$

unamortized TIB

$$\mathbf{\$151,218 \text{ (interest in lease + } \$33,750 \text{ (interest in TIB's))} \quad \mathbf{= \$184,968.}$$

The premium will be based as follows:

Net leasehold interest for the policy year:

$$\begin{aligned} \$3750 \times 40.3249 \text{ (PVAF 6\%-45 months)} &= \$151,218 \\ \$3750 \times 30.4178 \text{ (PVAF 6\%-33 months)} &= \underline{\$114,067} \\ &\$265,285/2 = \$132,643 \end{aligned}$$

Average TIB for the policy year:

$$\begin{aligned} \$90,000 \times 45/120 &= \$33,750 \\ \$90,000 \times 33/120 &= \underline{\$24,750} \\ &\$58,500/2 = \$ 29,250 \end{aligned}$$

$$\mathbf{\text{Premium basis is:} \quad \mathbf{\$132,643} \quad \mathbf{+} \quad \mathbf{\$29,250} \quad \mathbf{= \$161,893}}$$

Ok, just a little further... Same risk year 2. Comparable rents \$17.00 per square foot.

$$\begin{array}{rclclcl} \$17.00 & \times & 7500 & = & \$127,500/12 & = \$10,625 \text{ per month} \\ & & & & & \underline{\$6,250} \text{ current rent} \\ & & & & & \$4,375 \text{ leasehold interest} \end{array}$$

Assuming the present value of money at 6% the value of the gross leasehold interest is:

$$\$4375 \quad \times \quad 40.3249 \text{ (PVAF 6\%-45 months)} \quad = \quad \$176,421$$

$$\$90,000 \quad \times \quad 45/120 \quad = \quad \$33,750 \text{ unamortized TIB}$$

$$\mathbf{\$176,421 \text{ (interest in lease)} + \$33,750 \text{ (interest in TIB's)} = \mathbf{\$210,171.}$$

PREMIUM will be based upon:

Net leasehold interest for the policy year:

$$\$4375 \times 40.3249 \text{ (PVAF 6\%-45 months)} \quad = \quad \$176,241$$

$$\begin{array}{rcl} \$4375 \times 30.4178 \text{ (PVAF 6\%-33 months)} & = & \underline{\$133,078} \\ & & \$309,499/2 = \$154,749 \end{array}$$

Average TIB for the policy year:

$$\$90,000 \times 45/120 \quad = \quad \$33,750$$

$$\begin{array}{rcl} \$90,000 \times 33/120 & = & \underline{\$24,750} \\ & & \$58,500/2 = \$29,250 \end{array}$$

$$\mathbf{Premium \text{ basis is } \$154,749 + \$29,250 = \$183,999}$$

EXPLANATION OF DISCOUNT FACTOR FOR LEASEHOLD INTEREST

1. The discount factor is not used for the first three months of Leasehold Interest based on the assumption that it will take the insurance company that amount of time to adjust the loss. Accordingly, the insured probably would not receive any payment under the insurance prior to the three months period. 2. Loss payment under Leasehold Interest is made in one lump sum which could represent a significant financial advantage to the insured if they were to invest the money at the current interest rate providing them with more money than the loss represented. Accordingly, the insurance is written to discount the amount by the current interest rate thus if the insured were to invest the money they would end up even. 3. The factor is used in arriving at the amount of insurance to be provided and in setting the premium basis.

An EXAMPLE: \$2000 Leasehold Interest per month x 60 (5 years remaining on the lease). \$120,000 (Total Leasehold Interest). With a 6% interest assumption, the insured would purchase \$103.848 which represents a sum that would produce a \$2000 per month annuity for 5 years if invested at 6%. (6%-60 month PVAF is 51.9238)

Situation #3 – The Lease and Personal Property

Bubba, in attempt to control his capital outlay has decided to lease some office equipment as well as weight lifting equipment from his local supplier. His leased equipment includes:

1. Telephone system
2. Copy Machine
3. Fax Machine
4. Two (2) computers
5. Universal weight lifting machine – value \$40,000
6. Complete free weight dumbbell and barbell set – value \$20,000

Bubba has not read any of his leases (imagine that!), but wants his interest in this property adequately covered.

Bubba's lease states:

3. The renter shall during the rental term keep and maintain the property in good working condition and repair and shall be responsible for any loss, casualty, damage or destruction to said property notwithstanding how caused and Renter agrees to return said property in its present condition, reasonable wear and tear accepted.

Question #1 - Bubba has a fire that destroys the property listed above. Bubba is devastated. He calls you his agent. You insure Bubba's tenant's improvements and betterments and his business personal property with a Building and Personal Property Coverage Form. Assuming adequate coverage for Business Personal Property, how will this loss be paid?

What if Bubba's lease states:

8. *Insurance: For the lease term set forth above, you will provide and maintain, at your expense, (a) property insurance against the loss or theft of or damage to the Products, for their full replacement value naming us as loss payee and (b) public liability and third party property damage insurance naming us as additional insured. All insurance shall be in the form and amount and with companies satisfactory to us and will provide that we will be given thirty (30) days written notice before cancellation or material change of the policy. At our request, you will deliver the policies or certificates of insurance to us. If you do not give us evidence of insurance acceptable to us we have the right, but not the obligation, to obtain such insurance covering our interest in the Products for the Lease Term. The cost for such insurance will be an additional amount due from you under the lease.*

Question #2 - Will this lease language change your answer to question 1 above?

Question #3 - We now have put Bubba's property in the correct "pot." Bubba suffers yet another fire loss that destroys his leased property. How does the Building and Business Personal Property Coverage Form value damage to this type of property.

Situation #4 – The Rental Car Agreement and the Business Auto Policy

Bubba has two (2) salespersons that travel extensively to trade shows and exhibitions in order to keep up on the latest and greatest sporting goods equipment. Both salespersons rent cars when on business. Bubba has an account with several of the major rental car companies to get discounted rates. This may shock you, but no one has ever read the rental agreement to determine what, if anything, Bubba could be responsible for if the vehicles were involved in an accident. Again, no surprise, but Bubba never told you about the rental of these vehicles.

The rental agreement states:

...the renter agrees to return the vehicle in the same condition as rented, save normal wear and tear. The renter agrees to repair or replace any and all damage to the vehicle including a reasonable charge for loss of use and other charges such as towing, storage, legal, and/or administrative charges.

...said charges will be paid in the same manner and with the same method of payment used at the time of the original rental.

Loss Damage Waiver (LDW) LDW is an optional service which relieves you of any responsibility for the loss of or damage to the rental car resulting from any cause, provided the car is used in accordance with the terms of the rental agreement. Cost of LDW may vary depending on location or car type and is charged per each full or partial day of rental. (Exception - California LDW does not extend to theft. A renter is responsible for the theft of the car only if it results from failure to exercise ordinary care. See Loss Damage Waiver in the location index for specific charges.

PROHIBITED USE:

...protection can be void if any of the following violations occur. (Note-exclusion of protection can vary by location and should be verified at the rental counter).

- *Permit use of car by anyone other than authorized operators.*
- *Intentionally destroy, damage or aid in car's theft.*
- *Take or attempt to take the car to Mexico or elsewhere out of the U.S. without prior approval from the rental location.*
- *Engaging in any willful or wanton misconduct which may include reckless conduct such as, when overloaded, to carry persons or property for hire, or off regularly maintained roads, or leaving the car and failing to remove keys or close and lock all doors, windows, trunk and car is vandalized or stolen.*
- *Use or permit the use of the car by anyone, under the influence of alcohol or drugs, for purposes that could properly be charged a felony, such as the illegal transportation of persons, drugs or contraband, to tow or push, speed contest, driver training, or is obtained from Hertz by fraud or misrepresentation.*

Question # 1 - One of Bubba's employees while in Las Vegas at a national sporting goods convention rented a car in the name of Bubba's Sporting Emporium, Inc. using her company credit card that is in the same name. Unfortunately, she has been involved in an accident causing \$14,000 damage to the rental car not including loss of use. Her dilemma is how to explain the additional charges on the company credit card. What is your advice as Bubba's agent?

Question # 2 – The same employee several months later has decided the way to avoid all of this nonsense when renting a car is to rent the vehicle in her own name using her own credit card. She will simply turn in the expense of the car and gas on her monthly expense report. Unfortunately, her next rental experience resulted in an at fault accident totaling a \$30,000 rental car. Her new dilemma is to figure out how to include the \$30,000, plus loss of use in on her next expense report. She has called you before notifying Bubba of this latest tragedy. Does this set of facts change your answer to the question above?

Situation #5 – Bubba has decided to install a brand new sixty (60) foot sign on the roof of his building. He has the permission of Strip Centers, Inc. However, the prices he has received from the local sign installers are astronomical. But Bubba, being the creative business man that he is has decided to install the sign himself with a little help of his friends. Bubba has rented a crane and two scissor lifts from a local rental company to put the sign in place. Once again, Bubba did not read the rental agreement before taking possession of the equipment.

The rental agreement states:

Equipment rental

- *Rental rates do not include applicable sales tax, freight, or fire, theft, and vandalism insurance*
- *All units are covered by 30-day power train warranty*
- *Rental rates are subject to change without prior notice*
- *All damage/Abuse of rental equipment is the customer's responsibility*
- *Fuel tank is to be full when returned to avoid additional costs*

Required daily on all rentals

- *Inspect unit for safe operating conditions*
- *Check and maintain all fluid levels*
- *Lubricate/grease all areas and components*

Required every 250 hours on all rentals:

- *Take oil samples and send to nearest Ring Power facility*
- *Change oil and filters noting date and hours on service record tag*

Question # 1- While lifting the sign into place the boom of the crane collapses because the sign exceeded the lifting capacity of the crane. Bubba is furious with the rental company because of the damage to his sign. He is even more furious when he receives a bill from the rental company for \$ 16,000 for damage to the crane. What, if anything, can you his agent do for him?

Question # 2 – If your client was a contractor who rented this equipment, how would his Contractors Equipment policy respond?

Situation #6 - Bubba is pleased to announce the graduation of his oldest daughter from high school. The graduation party is held at the local country club where the announcement is made that his daughter will be attending Florida State University. Bubba could not be happier with his daughter's choice of schools. Bubba flies to Tallahassee with his daughter to pick-out an apartment that his daughter and best friend will be sharing. Bubba signs a one year lease with options to renew each year for five years. Once again, Bubba does not read the lease carefully.

The lease states:

Repairs and Maintenance: The landlord agrees to be responsible for major repairs to the interior and exterior of the building, provided however, that repairs required through damages caused by the tenant(s) or guests shall be charged to the tenant(s). Tenant(s) agree to immediately notify the landlord of any needed repairs in writing. The cost of repair or replacement of screens, light bulbs, heating and air conditioner filters must be changed each month by the tenant.

Insurance: It is agreed that the Landlord/Property Manager shall not be responsible for loss of any personal property or injury to any person coming upon the premises as the licensee or invitee of the tenant(s). The tenant(s) agree to purchase Renters Insurance with liability coverage of not less than \$100,000.

Return of Premises to Landlord: At the end of the term of this lease, the tenant(s) shall quit and deliver the premises to the landlord in as good or better condition as they were first leased.

Question #1 – Bubba's daughter does not know what an air conditioning filter is must less how to change one. Six months after occupancy Bubba's daughter notifies the property manager that the air conditioner is not working. After a visit from the local air conditioner repairperson, Bubba receives a bill from the property manager for \$1400 which is the cost of a new compressor for the apartment he rented. Does Bubba have any insurance for this unfortunate situation?

Question #2 – Bubba's daughter and her roommate through an end of the year party after finals before everyone goes home for the summer. During the party some adult beverages were served. A guest had a little too much to drink and fell off of the balcony. The lawsuits are filed and Bubba puts you on notice of the claim. However, Bubba has received a notice from the property management company and the owner of the building asking they be defended and protected from any and all judgments resulting from this unfortunate event. He forwards the letter to you, what is your advice?

EXHIBITS

COMMERCIAL PROPERTY CONDITIONS

This Coverage Part is subject to the following conditions, the Common Policy Conditions and applicable Loss Conditions and Additional Conditions in Commercial Property Coverage Forms.

A. CONCEALMENT, MISREPRESENTATION OR FRAUD

This Coverage Part is void in any case of fraud by you as it relates to this Coverage Part at any time. It is also void if you or any other insured, at any time, intentionally conceal or misrepresent a material fact concerning:

1. This Coverage Part;
2. The Covered Property;
3. Your interest in the Covered Property; or
4. A claim under this Coverage Part.

B. CONTROL OF PROPERTY

Any act or neglect of any person other than you beyond your direction or control will not affect this insurance.

The breach of any condition of this Coverage Part at any one or more locations will not affect coverage at any location where, at the time of loss or damage, the breach of condition does not exist.

C. INSURANCE UNDER TWO OR MORE COVERAGES

If two or more of this policy's coverages apply to the same loss or damage, we will not pay more than the actual amount of the loss or damage.

D. LEGAL ACTION AGAINST US

No one may bring a legal action against us under this Coverage Part unless:

1. There has been full compliance with all of the terms of this Coverage Part; and
2. The action is brought within 2 years after the date on which the direct physical loss or damage occurred.

E. LIBERALIZATION

If we adopt any revision that would broaden the coverage under this Coverage Part without additional premium within 45 days prior to or during the policy period, the broadened coverage will immediately apply to this Coverage Part.

F. NO BENEFIT TO BAILEE

No person or organization, other than you, having custody of Covered Property will benefit from this insurance.

G. OTHER INSURANCE

1. You may have other insurance subject to the same plan, terms, conditions and provisions as the insurance under this Coverage Part. If you do, we will pay our share of the covered loss or damage. Our share is the proportion that the applicable Limit of Insurance under this Coverage Part bears to the Limits of Insurance of all insurance covering on the same basis.

2. If there is other insurance covering the same loss or damage, other than that described in 1. above, we will pay only for the amount of covered loss or damage in excess of the amount due from that other insurance, whether you can collect on it or not. But we will not pay more than the applicable Limit of Insurance.

H. POLICY PERIOD, COVERAGE TERRITORY

Under this Coverage Part:

1. We cover loss or damage commencing:
 - a. During the policy period shown in the Declarations; and
 - b. Within the coverage territory.
2. The coverage territory is:
 - a. The United States of America (including its territories and possessions);
 - b. Puerto Rico; and
 - c. Canada.

I. TRANSFER OF RIGHTS OF RECOVERY AGAINST OTHERS TO US

If any person or organization to or for whom we make payment under this Coverage Part has rights to recover damages from another, those rights are transferred to us to the extent of our payment. That person or organization must do everything necessary to secure our rights and must do nothing after loss to impair them. But you may waive your rights against another party in writing:

1. Prior to a loss to your Covered Property or Covered Income.
2. After a loss to your Covered Property or Covered Income only if, at time of loss, that party is one of the following:
 - a. Someone insured by this insurance;
 - b. A business firm:
 - (1) Owned or controlled by you; or
 - (2) That owns or controls you; or
 - c. Your tenant.

This will not restrict your insurance.

SAMPLE

BUILDING AND PERSONAL PROPERTY COVERAGE FORM

Various provisions in this policy restrict coverage. Read the entire policy carefully to determine rights, duties and what is and is not covered.

Throughout this policy, the words "you" and "your" refer to the Named Insured shown in the Declarations. The words "we", "us" and "our" refer to the company providing this insurance.

Other words and phrases that appear in quotation marks have special meaning. Refer to Section H. Definitions.

A. Coverage

We will pay for direct physical loss of or damage to Covered Property at the premises described in the Declarations caused by or resulting from any Covered Cause of Loss.

1. Covered Property

Covered Property, as used in this Coverage Part, means the type of property described in this section, **A.1.**, and limited in **A.2.** Property Not Covered, if a Limit Of Insurance is shown in the Declarations for that type of property.

a. Building, meaning the building or structure described in the Declarations, including:

- (1) Completed additions;
- (2) Fixtures, including outdoor fixtures;
- (3) Permanently installed:
 - (a) Machinery; and
 - (b) Equipment;
- (4) Personal property owned by you that is used to maintain or service the building or structure or its premises, including:
 - (a) Fire-extinguishing equipment;
 - (b) Outdoor furniture;
 - (c) Floor coverings; and
 - (d) Appliances used for refrigerating, ventilating, cooking, dishwashing or laundering;
- (5) If not covered by other insurance:
 - (a) Additions under construction, alterations and repairs to the building or structure;
 - (b) Materials, equipment, supplies and temporary structures, on or within 100 feet of the described premises, used for making additions, alterations or repairs to the building or structure.

b. Your Business Personal Property

consists of the following property located in or on the building or structure described in the Declarations or in the open (or in a vehicle) within 100 feet of the building or structure or within 100 feet of the premises described in the Declarations, whichever distance is greater:

- (1) Furniture and fixtures;
- (2) Machinery and equipment;
- (3) "Stock";
- (4) All other personal property owned by you and used in your business;
- (5) Labor, materials or services furnished or arranged by you on personal property of others;
- (6) Your use interest as tenant in improvements and betterments. Improvements and betterments are fixtures, alterations, installations or additions:
 - (a) Made a part of the building or structure you occupy but do not own; and
 - (b) You acquired or made at your expense but cannot legally remove;
- (7) Leased personal property for which you have a contractual responsibility to insure, unless otherwise provided for under Personal Property Of Others.

c. Personal Property Of Others that is:

- (1) In your care, custody or control; and
- (2) Located in or on the building or structure described in the Declarations or in the open (or in a vehicle) within 100 feet of the building or structure or within 100 feet of the premises described in the Declarations, whichever distance is greater.

However, our payment for loss of or damage to personal property of others will only be for the account of the owner of the property.

2. Property Not Covered

Covered Property does not include:

- a. Accounts, bills, currency, food stamps or other evidences of debt, money, notes or securities. Lottery tickets held for sale are not securities;
- b. Animals, unless owned by others and boarded by you, or if owned by you, only as "stock" while inside of buildings;
- c. Automobiles held for sale;
- d. Bridges, roadways, walks, patios or other paved surfaces;
- e. Contraband, or property in the course of illegal transportation or trade;
- f. The cost of excavations, grading, backfilling or filling;
- g. Foundations of buildings, structures, machinery or boilers if their foundations are below:
 - (1) The lowest basement floor; or
 - (2) The surface of the ground, if there is no basement;
- h. Land (including land on which the property is located), water, growing crops or lawns (other than lawns which are part of a vegetated roof);
- i. Personal property while airborne or waterborne;
- j. Bulkheads, pilings, piers, wharves or docks;
- k. Property that is covered under another coverage form of this or any other policy in which it is more specifically described, except for the excess of the amount due (whether you can collect on it or not) from that other insurance;
- l. Retaining walls that are not part of a building;
- m. Underground pipes, flues or drains;
- n. Electronic data, except as provided under the Additional Coverage, Electronic Data. Electronic data means information, facts or computer programs stored as or on, created or used on, or transmitted to or from computer software (including systems and applications software), on hard or floppy disks, CD-ROMs, tapes, drives, cells, data processing devices or any other repositories of computer software which are used with electronically controlled equipment. The term computer programs, referred to in the foregoing description of electronic data, means a set of related electronic instructions which direct the operations and functions of a computer or device connected to it, which enable the computer or device to receive, process, store, retrieve or send data. This paragraph, n., does not apply to your "stock" of prepackaged software, or to electronic data which is integrated in and operates or controls the building's elevator, lighting, heating, ventilation, air conditioning or security system;
- o. The cost to replace or restore the information on valuable papers and records, including those which exist as electronic data. Valuable papers and records include but are not limited to proprietary information, books of account, deeds, manuscripts, abstracts, drawings and card index systems. Refer to the Coverage Extension for Valuable Papers And Records (Other Than Electronic Data) for limited coverage for valuable papers and records other than those which exist as electronic data;
- p. Vehicles or self-propelled machines (including aircraft or watercraft) that:
 - (1) Are licensed for use on public roads; or
 - (2) Are operated principally away from the described premises.This paragraph does not apply to:
 - (a) Vehicles or self-propelled machines or autos you manufacture, process or warehouse;

- (b) Vehicles or self-propelled machines, other than autos, you hold for sale;
 - (c) Rowboats or canoes out of water at the described premises; or
 - (d) Trailers, but only to the extent provided for in the Coverage Extension for Non-owned Detached Trailers; or
- q. The following property while outside of buildings:
- (1) Grain, hay, straw or other crops;
 - (2) Fences, radio or television antennas (including satellite dishes) and their lead-in wiring, masts or towers, trees, shrubs or plants (other than trees, shrubs or plants which are "stock" or are part of a vegetated roof), all except as provided in the Coverage Extensions.

3. Covered Causes Of Loss

See applicable Causes Of Loss form as shown in the Declarations.

4. Additional Coverages

a. Debris Removal

- (1) Subject to Paragraphs (2), (3) and (4), we will pay your expense to remove debris of Covered Property and other debris that is on the described premises, when such debris is caused by or results from a Covered Cause of Loss that occurs during the policy period. The expenses will be paid only if they are reported to us in writing within 180 days of the date of direct physical loss or damage.
 - (2) Debris Removal does not apply to costs to:
 - (a) Remove debris of property of yours that is not insured under this policy, or property in your possession that is not Covered Property;
 - (b) Remove debris of property owned by or leased to the landlord of the building where your described premises are located, unless you have a contractual responsibility to insure such property and it is insured under this policy;
 - (c) Remove any property that is Property Not Covered, including property addressed under the Outdoor Property Coverage Extension;
 - (d) Remove property of others of a type that would not be Covered Property under this Coverage Form;
 - (e) Remove deposits of mud or earth from the grounds of the described premises;
 - (f) Extract "pollutants" from land or water; or
 - (g) Remove, restore or replace polluted land or water.
- (3) Subject to the exceptions in Paragraph (4), the following provisions apply:
- (a) The most we will pay for the total of direct physical loss or damage plus debris removal expense is the Limit of Insurance applicable to the Covered Property that has sustained loss or damage.
 - (b) Subject to (a) above, the amount we will pay for debris removal expense is limited to 25% of the sum of the deductible plus the amount that we pay for direct physical loss or damage to the Covered Property that has sustained loss or damage. However, if no Covered Property has sustained direct physical loss or damage, the most we will pay for removal of debris of other property (if such removal is covered under this Additional Coverage) is \$5,000 at each location.
- (4) We will pay up to an additional \$25,000 for debris removal expense, for each location, in any one occurrence of physical loss or damage to Covered Property, if one or both of the following circumstances apply:
- (a) The total of the actual debris removal expense plus the amount we pay for direct physical loss or damage exceeds the Limit of Insurance on the Covered Property that has sustained loss or damage.
 - (b) The actual debris removal expense exceeds 25% of the sum of the deductible plus the amount that we pay for direct physical loss or damage to the Covered Property that has sustained loss or damage.

Therefore, if (4)(a) and/or (4)(b) applies, our total payment for direct physical loss or damage and debris removal expense may reach but will never exceed the Limit of Insurance on the Covered Property that has sustained loss or damage, plus \$25,000.

(5) Examples

The following examples assume that there is no Coinsurance penalty.

Example 1

Limit of Insurance:	\$ 90,000
Amount of Deductible:	\$ 500
Amount of Loss:	\$ 50,000
Amount of Loss Payable:	\$ 49,500
	(\$50,000 – \$500)
Debris Removal Expense:	\$ 10,000
Debris Removal Expense Payable:	\$ 10,000
	(\$10,000 is 20% of \$50,000.)

The debris removal expense is less than 25% of the sum of the loss payable plus the deductible. The sum of the loss payable and the debris removal expense (\$49,500 + \$10,000 = \$59,500) is less than the Limit of Insurance. Therefore, the full amount of debris removal expense is payable in accordance with the terms of Paragraph (3).

Example 2

Limit of Insurance:	\$ 90,000
Amount of Deductible:	\$ 500
Amount of Loss:	\$ 80,000
Amount of Loss Payable:	\$ 79,500
	(\$80,000 – \$500)
Debris Removal Expense:	\$ 40,000
Debris Removal Expense Payable	
Basic Amount:	\$ 10,500
Additional Amount:	\$ 25,000

The basic amount payable for debris removal expense under the terms of Paragraph (3) is calculated as follows: \$80,000 (\$79,500 + \$500) x .25 = \$20,000, capped at \$10,500. The cap applies because the sum of the loss payable (\$79,500) and the basic amount payable for debris removal expense (\$10,500) cannot exceed the Limit of Insurance (\$90,000).

The additional amount payable for debris removal expense is provided in accordance with the terms of Paragraph (4), because the debris removal expense (\$40,000) exceeds 25% of the loss payable plus the deductible (\$40,000 is 50% of \$80,000), and because the sum of the loss payable and debris removal expense (\$79,500 + \$40,000 = \$119,500) would exceed the Limit of Insurance (\$90,000). The additional amount of covered debris removal expense is \$25,000, the maximum payable under Paragraph (4). Thus, the total payable for debris removal expense in this example is \$35,500; \$4,500 of the debris removal expense is not covered.

b. Preservation Of Property

If it is necessary to move Covered Property from the described premises to preserve it from loss or damage by a Covered Cause of Loss, we will pay for any direct physical loss or damage to that property:

- (1) While it is being moved or while temporarily stored at another location; and
- (2) Only if the loss or damage occurs within 30 days after the property is first moved.

c. Fire Department Service Charge

When the fire department is called to save or protect Covered Property from a Covered Cause of Loss, we will pay up to \$1,000 for service at each premises described in the Declarations, unless a higher limit is shown in the Declarations. Such limit is the most we will pay regardless of the number of responding fire departments or fire units, and regardless of the number or type of services performed.

This Additional Coverage applies to your liability for fire department service charges:

- (1) Assumed by contract or agreement prior to loss; or
- (2) Required by local ordinance.

No Deductible applies to this Additional Coverage.

d. Pollutant Clean-up And Removal

We will pay your expense to extract "pollutants" from land or water at the described premises if the discharge, dispersal, seepage, migration, release or escape of the "pollutants" is caused by or results from a Covered Cause of Loss that occurs during the policy period. The expenses will be paid only if they are reported to us in writing within 180 days of the date on which the Covered Cause of Loss occurs.

This Additional Coverage does not apply to costs to test for, monitor or assess the existence, concentration or effects of "pollutants". But we will pay for testing which is performed in the course of extracting the "pollutants" from the land or water.

The most we will pay under this Additional Coverage for each described premises is \$10,000 for the sum of all covered expenses arising out of Covered Causes of Loss occurring during each separate 12-month period of this policy.

e. Increased Cost Of Construction

- (1) This Additional Coverage applies only to buildings to which the Replacement Cost Optional Coverage applies.
- (2) In the event of damage by a Covered Cause of Loss to a building that is Covered Property, we will pay the increased costs incurred to comply with the minimum standards of an ordinance or law in the course of repair, rebuilding or replacement of damaged parts of that property, subject to the limitations stated in e.(3) through e.(9) of this Additional Coverage.
- (3) The ordinance or law referred to in e.(2) of this Additional Coverage is an ordinance or law that regulates the construction or repair of buildings or establishes zoning or land use requirements at the described premises and is in force at the time of loss.
- (4) Under this Additional Coverage, we will not pay any costs due to an ordinance or law that:
 - (a) You were required to comply with before the loss, even when the building was undamaged; and
 - (b) You failed to comply with.

(5) Under this Additional Coverage, we will not pay for:

- (a) The enforcement of or compliance with any ordinance or law which requires demolition, repair, replacement, reconstruction, remodeling or remediation of property due to contamination by "pollutants" or due to the presence, growth, proliferation, spread or any activity of "fungus", wet or dry rot or bacteria; or
- (b) Any costs associated with the enforcement of or compliance with an ordinance or law which requires any insured or others to test for, monitor, clean up, remove, contain, treat, detoxify or neutralize, or in any way respond to, or assess the effects of "pollutants", "fungus", wet or dry rot or bacteria.

(6) The most we will pay under this Additional Coverage, for each described building insured under this Coverage Form, is \$10,000 or 5% of the Limit of Insurance applicable to that building, whichever is less. If a damaged building is covered under a blanket Limit of Insurance which applies to more than one building or item of property, then the most we will pay under this Additional Coverage, for that damaged building, is the lesser of \$10,000 or 5% times the value of the damaged building as of the time of loss times the applicable Coinsurance percentage.

The amount payable under this Additional Coverage is additional insurance.

(7) With respect to this Additional Coverage:

- (a) We will not pay for the Increased Cost of Construction:
 - (i) Until the property is actually repaired or replaced at the same or another premises; and
 - (ii) Unless the repair or replacement is made as soon as reasonably possible after the loss or damage, not to exceed two years. We may extend this period in writing during the two years.

- (b) If the building is repaired or replaced at the same premises, or if you elect to rebuild at another premises, the most we will pay for the Increased Cost of Construction, subject to the provisions of **e.(6)** of this Additional Coverage, is the increased cost of construction at the same premises.
- (c) If the ordinance or law requires relocation to another premises, the most we will pay for the Increased Cost of Construction, subject to the provisions of **e.(6)** of this Additional Coverage, is the increased cost of construction at the new premises.
- (8) This Additional Coverage is not subject to the terms of the Ordinance Or Law Exclusion to the extent that such Exclusion would conflict with the provisions of this Additional Coverage.
- (9) The costs addressed in the Loss Payment and Valuation Conditions and the Replacement Cost Optional Coverage, in this Coverage Form, do not include the increased cost attributable to enforcement of or compliance with an ordinance or law. The amount payable under this Additional Coverage, as stated in **e.(6)** of this Additional Coverage, is not subject to such limitation.

f. Electronic Data

- (1) Under this Additional Coverage, electronic data has the meaning described under Property Not Covered, Electronic Data. This Additional Coverage does not apply to your "stock" of prepackaged software, or to electronic data which is integrated in and operates or controls the building's elevator, lighting, heating, ventilation, air conditioning or security system.
 - (2) Subject to the provisions of this Additional Coverage, we will pay for the cost to replace or restore electronic data which has been destroyed or corrupted by a Covered Cause of Loss. To the extent that electronic data is not replaced or restored, the loss will be valued at the cost of replacement of the media on which the electronic data was stored, with blank media of substantially identical type.
- (3) The Covered Causes of Loss applicable to Your Business Personal Property apply to this Additional Coverage, Electronic Data, subject to the following:
 - (a) If the Causes Of Loss – Special Form applies, coverage under this Additional Coverage, Electronic Data, is limited to the "specified causes of loss" as defined in that form and Collapse as set forth in that form.
 - (b) If the Causes Of Loss – Broad Form applies, coverage under this Additional Coverage, Electronic Data, includes Collapse as set forth in that form.
 - (c) If the Causes Of Loss form is endorsed to add a Covered Cause of Loss, the additional Covered Cause of Loss does not apply to the coverage provided under this Additional Coverage, Electronic Data.
 - (d) The Covered Causes of Loss include a virus, harmful code or similar instruction introduced into or enacted on a computer system (including electronic data) or a network to which it is connected, designed to damage or destroy any part of the system or disrupt its normal operation. But there is no coverage for loss or damage caused by or resulting from manipulation of a computer system (including electronic data) by any employee, including a temporary or leased employee, or by an entity retained by you or for you to inspect, design, install, modify, maintain, repair or replace that system.

- (4) The most we will pay under this Additional Coverage, Electronic Data, is \$2,500 (unless a higher limit is shown in the Declarations) for all loss or damage sustained in any one policy year, regardless of the number of occurrences of loss or damage or the number of premises, locations or computer systems involved. If loss payment on the first occurrence does not exhaust this amount, then the balance is available for subsequent loss or damage sustained in but not after that policy year. With respect to an occurrence which begins in one policy year and continues or results in additional loss or damage in a subsequent policy year(s), all loss or damage is deemed to be sustained in the policy year in which the occurrence began.

5. Coverage Extensions

Except as otherwise provided, the following Extensions apply to property located in or on the building described in the Declarations or in the open (or in a vehicle) within 100 feet of the described premises.

If a Coinsurance percentage of 80% or more, or a Value Reporting period symbol, is shown in the Declarations, you may extend the insurance provided by this Coverage Part as follows:

a. Newly Acquired Or Constructed Property

(1) Buildings

If this policy covers Building, you may extend that insurance to apply to:

- (a) Your new buildings while being built on the described premises; and
- (b) Buildings you acquire at locations, other than the described premises, intended for:
 - (i) Similar use as the building described in the Declarations; or
 - (ii) Use as a warehouse.

The most we will pay for loss or damage under this Extension is \$250,000 at each building.

(2) Your Business Personal Property

- (a) If this policy covers Your Business Personal Property, you may extend that insurance to apply to:
 - (i) Business personal property, including such property that you newly acquire, at any location you acquire other than at fairs, trade shows or exhibitions; or
 - (ii) Business personal property, including such property that you newly acquire, located at your newly constructed or acquired buildings at the location described in the Declarations.

The most we will pay for loss or damage under this Extension is \$100,000 at each building.

- (b) This Extension does not apply to:
 - (i) Personal property of others that is temporarily in your possession in the course of installing or performing work on such property; or
 - (ii) Personal property of others that is temporarily in your possession in the course of your manufacturing or wholesaling activities.

(3) Period Of Coverage

With respect to insurance provided under this Coverage Extension for Newly Acquired Or Constructed Property, coverage will end when any of the following first occurs:

- (a) This policy expires;
- (b) 30 days expire after you acquire the property or begin construction of that part of the building that would qualify as covered property; or
- (c) You report values to us.

We will charge you additional premium for values reported from the date you acquire the property or begin construction of that part of the building that would qualify as covered property.

b. Personal Effects And Property Of Others

You may extend the insurance that applies to Your Business Personal Property to apply to:

- (1) Personal effects owned by you, your officers, your partners or members, your managers or your employees. This Extension does not apply to loss or damage by theft.
- (2) Personal property of others in your care, custody or control.

The most we will pay for loss or damage under this Extension is \$2,500 at each described premises. Our payment for loss of or damage to personal property of others will only be for the account of the owner of the property.

c. Valuable Papers And Records (Other Than Electronic Data)

- (1) You may extend the insurance that applies to Your Business Personal Property to apply to the cost to replace or restore the lost information on valuable papers and records for which duplicates do not exist. But this Extension does not apply to valuable papers and records which exist as electronic data. Electronic data has the meaning described under Property Not Covered, Electronic Data.
- (2) If the Causes Of Loss – Special Form applies, coverage under this Extension is limited to the "specified causes of loss" as defined in that form and Collapse as set forth in that form.
- (3) If the Causes Of Loss – Broad Form applies, coverage under this Extension includes Collapse as set forth in that form.
- (4) Under this Extension, the most we will pay to replace or restore the lost information is \$2,500 at each described premises, unless a higher limit is shown in the Declarations. Such amount is additional insurance. We will also pay for the cost of blank material for reproducing the records (whether or not duplicates exist) and (when there is a duplicate) for the cost of labor to transcribe or copy the records. The costs of blank material and labor are subject to the applicable Limit of Insurance on Your Business Personal Property and, therefore, coverage of such costs is not additional insurance.

d. Property Off-premises

- (1) You may extend the insurance provided by this Coverage Form to apply to your Covered Property while it is away from the described premises, if it is:
 - (a) Temporarily at a location you do not own, lease or operate;
 - (b) In storage at a location you lease, provided the lease was executed after the beginning of the current policy term; or
 - (c) At any fair, trade show or exhibition.
- (2) This Extension does not apply to property:
 - (a) In or on a vehicle; or
 - (b) In the care, custody or control of your salespersons, unless the property is in such care, custody or control at a fair, trade show or exhibition.
- (3) The most we will pay for loss or damage under this Extension is \$10,000.

e. Outdoor Property

You may extend the insurance provided by this Coverage Form to apply to your outdoor fences, radio and television antennas (including satellite dishes), trees, shrubs and plants (other than trees, shrubs or plants which are "stock" or are part of a vegetated roof), including debris removal expense, caused by or resulting from any of the following causes of loss if they are Covered Causes of Loss:

- (1) Fire;
- (2) Lightning;
- (3) Explosion;
- (4) Riot or Civil Commotion; or
- (5) Aircraft.

The most we will pay for loss or damage under this Extension is \$1,000, but not more than \$250 for any one tree, shrub or plant. These limits apply to any one occurrence, regardless of the types or number of items lost or damaged in that occurrence.

Subject to all aforementioned terms and limitations of coverage, this Coverage Extension includes the expense of removing from the described premises the debris of trees, shrubs and plants which are the property of others, except in the situation in which you are a tenant and such property is owned by the landlord of the described premises.

f. Non-owned Detached Trailers

- (1) You may extend the insurance that applies to Your Business Personal Property to apply to loss or damage to trailers that you do not own, provided that:
 - (a) The trailer is used in your business;
 - (b) The trailer is in your care, custody or control at the premises described in the Declarations; and
 - (c) You have a contractual responsibility to pay for loss or damage to the trailer.
- (2) We will not pay for any loss or damage that occurs:
 - (a) While the trailer is attached to any motor vehicle or motorized conveyance, whether or not the motor vehicle or motorized conveyance is in motion;
 - (b) During hitching or unhitching operations, or when a trailer becomes accidentally unhitched from a motor vehicle or motorized conveyance.
- (3) The most we will pay for loss or damage under this Extension is \$5,000, unless a higher limit is shown in the Declarations.
- (4) This insurance is excess over the amount due (whether you can collect on it or not) from any other insurance covering such property.

g. Business Personal Property Temporarily In Portable Storage Units

- (1) You may extend the insurance that applies to Your Business Personal Property to apply to such property while temporarily stored in a portable storage unit (including a detached trailer) located within 100 feet of the building or structure described in the Declarations or within 100 feet of the premises described in the Declarations, whichever distance is greater.

- (2) If the applicable Covered Causes of Loss form or endorsement contains a limitation or exclusion concerning loss or damage from sand, dust, sleet, snow, ice or rain to property in a structure, such limitation or exclusion also applies to property in a portable storage unit.
- (3) Coverage under this Extension:
 - (a) Will end 90 days after the business personal property has been placed in the storage unit;
 - (b) Does not apply if the storage unit itself has been in use at the described premises for more than 90 consecutive days, even if the business personal property has been stored there for 90 or fewer days as of the time of loss or damage.
- (4) Under this Extension, the most we will pay for the total of all loss or damage to business personal property is \$10,000 (unless a higher limit is indicated in the Declarations for such Extension) regardless of the number of storage units. Such limit is part of, not in addition to, the applicable Limit of Insurance on Your Business Personal Property. Therefore, payment under this Extension will not increase the applicable Limit of Insurance on Your Business Personal Property.
- (5) This Extension does not apply to loss or damage otherwise covered under this Coverage Form or any endorsement to this Coverage Form or policy, and does not apply to loss or damage to the storage unit itself.

Each of these Extensions is additional insurance unless otherwise indicated. The Additional Condition, Coinsurance, does not apply to these Extensions.

B. Exclusions And Limitations

See applicable Causes Of Loss form as shown in the Declarations.

C. Limits Of Insurance

The most we will pay for loss or damage in any one occurrence is the applicable Limit Of Insurance shown in the Declarations.

The most we will pay for loss or damage to outdoor signs, whether or not the sign is attached to a building, is \$2,500 per sign in any one occurrence.

The amounts of insurance stated in the following Additional Coverages apply in accordance with the terms of such coverages and are separate from the Limit(s) Of Insurance shown in the Declarations for any other coverage:

1. Fire Department Service Charge;
2. Pollutant Clean-up And Removal;
3. Increased Cost Of Construction; and
4. Electronic Data.

Payments under the Preservation Of Property Additional Coverage will not increase the applicable Limit of Insurance.

D. Deductible

In any one occurrence of loss or damage (hereinafter referred to as loss), we will first reduce the amount of loss if required by the Coinsurance Condition or the Agreed Value Optional Coverage. If the adjusted amount of loss is less than or equal to the Deductible, we will not pay for that loss. If the adjusted amount of loss exceeds the Deductible, we will then subtract the Deductible from the adjusted amount of loss and will pay the resulting amount or the Limit of Insurance, whichever is less.

When the occurrence involves loss to more than one item of Covered Property and separate Limits of Insurance apply, the losses will not be combined in determining application of the Deductible. But the Deductible will be applied only once per occurrence.

Example 1

(This example assumes there is no Coinsurance penalty.)

Deductible:	\$ 250
Limit of Insurance – Building 1:	\$ 60,000
Limit of Insurance – Building 2:	\$ 80,000
Loss to Building 1:	\$ 60,100
Loss to Building 2:	\$ 90,000

The amount of loss to Building 1 (\$60,100) is less than the sum (\$60,250) of the Limit of Insurance applicable to Building 1 plus the Deductible.

The Deductible will be subtracted from the amount of loss in calculating the loss payable for Building 1:

\$ 60,100
– 250
<hr style="width: 50px; margin-left: 0;"/>

\$ 59,850 Loss Payable – Building 1

The Deductible applies once per occurrence and therefore is not subtracted in determining the amount of loss payable for Building 2. Loss payable for Building 2 is the Limit of Insurance of \$80,000.

Total amount of loss payable:
\$59,850 + \$80,000 = \$139,850

Example 2

(This example, too, assumes there is no Coinsurance penalty.)

The Deductible and Limits of Insurance are the same as those in Example 1.

Loss to Building 1:	\$ 70,000
(Exceeds Limit of Insurance plus Deductible)	
Loss to Building 2:	\$ 90,000
(Exceeds Limit of Insurance plus Deductible)	
Loss Payable – Building 1:	\$ 60,000
(Limit of Insurance)	
Loss Payable – Building 2:	\$ 80,000
(Limit of Insurance)	
Total amount of loss payable:	\$ 140,000

E. Loss Conditions

The following conditions apply in addition to the Common Policy Conditions and the Commercial Property Conditions:

1. Abandonment

There can be no abandonment of any property to us.

2. Appraisal

If we and you disagree on the value of the property or the amount of loss, either may make written demand for an appraisal of the loss. In this event, each party will select a competent and impartial appraiser. The two appraisers will select an umpire. If they cannot agree, either may request that selection be made by a judge of a court having jurisdiction. The appraisers will state separately the value of the property and amount of loss. If they fail to agree, they will submit their differences to the umpire. A decision agreed to by any two will be binding. Each party will:

- a. Pay its chosen appraiser; and
- b. Bear the other expenses of the appraisal and umpire equally.

If there is an appraisal, we will still retain our right to deny the claim.

3. Duties In The Event Of Loss Or Damage

a. You must see that the following are done in the event of loss or damage to Covered Property:

- (1) Notify the police if a law may have been broken.

- (2) Give us prompt notice of the loss or damage. Include a description of the property involved.
 - (3) As soon as possible, give us a description of how, when and where the loss or damage occurred.
 - (4) Take all reasonable steps to protect the Covered Property from further damage, and keep a record of your expenses necessary to protect the Covered Property, for consideration in the settlement of the claim. This will not increase the Limit of Insurance. However, we will not pay for any subsequent loss or damage resulting from a cause of loss that is not a Covered Cause of Loss. Also, if feasible, set the damaged property aside and in the best possible order for examination.
 - (5) At our request, give us complete inventories of the damaged and undamaged property. Include quantities, costs, values and amount of loss claimed.
 - (6) As often as may be reasonably required, permit us to inspect the property proving the loss or damage and examine your books and records.
Also, permit us to take samples of damaged and undamaged property for inspection, testing and analysis, and permit us to make copies from your books and records.
 - (7) Send us a signed, sworn proof of loss containing the information we request to investigate the claim. You must do this within 60 days after our request. We will supply you with the necessary forms.
 - (8) Cooperate with us in the investigation or settlement of the claim.
- b. We may examine any insured under oath, while not in the presence of any other insured and at such times as may be reasonably required, about any matter relating to this insurance or the claim, including an insured's books and records. In the event of an examination, an insured's answers must be signed.

4. Loss Payment

- a. In the event of loss or damage covered by this Coverage Form, at our option, we will either:
 - (1) Pay the value of lost or damaged property;
 - (2) Pay the cost of repairing or replacing the lost or damaged property, subject to **b.** below;
 - (3) Take all or any part of the property at an agreed or appraised value; or
 - (4) Repair, rebuild or replace the property with other property of like kind and quality, subject to **b.** below.

We will determine the value of lost or damaged property, or the cost of its repair or replacement, in accordance with the applicable terms of the Valuation Condition in this Coverage Form or any applicable provision which amends or supersedes the Valuation Condition.
- b. The cost to repair, rebuild or replace does not include the increased cost attributable to enforcement of or compliance with any ordinance or law regulating the construction, use or repair of any property.
- c. We will give notice of our intentions within 30 days after we receive the sworn proof of loss.
- d. We will not pay you more than your financial interest in the Covered Property.
- e. We may adjust losses with the owners of lost or damaged property if other than you. If we pay the owners, such payments will satisfy your claims against us for the owners' property. We will not pay the owners more than their financial interest in the Covered Property.
- f. We may elect to defend you against suits arising from claims of owners of property. We will do this at our expense.
- g. We will pay for covered loss or damage within 30 days after we receive the sworn proof of loss, if you have complied with all of the terms of this Coverage Part, and:
 - (1) We have reached agreement with you on the amount of loss; or
 - (2) An appraisal award has been made.

h. A party wall is a wall that separates and is common to adjoining buildings that are owned by different parties. In settling covered losses involving a party wall, we will pay a proportion of the loss to the party wall based on your interest in the wall in proportion to the interest of the owner of the adjoining building. However, if you elect to repair or replace your building and the owner of the adjoining building elects not to repair or replace that building, we will pay you the full value of the loss to the party wall, subject to all applicable policy provisions including Limits of Insurance, the Valuation and Coinsurance Conditions and all other provisions of this Loss Payment Condition. Our payment under the provisions of this paragraph does not alter any right of subrogation we may have against any entity, including the owner or insurer of the adjoining building, and does not alter the terms of the Transfer Of Rights Of Recovery Against Others To Us Condition in this policy.

5. Recovered Property

If either you or we recover any property after loss settlement, that party must give the other prompt notice. At your option, the property will be returned to you. You must then return to us the amount we paid to you for the property. We will pay recovery expenses and the expenses to repair the recovered property, subject to the Limit of Insurance.

6. Vacancy

a. Description Of Terms

(1) As used in this Vacancy Condition, the term building and the term vacant have the meanings set forth in **(1)(a)** and **(1)(b)** below:

(a) When this policy is issued to a tenant, and with respect to that tenant's interest in Covered Property, building means the unit or suite rented or leased to the tenant. Such building is vacant when it does not contain enough business personal property to conduct customary operations.

(b) When this policy is issued to the owner or general lessee of a building, building means the entire building. Such building is vacant unless at least 31% of its total square footage is:

- (i)** Rented to a lessee or sublessee and used by the lessee or sublessee to conduct its customary operations; and/or
- (ii)** Used by the building owner to conduct customary operations.

(2) Buildings under construction or renovation are not considered vacant.

b. Vacancy Provisions

If the building where loss or damage occurs has been vacant for more than 60 consecutive days before that loss or damage occurs:

(1) We will not pay for any loss or damage caused by any of the following, even if they are Covered Causes of Loss:

- (a)** Vandalism;
- (b)** Sprinkler leakage, unless you have protected the system against freezing;
- (c)** Building glass breakage;
- (d)** Water damage;
- (e)** Theft; or
- (f)** Attempted theft.

(2) With respect to Covered Causes of Loss other than those listed in **b.(1)(a)** through **b.(1)(f)** above, we will reduce the amount we would otherwise pay for the loss or damage by 15%.

7. Valuation

We will determine the value of Covered Property in the event of loss or damage as follows:

- a.** At actual cash value as of the time of loss or damage, except as provided in **b.**, **c.**, **d.** and **e.** below.
- b.** If the Limit of Insurance for Building satisfies the Additional Condition, Coinsurance, and the cost to repair or replace the damaged building property is \$2,500 or less, we will pay the cost of building repairs or replacement.

The cost of building repairs or replacement does not include the increased cost attributable to enforcement of or compliance with any ordinance or law regulating the construction, use or repair of any property.

However, the following property will be valued at the actual cash value, even when attached to the building:

- (1) Awnings or floor coverings;
 - (2) Appliances for refrigerating, ventilating, cooking, dishwashing or laundering; or
 - (3) Outdoor equipment or furniture.
- c. "Stock" you have sold but not delivered at the selling price less discounts and expenses you otherwise would have had.
- d. Glass at the cost of replacement with safety-glazing material if required by law.
- e. Tenants' Improvements and Betterments at:
- (1) Actual cash value of the lost or damaged property if you make repairs promptly.
 - (2) A proportion of your original cost if you do not make repairs promptly. We will determine the proportionate value as follows:
 - (a) Multiply the original cost by the number of days from the loss or damage to the expiration of the lease; and
 - (b) Divide the amount determined in (a) above by the number of days from the installation of improvements to the expiration of the lease.

If your lease contains a renewal option, the expiration of the renewal option period will replace the expiration of the lease in this procedure.

- (3) Nothing if others pay for repairs or replacement.

F. Additional Conditions

The following conditions apply in addition to the Common Policy Conditions and the Commercial Property Conditions:

1. Coinsurance

If a Coinsurance percentage is shown in the Declarations, the following condition applies:

- a. We will not pay the full amount of any loss if the value of Covered Property at the time of loss times the Coinsurance percentage shown for it in the Declarations is greater than the Limit of Insurance for the property.

Instead, we will determine the most we will pay using the following steps:

- (1) Multiply the value of Covered Property at the time of loss by the Coinsurance percentage;
- (2) Divide the Limit of Insurance of the property by the figure determined in Step (1);
- (3) Multiply the total amount of loss, before the application of any deductible, by the figure determined in Step (2); and
- (4) Subtract the deductible from the figure determined in Step (3).

We will pay the amount determined in Step (4) or the Limit of Insurance, whichever is less. For the remainder, you will either have to rely on other insurance or absorb the loss yourself.

Example 1 (Underinsurance)

When:	The value of the property is:	\$ 250,000
	The Coinsurance percentage for it is:	80%
	The Limit of Insurance for it is:	\$ 100,000
	The Deductible is:	\$ 250
	The amount of loss is:	\$ 40,000

Step (1): $\$250,000 \times 80\% = \$200,000$
(the minimum amount of insurance to meet your Coinsurance requirements)

Step (2): $\$100,000 \div \$200,000 = .50$

Step (3): $\$40,000 \times .50 = \$20,000$

Step (4): $\$20,000 - \$250 = \$19,750$

We will pay no more than \$19,750. The remaining \$20,250 is not covered.

Example 2 (Adequate Insurance)

When:	The value of the property is:	\$ 250,000
	The Coinsurance percentage for it is:	80%
	The Limit of Insurance for it is:	\$ 200,000
	The Deductible is:	\$ 250
	The amount of loss is:	\$ 40,000

The minimum amount of insurance to meet your Coinsurance requirement is \$200,000 ($\$250,000 \times 80\%$). Therefore, the Limit of Insurance in this example is adequate, and no penalty applies. We will pay no more than \$39,750 ($\$40,000$ amount of loss minus the deductible of \$250).

- b. If one Limit of Insurance applies to two or more separate items, this condition will apply to the total of all property to which the limit applies.

Example 3

When: The value of the property is:

Building at Location 1:	\$ 75,000
Building at Location 2:	\$ 100,000
Personal Property at Location 2:	<u>\$ 75,000</u>
	\$ 250,000
The Coinsurance percentage for it is:	90%
The Limit of Insurance for Buildings and Personal Property at Locations 1 and 2 is:	\$ 180,000
The Deductible is:	\$ 1,000
The amount of loss is:	
Building at Location 2:	\$ 30,000
Personal Property at Location 2:	<u>\$ 20,000</u>
	\$ 50,000

Step (1): $\$250,000 \times 90\% = \$225,000$
 (the minimum amount of insurance to meet your Coinsurance requirements and to avoid the penalty shown below)

Step (2): $\$180,000 \div \$225,000 = .80$

Step (3): $\$50,000 \times .80 = \$40,000$

Step (4): $\$40,000 - \$1,000 = \$39,000$

We will pay no more than \$39,000. The remaining \$11,000 is not covered.

2. Mortgageholders

- a. The term mortgageholder includes trustee.
- b. We will pay for covered loss of or damage to buildings or structures to each mortgageholder shown in the Declarations in their order of precedence, as interests may appear.
- c. The mortgageholder has the right to receive loss payment even if the mortgageholder has started foreclosure or similar action on the building or structure.
- d. If we deny your claim because of your acts or because you have failed to comply with the terms of this Coverage Part, the mortgageholder will still have the right to receive loss payment if the mortgageholder:
 - (1) Pays any premium due under this Coverage Part at our request if you have failed to do so;

- (2) Submits a signed, sworn proof of loss within 60 days after receiving notice from us of your failure to do so; and
- (3) Has notified us of any change in ownership, occupancy or substantial change in risk known to the mortgageholder.

All of the terms of this Coverage Part will then apply directly to the mortgageholder.

- e. If we pay the mortgageholder for any loss or damage and deny payment to you because of your acts or because you have failed to comply with the terms of this Coverage Part:
 - (1) The mortgageholder's rights under the mortgage will be transferred to us to the extent of the amount we pay; and
 - (2) The mortgageholder's right to recover the full amount of the mortgageholder's claim will not be impaired.

At our option, we may pay to the mortgageholder the whole principal on the mortgage plus any accrued interest. In this event, your mortgage and note will be transferred to us and you will pay your remaining mortgage debt to us.

- f. If we cancel this policy, we will give written notice to the mortgageholder at least:
 - (1) 10 days before the effective date of cancellation if we cancel for your nonpayment of premium; or
 - (2) 30 days before the effective date of cancellation if we cancel for any other reason.
- g. If we elect not to renew this policy, we will give written notice to the mortgageholder at least 10 days before the expiration date of this policy.

G. Optional Coverages

If shown as applicable in the Declarations, the following Optional Coverages apply separately to each item:

1. Agreed Value

- a. The Additional Condition, Coinsurance, does not apply to Covered Property to which this Optional Coverage applies. We will pay no more for loss of or damage to that property than the proportion that the Limit of Insurance under this Coverage Part for the property bears to the Agreed Value shown for it in the Declarations.

- b. If the expiration date for this Optional Coverage shown in the Declarations is not extended, the Additional Condition, Coinsurance, is reinstated and this Optional Coverage expires.
- c. The terms of this Optional Coverage apply only to loss or damage that occurs:
 - (1) On or after the effective date of this Optional Coverage; and
 - (2) Before the Agreed Value expiration date shown in the Declarations or the policy expiration date, whichever occurs first.

2. Inflation Guard

- a. The Limit of Insurance for property to which this Optional Coverage applies will automatically increase by the annual percentage shown in the Declarations.
- b. The amount of increase will be:
 - (1) The Limit of Insurance that applied on the most recent of the policy inception date, the policy anniversary date, or any other policy change amending the Limit of Insurance, times
 - (2) The percentage of annual increase shown in the Declarations, expressed as a decimal (example: 8% is .08), times
 - (3) The number of days since the beginning of the current policy year or the effective date of the most recent policy change amending the Limit of Insurance, divided by 365.

Example

If: The applicable Limit of Insurance is: \$ 100,000
 The annual percentage increase is: 8%
 The number of days since the beginning of the policy year (or last policy change) is: 146
 The amount of increase is:
 $\$100,000 \times .08 \times 146 \div 365 =$ \$ 3,200

3. Replacement Cost

- a. Replacement Cost (without deduction for depreciation) replaces Actual Cash Value in the Valuation Loss Condition of this Coverage Form.
- b. This Optional Coverage does not apply to:
 - (1) Personal property of others;
 - (2) Contents of a residence;
 - (3) Works of art, antiques or rare articles, including etchings, pictures, statuary, marbles, bronzes, porcelains and bric-a-brac; or

- (4) "Stock", unless the Including "Stock" option is shown in the Declarations.

Under the terms of this Replacement Cost Optional Coverage, tenants' improvements and betterments are not considered to be the personal property of others.

- c. You may make a claim for loss or damage covered by this insurance on an actual cash value basis instead of on a replacement cost basis. In the event you elect to have loss or damage settled on an actual cash value basis, you may still make a claim for the additional coverage this Optional Coverage provides if you notify us of your intent to do so within 180 days after the loss or damage.
- d. We will not pay on a replacement cost basis for any loss or damage:
 - (1) Until the lost or damaged property is actually repaired or replaced; and
 - (2) Unless the repair or replacement is made as soon as reasonably possible after the loss or damage.

With respect to tenants' improvements and betterments, the following also apply:

- (3) If the conditions in d.(1) and d.(2) above are not met, the value of tenants' improvements and betterments will be determined as a proportion of your original cost, as set forth in the Valuation Loss Condition of this Coverage Form; and
- (4) We will not pay for loss or damage to tenants' improvements and betterments if others pay for repairs or replacement.
- e. We will not pay more for loss or damage on a replacement cost basis than the least of (1), (2) or (3), subject to f. below:
 - (1) The Limit of Insurance applicable to the lost or damaged property;
 - (2) The cost to replace the lost or damaged property with other property:
 - (a) Of comparable material and quality; and
 - (b) Used for the same purpose; or
 - (3) The amount actually spent that is necessary to repair or replace the lost or damaged property.

If a building is rebuilt at a new premises, the cost described in e.(2) above is limited to the cost which would have been incurred if the building had been rebuilt at the original premises.

- f. The cost of repair or replacement does not include the increased cost attributable to enforcement of or compliance with any ordinance or law regulating the construction, use or repair of any property.

4. Extension Of Replacement Cost To Personal Property Of Others

a. If the Replacement Cost Optional Coverage is shown as applicable in the Declarations, then this Extension may also be shown as applicable. If the Declarations show this Extension as applicable, then Paragraph **3.b.(1)** of the Replacement Cost Optional Coverage is deleted and all other provisions of the Replacement Cost Optional Coverage apply to replacement cost on personal property of others.

b. With respect to replacement cost on the personal property of others, the following limitation applies:

If an item(s) of personal property of others is subject to a written contract which governs your liability for loss or damage to that item(s), then valuation of that item(s) will be based on the amount for which you are liable under such contract, but not to exceed the lesser of the replacement cost of the property or the applicable Limit of Insurance.

H. Definitions

1. "Fungus" means any type or form of fungus, including mold or mildew, and any mycotoxins, spores, scents or by-products produced or released by fungi.
2. "Pollutants" means any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed.
3. "Stock" means merchandise held in storage or for sale, raw materials and in-process or finished goods, including supplies used in their packing or shipping.

SAMPLE

LEGAL LIABILITY COVERAGE FORM

Various provisions in this policy restrict coverage. Read the entire policy carefully to determine rights, duties and what is and is not covered.

Throughout this policy, the words "you" and "your" refer to the Named Insured shown in the Declarations. The words "we", "us" and "our" refer to the company providing this insurance.

Other words and phrases that appear in quotation marks have special meaning. Refer to Section F. Definitions.

A. Coverage

We will pay those sums that you become legally obligated to pay as damages because of direct physical loss or damage, including loss of use, to Covered Property caused by accident and arising out of any Covered Cause of Loss. We will have the right and duty to defend any "suit" seeking those damages. However, we have no duty to defend you against a "suit" seeking damages for direct physical loss or damage to which this insurance does not apply. We may investigate and settle any claim or "suit" at our discretion. But:

- (1) The amount we will pay for damages is limited as described in Section C. Limits Of Insurance; and
- (2) Our right and duty to defend end when we have used up the Limit of Insurance in the payment of judgments or settlements.

1. Covered Property And Limitations

Covered Property, as used in this Coverage Form, means tangible property of others in your care, custody or control that is described in the Declarations or on the Legal Liability Coverage Schedule.

Covered Property does not include electronic data. Electronic data means information, facts or computer programs stored as or on, created or used on, or transmitted to or from computer software (including systems and applications software), on hard or floppy disks, CD-ROMs, tapes, drives, cells, data processing devices or any other repositories of computer software which are used with electronically controlled equipment. The term computer programs, referred to in the foregoing description of electronic data, means a set of related electronic instructions which direct the operations and functions of a computer or device connected to it, which enable the computer or device to receive, process, store, retrieve or send data. This paragraph does not apply to electronic data which is integrated in and operates or controls the building's elevator, lighting, heating, ventilation, air conditioning or security system.

2. Covered Causes Of Loss

See applicable Causes of Loss form as shown in the Declarations.

3. Additional Coverage

SUPPLEMENTARY PAYMENTS

We will pay, with respect to any claim or any "suit" against you we defend:

- a. All expenses we incur.
- b. The cost of bonds to release attachments, but only for bond amounts within our Limit of Insurance. We do not have to furnish these bonds.
- c. All reasonable expenses incurred by you at our request, including actual loss of earnings up to \$250 a day because of time off from work.
- d. All costs taxed against you in the "suit".
- e. Prejudgment interest awarded against you on that part of the judgment we pay. If we make an offer to pay the Limit of Insurance, we will not pay any prejudgment interest based on that period of time after the offer.
- f. All interest on the full amount of any judgment that accrues after entry of the judgment and before we have paid, offered to pay, or deposited in court the part of the judgment that is within our Limit of Insurance.

These payments will not reduce the applicable Limit of Insurance.

4. Coverage Extensions

a. Additional Insureds

If the Named Insured shown in the Declarations is a partnership, limited liability company or corporation, throughout this Coverage Form the words "you" and "your" include:

- (1) Partners, members, executive officers, trustees, directors and stockholders of such partnership, limited liability company or corporation, but only with respect to their duties as such; and
- (2) Managers of a limited liability company, but only with respect to their duties as such.

b. Newly Acquired Organizations

Throughout this Coverage Form, the words "you" and "your" also include any organization (other than a partnership, joint venture or limited liability company) you newly acquire or form and over which you maintain ownership or majority interest if there is no other similar insurance available to that organization.

This Coverage Extension ends:

- (1) 90 days after you acquire or form the organization; or
 - (2) At the end of the policy period shown in the Declarations;
- whichever is earlier.

This Extension does not apply to direct physical loss or damage that occurred before you acquired or formed the organization.

c. Newly Acquired Property

- (1) You may extend the insurance that applies to Covered Property, as used in this Coverage Form, to apply to your liability for tangible property of others that comes under your care, custody or control after the beginning of the current policy period. This Extension is subject to the following:

- (a) All terms and Conditions of this Coverage Form.

- (b) Buildings must be intended for:

- (i) Similar use as the building described in the Declarations or on the Legal Liability Coverage Schedule; or
- (ii) Use as a warehouse.

The most we will pay as the result of any one accident for loss or damage to buildings covered under this Extension is \$250,000 at each building.

- (c) Personal property must be at a location:

- (i) That you own; or
 - (ii) That is or comes under your care, custody or control;
- other than at fairs or exhibitions.

The most we will pay as the result of any one accident for loss or damage to personal property covered under this Extension is \$100,000 at each building.

- (2) Insurance under this Extension for each item of property of others will end when any of the following first occurs:
 - (a) This policy expires;
 - (b) 30 days expire after the property has come under your care, custody or control; or
 - (c) You report values to us.

We will charge you additional premium for values reported from the date the property comes under your care, custody or control.

This Extension does not apply to direct physical loss or damage that occurred before the property came under your care, custody or control.

B. Exclusions And Limitations

See applicable Causes of Loss form as shown in the Declarations.

C. Limits Of Insurance

The most we will pay in damages as the result of any one accident is the applicable Limit Of Insurance shown on the Legal Liability Coverage Schedule, or in the Declarations.

Payments under the Additional Coverage and the Newly Acquired Property Coverage Extension are in addition to the Limits of Insurance.

The existence of one or more:

1. Additional Insureds; or
2. Newly Acquired Organizations,

does not increase the Limit of Insurance.

D. Loss Conditions

The following conditions apply in addition to the Commercial Property Conditions:

1. Duties In The Event Of Accident, Claim Or Suit

- a. You must see to it that we are notified promptly of any accident that may result in a claim. Notice should include:

- (1) How, when and where the accident took place; and
- (2) The names and addresses of any witnesses.

Notice of an accident is not notice of a claim.

- b. If a claim is made or "suit" is brought against you, you must see to it that we receive prompt written notice of the claim or "suit".

- c. You must:

- (1) Immediately send us copies of any demands, notices, summonses or legal papers received in connection with the claim or "suit";
- (2) Authorize us to obtain records and other information;
- (3) Cooperate with us in the investigation, settlement or defense of the claim or "suit"; and

- (4) Assist us, upon our request, in the enforcement of any right against any person or organization that may be liable to you because of damage to which this insurance may also apply.

- d. You will not, except at your own cost, voluntarily make a payment, assume any obligation, or incur any expense without our consent.

2. Legal Action Against Us

No person or organization has a right under this Coverage Form:

- a. To join us as a party or otherwise bring us into a "suit" asking for damages from you; or
- b. To sue us on this Coverage Form unless all of its terms have been fully complied with.

A person or organization may sue us to recover on an agreed settlement or on a final judgment against you obtained after an actual trial; but we will not be liable for damages that are not payable under the terms of this Coverage Form or that are in excess of the Limit of Insurance. An agreed settlement means a settlement and release of liability signed by us, you and the claimant or the claimant's legal representative.

3. Other Insurance

You may have other insurance covering the same loss as the insurance under this Coverage Form. If you do, we will pay our share of the covered loss. Our share is the proportion that the Limit of Insurance under this Coverage Form covering such loss bears to the Limits of Insurance of all insurance covering the loss.

4. Transfer Of Rights Of Recovery Against Others To Us

If you have rights to recover all or part of any payment we have made under this Coverage Form, those rights are transferred to us. You must do nothing after loss to impair them. At our request, you will bring "suit" or transfer those rights to us and help us enforce them.

E. Additional Conditions

The following conditions apply in addition to the Common Policy Conditions:

1. Amendment Of Commercial Property Conditions

None of the Commercial Property Conditions apply to this Coverage Form, except:

- a. Condition **A.** Concealment, Misrepresentation Or Fraud;

- b. Condition **C.** Insurance Under Two Or More Coverages; and
- c. Condition **E.** Liberalization.

2. Bankruptcy

Bankruptcy or insolvency of you or your estate will not relieve us of our obligations under this Coverage Form.

3. Policy Period, Coverage Territory

Under this Coverage Form:

- a. We will pay for loss or damage caused by an accident that occurs:
 - (1) During the Policy Period shown in the Declarations; and

- (2) Within the coverage territory.

b. The coverage territory is:

- (1) The United States of America;
- (2) Puerto Rico; and
- (3) Canada.

4. Separation Of Insureds

The insurance under this Coverage Form applies separately to you and each additional insured, except with respect to the Limits of Insurance.

F. Definitions

"Suit" includes an arbitration proceeding to which you must submit or submit with our consent.

SAMPLE

LEASEHOLD INTEREST COVERAGE FORM

Throughout this policy the words "you" and "your" refer to the Named Insured shown in the Declarations. The words "we", "us" and "our" refer to the Company providing this insurance.

Other words and phrases that appear in quotation marks have special meaning. Refer to SECTION F. – DEFINITIONS.

A. COVERAGE

We will pay for loss of Covered Leasehold Interest you sustain due to the cancellation of your lease. The cancellation must result from direct physical loss of or damage to property at the premises described in the Declarations caused by or resulting from any Covered Cause of Loss.

1. Covered Leasehold Interest

Covered Leasehold Interest means the following for which an amount of "net leasehold interest" at inception is shown in the Leasehold Interest Coverage Schedule:

a. **Tenants' Lease Interest**, meaning the difference between the:

- (1) Rent you pay at the described premises; and
- (2) Rental value of the described premises that you lease.

b. **Bonus Payments**, meaning the unamortized portion of a cash bonus that will not be refunded to you. A cash bonus is money you paid to acquire your lease. It does not include:

- (1) Rent, whether or not prepaid; or
- (2) Security.

c. **Improvements and Betterments**, meaning the unamortized portion of payments made by you for improvements and betterments. It does not include the value of improvements and betterments recoverable under any other insurance, but only to the extent of such other insurance.

Improvements and betterments are fixtures, alterations, installations or additions:

- (1) Made a part of the building or structure you occupy but do not own; and

- (2) You acquired or made at your expense but cannot legally remove.

d. **Prepaid Rent**, meaning the unamortized portion of any amount of advance rent you paid that will not be refunded to you. This does not include the customary rent due at:

- (1) The beginning of each month; or
- (2) Any other rental period.

2. Covered Causes Of Loss

See applicable Causes of Loss Form as shown in the Declarations.

B. EXCLUSIONS AND LIMITATIONS

See applicable Causes of Loss Form as shown in the Declarations.

C. LIMITS OF INSURANCE

1. Applicable to Tenants' Lease Interest

a. The most we will pay for loss because of the cancellation of any one lease is your "net leasehold interest" at the time of loss.

But, if your lease is cancelled and your landlord lets you continue to use your premises under a new lease or other arrangement, the most we will pay for loss because of the cancellation of any one lease is the lesser of:

- (1) The difference between the rent you now pay and the rent you will pay under the new lease or other arrangement; or
- (2) Your "net leasehold interest" at the time of loss.

- b. Your "net leasehold interest" decreases automatically each month. The amount of "net leasehold interest" at any time is your "gross leasehold interest" times the leasehold interest factor for the remaining months of your lease. A proportionate share applies for any period of time less than a month.

Refer to the end of this form for a table of leasehold interest factors.

2. Applicable to Bonus Payments, Improvements and Betterments and Prepaid Rent

- a. The most we will pay for loss because of the cancellation of any one lease is your "net leasehold interest" at the time of loss.

But, if your lease is cancelled and your landlord lets you continue to use your premises under a new lease or other arrangement, the most we will pay for loss because of the cancellation of any one lease is the lesser of:

- (1) The loss sustained by you; or
- (2) Your "net leasehold interest" at the time of loss.

- b. Your "net leasehold interest" decreases automatically each month. The amount of each decrease is your "monthly leasehold interest". A proportionate share applies for any period of time less than a month.

D. LOSS CONDITIONS

The following conditions apply in addition to the Common Policy Conditions and the Commercial Property Conditions.

1. Appraisal

If we and you disagree on the amount of loss, either may make written demand for an appraisal. In this event, each party will select a competent and impartial appraiser. The two appraisers will select an umpire. If they cannot agree, either may request that selection be made by a judge of a court having jurisdiction. The appraisers will state the amount of loss. If they fail to agree, they will submit their differences to the umpire. A decision agreed to by any two will be binding. Each party will:

- a. Pay its chosen appraiser; and
- b. Bear the other expenses of the appraisal and umpire equally.

If there is an appraisal, we will still retain our right to deny the claim.

2. Duties In The Event Of Loss Of Covered Leasehold Interest

- a. You must see that the following are done in the event of loss of Covered Leasehold Interest:

- (1) Notify the police if a law may have been broken.
- (2) Give us prompt notice of the direct physical loss or damage. Include a description of the property involved.
- (3) As soon as possible, give us a description of how, when and where the direct physical loss or damage occurred.
- (4) Take all reasonable steps to protect the property at the described premises from further damage by a Covered Cause of Loss. However, we will not pay for any subsequent loss or damage resulting from a cause of loss that is not a Covered Cause of Loss. Also, if feasible, set the damaged property aside and in the best possible order for examination.
- (5) As often as may be reasonably required, permit us to inspect the property proving the loss or damage and examine your books and records.

Also permit us to take samples of damaged and undamaged property for inspection, testing and analysis, and permit us to make copies from your books and records.

- (6) Send us a signed, sworn proof of loss containing the information we request to investigate the claim. You must do this within 60 days after our request. We will supply you with the necessary forms.
 - (7) Cooperate with us in the investigation or settlement of the claim.
- b. We may examine any insured under oath, while not in the presence of any other insured and at such times as may be reasonably required, about any matter relating to this insurance or the claim, including an insured's books and records. In the event of an examination, an insured's answers must be signed.

3. Loss Payment

We will pay for covered loss within 30 days after we receive the sworn proof of loss, if:

- a. You have complied with all of the terms of this Coverage Part; and
- b.(1) We have reached agreement with you on the amount of loss; or
- (2) An appraisal award has been made.

4. Vacancy

a. Description of Terms

- (1) As used in this Vacancy Condition, with respect to the tenant's interest in Covered Property, building means the unit or suite rented or leased to the tenant. Such building is vacant when it does not contain enough business personal property to conduct customary operations.
- (2) Buildings under construction or renovation are not considered vacant.

b. Vacancy Provisions – Subleased Premises

The following provisions apply if the building where direct physical loss or damage occurs has been vacant for more than 60 consecutive days before that loss or damage occurs, provided you have entered into an agreement to sublease the described premises as of the time of loss or damage:

- (1) We will not pay for any loss or damage caused by any of the following even if they are Covered Causes of Loss:
 - (a) Vandalism;
 - (b) Sprinkler leakage, unless you have protected the system against freezing;
 - (c) Building glass breakage;
 - (d) Water damage;
 - (e) Theft; or
 - (f) Attempted theft.
- (2) With respect to a Covered Cause of Loss not listed in (1)(a) through (1)(f) above, we will reduce the amount we would otherwise pay for the loss or damage by 15%.
- c. If you have not entered into an agreement to sublease the described premises as of the time of loss or damage, we will not pay for any loss of Covered Leasehold Interest.

E. ADDITIONAL CONDITION

The following condition replaces the Cancellation Common Policy Condition:

CANCELLATION

1. The first Named Insured shown in the Declarations may cancel this policy by mailing or delivering to us advance notice of cancellation.
2. We may cancel this policy by mailing or delivering to the first Named Insured written notice of cancellation at least:
 - a. 10 days before the effective date of cancellation if we cancel for nonpayment of premium; or
 - b. 30 days before the effective date of cancellation if we cancel for any other reason.
3. We will mail or deliver our notice to the first Named Insured's last mailing address known to us.
4. Notice of cancellation will state the effective date of cancellation. The policy will end on that date.
5. If this policy is cancelled, we will send the first Named Insured any premium refund due. The cancellation will be effective even if we have not made or offered a refund.
6. If this coverage is cancelled, we will calculate the earned premium by:
 - a. Computing the average of the "net leasehold interest" at the:
 - (1) Inception date, and
 - (2) Cancellation date, of this coverage.
 - b. Multiplying the rate for the period of coverage by the average "net leasehold interest".
 - c. If we cancel, we will send you a premium refund based on the difference between the:
 - (1) Premium you originally paid us; and
 - (2) Proportion of the premium calculated by multiplying the amount in paragraph a. times the rate for the period of coverage for the expired term of the policy.
 - d. If you cancel, your refund may be less than the refund calculated in paragraph c.
7. If notice is mailed, proof of mailing will be sufficient proof of notice.

F. DEFINITIONS

1. **"Gross Leasehold Interest"** means the difference between the:

- a. Monthly rental value of the premises you lease; and
- b. Actual monthly rent you pay including taxes, insurance, janitorial or other service that you pay for as part of the rent.

This amount is not changed:

- (1) Whether you occupy all or part of the premises; or
- (2) If you sublet the premises.

Example:

Rental value of your leased premises	\$5,000
Monthly rent including taxes, insurance, janitorial or other service that you pay for as part of the rent	<u>-4,000</u>
"Gross Leasehold Interest"	\$1,000

2. **"Monthly Leasehold Interest"** means the monthly portion of covered Bonus Payments, Improvements and Betterments and Prepaid Rent. To find your "monthly leasehold interest", divide your original costs of Bonus Payments, Improvements and Betterments or Prepaid Rent by the number of months left in your lease at the time of the expenditure.

Example:

Original cost of Bonus Payment	\$12,000
With 24 months left in the lease at time of Bonus Payment	÷ <u>24</u>
"Monthly Leasehold Interest"	\$500

3. **"Net Leasehold Interest":**

a. Applicable to Tenants' Lease Interest.

"Net Leasehold Interest" means the present value of your "gross leasehold interest" for each remaining month of the term of the lease at the rate of interest shown in the Leasehold Interest Coverage Schedule.

The "net leasehold interest" is the amount that, placed at the rate of interest shown in the Leasehold Interest Coverage Schedule, would be equivalent to your receiving the "Gross Leasehold Interest" for each separate month of the unexpired term of the lease.

To find your "net leasehold interest" at any time, multiply your "gross leasehold interest" by the leasehold interest factor found in the table of leasehold interest factors attached to this form.

Example:

(20 months left in lease, 10% effective annual rate of interest)

"Gross Leasehold Interest"	\$ 1,000
Leasehold Interest Factor	<u>× 18.419</u>
"Net Leasehold Interest"	\$18,419

b. Applicable to Bonus Payments, Improvements and Betterments or Prepaid Rent.

"Net Leasehold Interest" means the un-amortized amount shown in the Schedule. Your "net leasehold interest" at any time is your "monthly leasehold interest" times the number of months left in your lease.

Example:

"Monthly Leasehold Interest"	\$ 500
With 10 months left in lease	<u>× 10</u>
"Net Leasehold Interest"	\$5,000

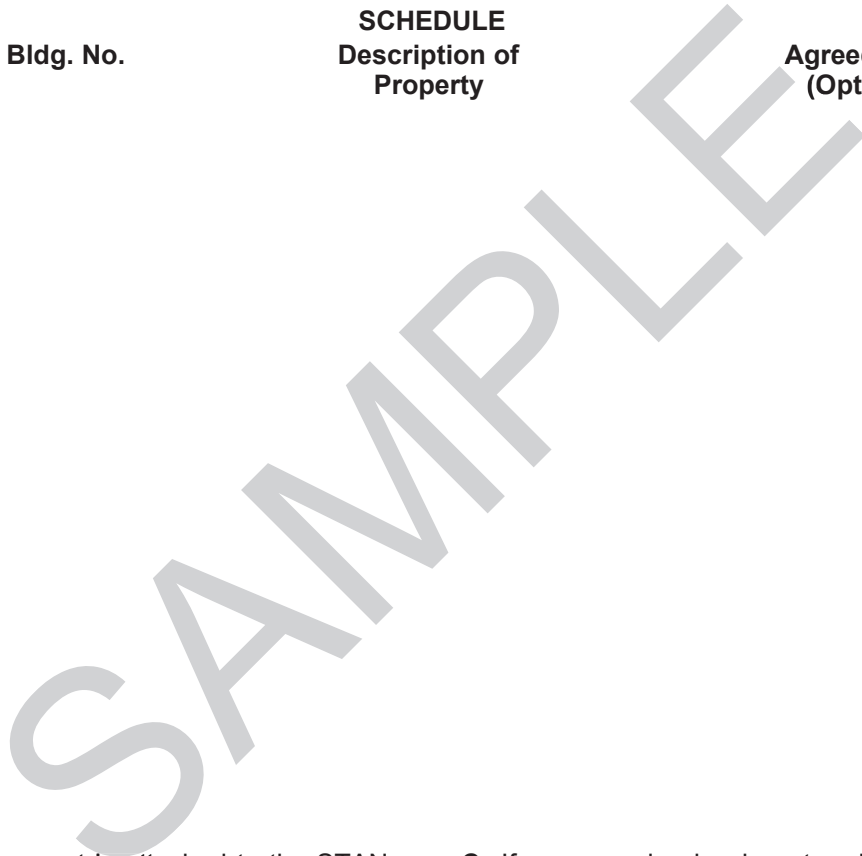
THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

LEASED PROPERTY

This endorsement modifies insurance provided under the following:

- BUILDING AND PERSONAL PROPERTY COVERAGE FORM
- CONDOMINIUM ASSOCIATION COVERAGE FORM
- CONDOMINIUM COMMERCIAL UNIT-OWNERS COVERAGE FORM
- STANDARD PROPERTY POLICY

Premises No.	Bldg. No.	SCHEDULE Description of Property	Agreed Value (Optional)
--------------	-----------	--	----------------------------



- A.** When this endorsement is attached to the STANDARD PROPERTY POLICY CP 00 99 the term Coverage Part in this endorsement is replaced by the term Policy.
- B.** Your Business Personal Property is revised to include personal property of others in your care, custody or control under written leases, as described in the Schedule or in the Declarations.
- C.** If an agreed value is entered for property in the Schedule or in the Declarations, this amount will be considered to be the value of the described property at the time of loss or damage. But this does not otherwise alter the application of the Coinsurance condition.
- D.** Property described in the Schedule or in the Declarations is not included under any Personal Property of Others coverage in this Coverage Part.



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Section 3

Future of the Deal in M&A/Understanding Governance, Risk & Compliance



FUTURE OF THE DEAL IN M&A/ UNDERSTANDING GOVERNANCE, RISK & COMPLIANCE



Presented by:
Lance J. Ewing, CRM, ARM, ERMP



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FUTURE OF THE DEAL IN M&A




Lance J. Ewing, CRM, ARM, ERMP



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The views and opinions expressed during this presentation are the views and opinions of the speaker(s) only, and **do not reflect the views, opinions, and/or any policies of their offices, companies or firms.**




3

What to Expect Knowledge Goals

- Know how risk management integrates into the M&A process
- Know who is on the due diligence team
- Identify true insurance acquisition risks
- Employ a M&A risk management checklist (partial)

THIS SESSION IS AUDIENCE INTERACTIVE!



4

The Landscape Has Changed

For 2022 **ALL** M&A deals were valued at over \$2.8T.

Domestically, manufacturing, technology and financial industries accounted for the largest share of deal volume, followed by energy and healthcare.

Companies now are typically in M&A deals solely to increase their market share, new geography expansion and improve shareholder value/return.

M&A deals today are resulting in two companies consolidating to form an entirely new company; the complete dissolution of one company after it is bought by another; or a company simply operating under the umbrella of the new parent company.



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M&A 2022

- Oracle's acquisition of Cerner for \$28.3B.
- Prologis' merger with Duke Realty for \$26B .
- Elon Musk's acquisition of Twitter for \$44B.
- Broadcom acquisition of VMware for \$61B.
- Microsoft acquisition of Activision Blizzard for \$68.7B.

In 2022, there were 314 merger and acquisitions (M&A) transactions valued at more than one billion U.S. dollars in the United States.

The overall number of M&A deals in the 12 months ending December 31, 2022 amounted to 18,072.



6

What is a Merger

A merger is the voluntary fusion of two companies on broadly equal terms into one new legal entity. The firms that agree to merge are normally equal in terms of size, customers, scale of operations, etc. For this reason, the term "merger of equals" is sometimes used.

There are 5 Types of Mergers:

- Vertical
- Horizontal
- Conglomerate
- Congeneric
- Market Extension



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What is a Merger

Vertical:

When two companies that produce parts or services for a specific finished product merge, the union is referred to as a vertical merger.

Vertical merger occurs when two companies operating at different levels within the same industry's supply chain combine their operations. Such mergers are done to increase synergies achieved through the cost reduction which results from merging with one or more supply companies.

One of the most well-known examples of a vertical merger took place in 2000 when internet provider America Online (AOL) combined with media conglomerate Time Warner.

[AOL Time Warner](#)

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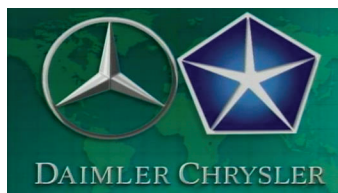
What is a Merger

Horizontal:

A horizontal merger occurs between companies operating in the same industry.

The merger is typically part of consolidation between two or more competitors offering the same products or services. Such mergers are common in industries with fewer firms, and the goal is to create a larger business with greater market share and economies of scale since competition among fewer companies tends to be higher.

The 1998 merger of Daimler-Benz and Chrysler is considered a horizontal merger.



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What is a Merger

Conglomerate:

This is a merger between two or more companies engaged in unrelated business activities.

The firms may operate in different industries or different geographical regions.

A **pure** conglomerate involves two firms that have nothing in common. A **mixed** conglomerate, on the other hand, takes place between organizations that, while operating in unrelated business activities, are actually trying to gain product or market extensions through the merger.

A conglomerate merger was formed when The Walt Disney Company merged with the American Broadcasting Company (ABC) in 1995.



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What is a Merger

Congeneric:

A congeneric merger is also known as a **Product Extension merger**.

It occurs when two or more companies operate in the same market or sector with overlapping factors, such as technology, marketing, production processes, research and development (R&D), join to form a new business entity.

A product extension merger is achieved when a new product line from one company is added to an existing product line of the other company.

An example of a congeneric merger is Citigroup's 1998 union with Travelers Insurance, two companies with complementing products.



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What is a Merger

Market Extension:

This type of merger occurs between companies that sell the same products but compete in different markets.

Typically, market extension mergers involve two companies which operate in different geographic regions.

Extension merger strategies include rebranding, price discounting and seeking new markets.

Companies that engage in a market extension merger seek to gain access to a bigger market and, thus, a bigger client base.

To extend their markets, Eagle Bancshares and RBC Centura merged in 2002.



12

What is an Acquisition

An acquisition is when one company purchases most or all of another company's shares in order to take control. An acquisition occurs when a buying company obtains **more than 50% ownership** in a target company. As part of the exchange, the acquiring company often purchases the target company's stock and other assets, which allows the acquiring company to make decisions regarding the newly acquired assets without the approval of the target company's shareholders.

There are 2 Types of Acquisitions:

- Friendly
- Hostile



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What is an Acquisition

Friendly:

Friendly acquisitions often work towards a mutual benefit for both the acquiring and target companies.

The companies develop strategies to ensure that the acquiring company purchases the appropriate assets, including the review of financial statements and other valuations, and that the purchase accounts for any obligations that may come with the assets.

Once both parties agree to the terms and meet any legal stipulations, the purchase normally proceeds.

It is important to understand that a friendly acquisition is NOT always about making money (growth first then profitability).



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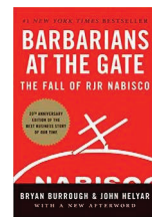
What is an Acquisition

Hostile:

Unfriendly acquisitions, commonly referred to as **hostile takeovers**, occur when the target company does not consent to the acquisition.

In this case, the acquiring company must gather a majority stake to force the acquisition. To acquire the necessary stake, the acquiring company can produce a tender offer calculated to inspire current shareholders to sell their holdings in exchange for an above-market-value price.

An acquisition is considered hostile if the target company's board rejects the offer, and if the bidder continues to pursue it, or the bidder makes the offer directly after having announced its firm intention to make an offer.



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What is a Divestiture

Corporate divestiture is a strategy to remove some of a group's assets under its current business portfolio. A divestiture most commonly results from a management decision to cease operating a business unit because it is not part of a core competency. However, it may also occur if a business unit is deemed to be redundant after a merger or acquisition, if the disposal of a unit increases the resale value of the firm, or if a court requires the sale of a business unit to improve market competition.

There are 3 Types of Divestitures:

- Carve-Out
- Spin-Off
- Split-Off



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What is a Divestiture

Carve-Out:

A carve-out is the partial divestiture of a business unit in which a parent company sells minority interest of a child company to outside investors.

A company undertaking a carve-out is not selling a business unit outright but, instead, is selling an equity stake in that business or spinning the business off on its own while retaining an equity stake.

A carve-out allows a company to capitalize on a business segment that may not be part of its core operations.



3Com's 20 percent carve-out of Palm

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What is a Divestiture

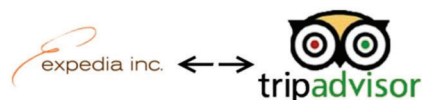
Spin-Off:

A spinoff is the creation of an independent company through the sale or distribution of new shares of an existing business or division of a parent company.

The spun-off companies are expected to be worth more as independent entities than as parts of a larger business.

A spinoff retains its assets, employees, and intellectual property from the parent company.

A corporation creates a spinoff by distributing 100% of its ownership interest in that business unit as a stock dividend to existing shareholders.



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What is a Divestiture

Split-Off:

A split-off is a method of reorganizing an existing corporate structure where shares of a business division, subsidiary or newly affiliated company are transferred to stockholders in exchange for stocks of the parent company.

A company will pursue a split-off when it wishes to create a distinction between the core business and new brand.

The benefit of a split-off for the parent company is akin to a stock buyback. Instead of purchasing stocks in cash, the larger corporation uses shares of the subsidiary company to reduce outstanding shares.

eBay turning PayPal public in 2014



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What is a Joint Venture

A Joint Venture (aka JV) is a business entity created by two or more companies, generally characterized by shared ownership, shared returns and risks, as well as shared governance.

Companies typically pursue joint ventures for one of four reasons:

- to access a new market(s), particularly emerging markets
- to gain scale efficiencies by combining assets and operations
- to share risk for major investments or projects
- to access skills, resources, brand or human capital



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Red Flags In M&A

Corporate governance questions for M&A

Results Inconsistent with Industry Peers. If a company's financial performance is much better than that of its industry peers with similar operations, something is likely to be awry. Even if the company's financial representations are legitimate, this may be a sign that the target's management, business model or strategy is highly unusual, even unparalleled. This could make it very difficult to reproduce the company's success under a different management or operational structure.

Improbable Financial Statement Changes. Financial statements should be presented according to generally accepted accounting principles (GAAP) and be consistent with industry norms. Red Flags would be unusual balance sheet changes or trend reversals, such as receivables growing faster than revenues.



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Red Flags In M&A

Corporate governance questions for M&A

Complex Business Models. Overly complex organizational structures involving unusual legal entities, numerous managerial lines of authority or contractual arrangements without apparent business purposes are all red flags. Simple reporting structures and legal entities are usually best.

Financial Accounting. Remember, financially distressed businesses under threat of bankruptcy or foreclosure face enormous temptation to cook the books and occasionally they succumb. Therefore, financially troubled entities warrant an extra level of scrutiny.

Suppliers and Customers. What entities are providing the goods and services to the target company? Examination of the contracts and agreements should be done with care. Similarly, who is the main customer or customers and what agreements are in place.



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Financial Minefields

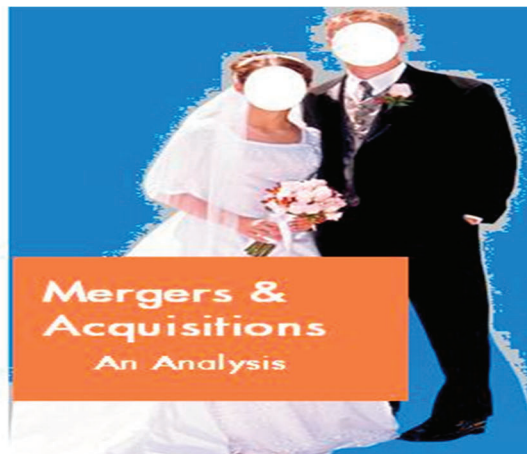
Corporate governance questions for M&A

- Risk fraught off-balance sheet financial instruments
- Insufficient or missing provisions and notes
- Stressed or too much liquidity
- Unrealistic financial planning assumptions
- Overvaluation or undervaluation of assets
- Loss of orders due to expiring contracts or product life cycles
- Outstanding litigation settlements
- Unexplained large increase in inventory
- Management bonuses related to year-end profit
- Uncollected receivables
- Unusual amount of professional fees



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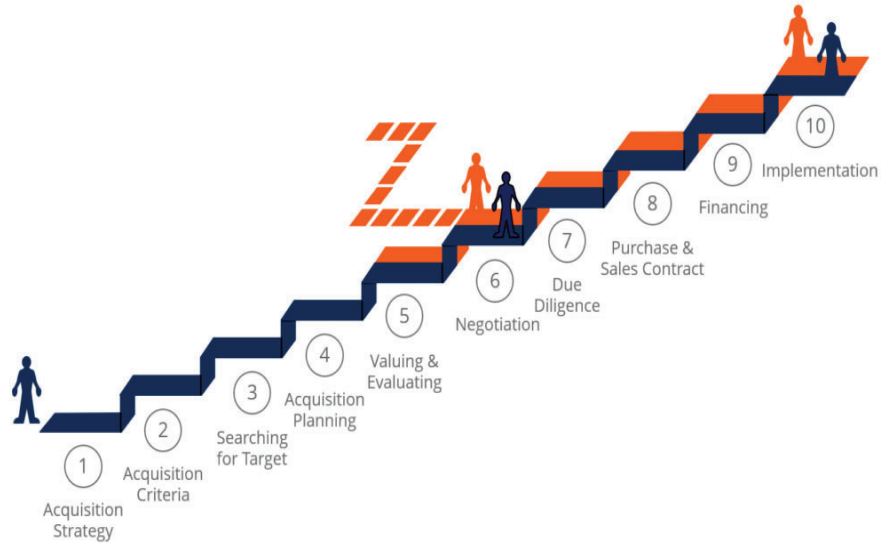
The M&A Process



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The M&A Process



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The M&A Process

Cultivate an acquisition strategy.

Developing a good acquisition strategy revolves around the acquirer having a clear idea of what they expect to gain from making the acquisition. Business purpose (e.g., expand product lines, take out competition or gain access to new markets)

Set the M&A search criteria.

Determining the key criteria for identifying potential target companies (e.g., profit margins, geographic location, or customer base)

Search for potential acquisition targets.

The acquirer uses their identified search criteria to look for and then evaluate potential target companies



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The M&A Process

Begin acquisition planning.

The acquirer makes contact with one or more companies that meet its search criteria and appear to offer good value. The purpose of initial conversations is to get more information and to see how amenable to a merger or acquisition the target company may be or if there is the potential for another type of transaction (divestiture, JV, etc.)

Perform valuation analysis.

Assuming initial conversations are positive, the acquirer asks the target company to provide initial information (current financials) that will enable the acquirer to further evaluate the target, both as a business on its own and as a suitable acquisition target.



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The M&A Process

Negotiations.

After producing several valuation models of the target company, the acquirer should have sufficient information to enable it to construct a reasonable offer. Once the initial offer has been presented, the two companies negotiate terms in more detail. Enter the lawyers and financial experts.

M&A due diligence.

Due diligence is a comprehensive process that begins when the initial offer has been accepted. Due diligence aims to confirm or correct the acquirer's assessment of the value of the target company by conducting a detailed examination and analysis of every aspect of the target company's operations (financial metrics, assets and liabilities, customers, human resources, etc.)



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The M&A Process

Purchase and sale contracts.

Assuming due diligence is completed with no major problems or concerns arising, the next step forward is executing a final contract. The parties will make a final decisions on the type of purchase agreement (e.g. asset purchase or share purchase)

Financing strategy for the acquisition.

The acquirer will have explored financing options for the deal earlier, but the details of financing come together after the purchase and sale agreement has been signed.

Closing and integration of the acquisition.

The acquisition deal closes, and management teams of the target and acquirer work together on the process of merging the two companies. The MOST important part of the M&A.



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The Due Diligence Team

- a. Financial reporting and accounting
- b. Risk Management
- c. IT
- d. Human Resources/Benefits
- e. Environmental, Health & Safety
- f. Operational/Business
- g. Legal
- h. Sales
- i. Actuarial
- j. Tax/Audit
- k. Outside Experts



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Qualities of the Team

- Expertise in their area of specialty (internal or external)
- Collaborative and candid (egos and emotions at the door)
- Leadership skills (Main leader and co-leader/Clean room/Virtual room leader)
- Works well under timelines and action plans (most of which are unreasonable)
- Multi-taskers/Pressure lovers
- Both written and oral communications skilled
- Ethical integrity
- Expecting of the unexpected



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Risk Management & Insurance in M&A

CURRENT CARRIER MARKET

Prolonged Low Interest Rate Environment
Highly Competitive Landscape
Soft Market
Higher Growth Rates in Emerging Markets (e.g. cyber)
Strong Cash Positions/Excess Capital
Reinsurance Flush
Foreign Buyers
Private Equity Buyers

Would indicate ripe opportunity for M&A

*Apollo Management buys Aspen
Hartford buys Navigators
AIG buys Validus*



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Risk Management & Insurance in M&A

CURRENT BROKER MARKET

- Price Conscious & Driven Clients (Lower Fees)
- Highly Competitive Landscape
- Margins Lower
- Quality Talent Race
- Strong Cash Positions/Excess Capital
- Stakeholders Want Return
- Foreign Brokerage
- Private Equity Investors

Would indicate ripe opportunity for M&A

- Marsh buys JLT AND Wortham*
- Brown & Brown buys Hays*
- Alliant buys Crystal*
- Epic buys Interpro*



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- With an estimated **30,000** brokerage and insurance services businesses in the United States, the insurance distribution segment is highly fragmented and continues to be ripe for further consolidation.
- 400,000** brokerage employees are expected to retire within the next several years.
- An estimated **25** percent of agents in the industry are expected to retire in 2018. A workforce concentrated in an older age group could be subject to succession challenges if many in the group retire in a short period of time.
- Private equity (PE)-backed acquisitions will continue in the insurance brokerage and insurance-service sectors in the foreseeable future.
- During the past decade, more than **3,300** businesses were traded as part of a wave of M&A deals with significant involvement from PE-backed businesses.
- Leading acquirers develop a detailed operations model and value creation plan for the target in diligence. With acquisition multiples at record highs, acquirers cannot afford to have operating cost leakage postacquisition.
- The question of whether to buy or build comes down to an investor's general investment thesis and investment parameters, consideration of a time horizon, and operational expertise.
- PE firms "dry powder" stands at roughly **\$1** trillion, according to Preqin, creating a situation where demand for attractive investments remains strong, and insurance brokerage investments have historically been strong performers for the majority of PE firms who have been involved in the industry.

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Legal Outlook for M&A

The basis for most M&A lawsuits typically allege that the target company's board of directors violated their fiduciary duties, with failure to discuss material information or through accepting an inadequate price or accepting a price reached via an inadequate process.

Of all deals valued at over \$100 million they resulted in 73% being litigated with at least one lawsuit. Lawsuits are normally filed within 48 days after the deal is announced. The average number of lawsuits per M&A deal is currently 2.8 suits filed. More than 74% of merger objection litigation was resolved before the deal closed. More M&A cases are being filed in Federal v. State courts.

Costs associated with the types of M&A lawsuits continue to increase. Merger objection litigation remains a significant problem for companies engaging in M&A transactions, and for their insurers.



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Audience Interactive Time

How many have been through an M&A?

How many have been through and M&A with a Client



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The Insurance Side of M&A

A thorough risk and insurance diligence exercise can/should include reviews of:

Insurable Exposures and offsetting policies (efficacy and cost differentials)

Reserves and Collateral for US Casualty (GAAP Compliance AND forecasting)

Contracts/Supply Agreements/P.O.s (Compliance and outliers)

Historical Financials (10Q/K) and Balance Sheets: Are there large reserves for liabilities beyond casualty forecasts? What are they?

Draft Purchase Agreement (BEYOND Indemnity wording. There MUST be a clear understanding of intent for insurable liabilities)

Benefits compliance

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The Insurance Side of M&A

What insurance related problems cause a deal to fail?

Standard

Uninsured/Underinsured losses

Eroded limits

Insolvent or financially unstable carriers on target company panel

Non-Standard

Tax Uncertainty

Gap in indemnity negotiation

Mass tort

Large reserves for self insured losses tipping deal value

Potential unrealized liabilities (Binary)



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The Insurance Side of M&A

Markets have recently offered risk transfer for various other “deal break” items, including:

The insurance marketplace is getting more and more entrepreneurial.



Mass Liability for chronic illness conditions (asbestos/silicosis, etc.)

Known Toxic Tort (BI/PD)

Compliance with Law or Regulation

Securities Claims

IBNR for warranty/product/cyber liability



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The Insurance Side of M&A

There is a boom in capacity in the non-standard risk insurance marketplace (hedge funds)

- Domestic, Bermuda, London/Europe
- Creating opportunities to offer real risk transfer for previously uninsurable or cost prohibitive issues
- **The change in what we call “transactional risk”**
 - Reps & Warranties is now considered a mainstream product for acquirers of all sizes. Pricing is stable and commoditized, and forms are broad
 - Tax Liability has also broadened
 - REITs



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The Insurance Side of M&A

Coverage Highlights	
Two Types of Policies	<ul style="list-style-type: none"> • Buyer-Side Policy • Seller-Side Policy
Amount of Coverage	<ul style="list-style-type: none"> • Up to \$750 million+ for any one transaction; dramatic increase in market capacity in last 24- 36 months (RLI, Everest, QBE, Liberty Mutual, XL, Starr, Swiss RE, Allianz, Hanover, Argo, AIG, etc.) • 21 carriers writing in total domestically
Price of Coverage	<ul style="list-style-type: none"> • Generally 2.5% to 4% of the limit of liability for US, 1-2.5% for non-US
Policy Period	<ul style="list-style-type: none"> • Typically matches survival in underlying agreement • Can be extended beyond survival in underlying agreement up to as long as a 7 year term
Process	<ul style="list-style-type: none"> • Start to finish in 10 to 15 business days • No cost to obtain Non-Binding Indication Letter (NBIL) • Can be expedited on case by case basis



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The Insurance Side of M&A

Why buyers request coverage

- ➔ Enhance amount/duration of indemnity
- ➔ Distinguish bid in auction
- ➔ Ameliorate collection concerns
- ➔ Protect key relationships
- ➔ Reduce Tension with post-closing Management (who is also Seller) in the event of a breach
- ➔ Insure certainty of purchase price
- ➔ Address stakeholder concerns



Why sellers request coverage

- ➔ Distribute sale proceeds on an expedited basis
- ➔ Protect sale price
- ➔ Supplement disclosure process
- ➔ Protect passive sellers
- ➔ Increase cooperation with Buyer in the event of a breach
- ➔ Reduce contingent liabilities
- ➔ Address stakeholder concerns



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The Insurance Side of M&A

Price of Coverage: Generally 4% to 7% of the limited liability (depending upon the scope of risk)

Policy Period: Up to Seven (7) years

Scope of Coverage:

- Additional tax
- Additional taxes due to certain claims payments
- Interest & penalties imposed on additional tax
- Defense costs (certain instances)
- Available for US and non-US risks
- Limits are case by case (minimum average \$5-10M USD & maximum \$350-400M USD)
- Deductible and retention are case by case



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The Insurance Side of M&A

Environmental Coverage

Risk transfer related to transactional environmental liabilities is widely available, and is one of the oldest areas of insurable transactional risk.

- A VERY large marketplace exists, allowing buyers access to wide coverage forms at relatively low cost
- Multi-year programs as long as 10 year can be obtained for pre-existing unknown conditions or 5-7 years going forward (depending upon the nature of the risk)
- Programs can be heavily manuscripted (Buyer Friendly)
- Toxic Tort for known conditions, redevelopment exclusion removal, etc.



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M&A Checklist (Partial)

Your role in M&A Due Diligence as a risk professional BEFORE the Deal closes

Partial Checklist

- Create schedule of insurance
- Occurrence versus claims-made policies (3-5 years historical data)
- Exclusions or gaps in coverage
- Inconsistencies between primary and excess policies
- Determine ownership of policies (in some deals the buyer gets the originals and in others the buyer ONLY gets copies)

Insurer contracts – agreements

- a. Collateral trust, LOCs, escrows
- b. Retrospectively rated plans
- c. SIR (self-insured retention) financial requirements
- d. Deductible – per occurrence and aggregate



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M&A Checklist (Partial)

Partial Checklist

Property/casualty issues

- a. Projection of claim costs
- b. Premium calculations – short rate calculations
- c. Cash flow analysis – funded claims adequate
- d. Collateral
- e. Service costs
- f. Transfer costs
- g. TPA contract and fees



Material on captives (loans/investments/dividends/officers/by-laws)
International exposures



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M&A Checklist (Partial)

Partial Checklist

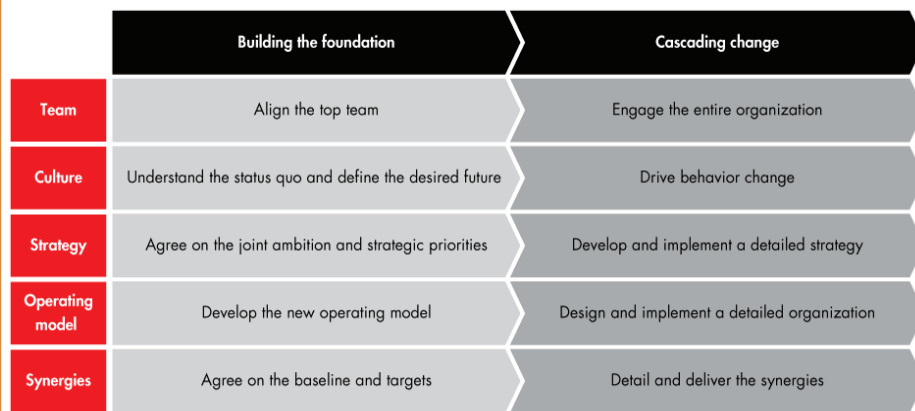
- OSHA, EPA, EEOC, ADA, SEC, DOJ citations, litigation, responses due, fines
- Capital expenditures in process or under contract
- Last 3 -5 years facility closures
- Discontinued products, services, operations
- Successor liabilities from previous acquisitions or consolidations
- Contractual obligations
- Appraisals
- A.M. Best ratings and any insurer insolvencies
- Total cost of risk report (TCOR)
- Risk appetite: retrospectively rated programs, SIRs, deductibles, collateral requirements
- Cash flow to fund claims within deductible or SIR
- Experience modifier history



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The M&A Aftermath

Figure 1: Merger integration requires establishing a foundation and cascading change in five critical areas



Source: Bain & Company

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The M&A Aftermath

Your role in M&A Due Diligence as a risk professional AFTER the Deal closes

When the dust settles NEWCO's risk priorities will have changed:

- Risk appetites
- Risk tolerances
- Brokers, Carriers, TPAs, Service Providers
- Financial (liquidity, cash flow, budgeting)
- Retentions and limits
- Valuations (divestitures and spinoffs)
- Business interruption
- Employee (risk management department, new faces and reporting structures)
- Corporate Culture



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The M&A Aftermath

When the dust settles NEWCO's risk priorities will have changed:

- Employee Benefits
- Morale
- Competition (Sales & Marketing)
- Product(s)
- Customers
- Shareholders (Institutional Investors)
- Regulatory Requirements
- Risk Management Team



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UNDERSTANDING GOVERNANCE, RISK & COMPLIANCE



Lance J. Ewing, CRM, ARM, ERMP



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2

What to Expect Knowledge Goals

- Increase understanding of governance, risk management, compliance (internal audit) & ethics
- Establish a connection between governance, risk management and compliance
- Discuss what skills and attributes are needed to partner with or take on these areas of responsibility



3

The Landscape Has Changed

- Risk Appetite – A Risk Appetite Framework (RAF) encompassing all risks and the resulting Risk Appetite Statement (RAS)
- Risk Compliance – Particularly “conduct risk”, adherence to P&P, ethical standards, fairness and disclosure
- Reputational Risk – Assessing the impact of potential reputational damage on returns, market share
- Capital Allocation – Measuring capital at risk and how risks are linked
- Risk Culture – Shifting accountability to the front office and line
- Stress Testing – Looking at the potential impact of possible events, inter-relationships, on the overall portfolio
- Operational Risk – Fraud, Fines, Business Ethics, etc.
- Risk Technology/Architecture/Cyber-security – improved risk information, reporting, data and analysis; and stronger cyber security and anti-hacking measures (**GROWING AND MAY BE MOST IMPORTANT**)



4

Corporate Governance

Corporate Governance is defined as a set of systems, processes and principles which ensure that a company is governed in the best interest of all stakeholders.

- It is the system by which companies are directed and controlled.
- It is about promoting corporate fairness, transparency and accountability.
- It ensures:
 - Disclosures and effective decision making to achieve objectives;
 - Transparency in business transactions;
 - Statutory and legal compliances;
 - Protection of shareholder interests;
 - Commitment to values and ethical conduct of business.



5



6

The Golden Rules of Corporate Governance



Ethics Above Everything



Align Our Business Goals



Perform Strategic Management



Organize Regularly



Report Honestly



7

Global Governance

Corporate governance practices around the world are surprisingly diverse.

- Differences partly reflect the size, sectors of activity, and lifecycle of companies.
- The nation state is still the main driver of corporate governance variations. For example, multinational corporations like Toyota, VW, and Ford are engaged in broadly similar economic tasks (manufacture and distribution of automobiles.) However, their activities are subject to entirely differing frameworks of monitoring, oversight and control due to the governance of their countries of incorporation.
- This is not to say that global market forces do not have an impact on governance practices. Large publicly traded firms around the world increasingly conform to international standards of corporate governance “best practice”. Set by organizations such as the EU and the International Accounting Standards Board. Such behavior helps them to convince capital market investors and gain access to external finance at the lowest possible cost.



8

Corporate Risk Management

Corporate Risk is really Enterprise Risk Management (ERM) within GRC. ERM is defined as a holistic approach to identifying, defining, quantifying, and treating all of the risks facing an organization, whether insurable or not.

- Creates a more risk focused culture for the organization.
- Standardizes risk reporting (Risk Register).
- Improves board and shareholder concentration on risk.
- Efficient financial use of corporate resources (use of capital).
- Identifies upside and downside risk.
- Effective coordination of regulatory and compliance.



9



10

ENTERPRISE RISK MANAGEMENT

Enterprise risk management (ERM) is the capability of an organization to understand, control, and articulate the nature and level of the risks taken in pursuit of a risk adjusted return. The risks can be categorized as Credit, Liquidity, Strategic / Business / Reputation, Market, Operational, Compliance / Legal, Financial, and Capital Adequacy.

What Is ERM? It is the capability to effectively answer the following questions:



- Circular depiction is highly intentional
- Components are meant to be dynamic (reviewed back/forth in any sequence)
- Having the right culture is key

11

Corporate Compliance

Corporate Compliance in simple terms, is the process of assuring a company and their employees follow the laws, regulations, standards, and ethical practices that apply to the organization.

- Obeys laws & industry regulations (internal & external audit).
- Follow corporate rules, policies, procedures and ethics.
- Protect corporate reputation.
- Reduce legal risks and future litigation.
- Increase employee retention and talent attraction.



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Legal Compliance

Legislation is enacted at various levels – state, federal, etc. – and it may affect the organization, depending on the type of business transactions they perform and the types of data they collect, process and store. Additional legislation is introduced as risks continue to evolve.



- Gramm Leach Bliley**
- Data Security Breach Notification**
- Fair & Accurate Credit Transactions Act of 2003 (FACTA)**
- Health Insurance Portability & Accountability Act of (HIPAA)**

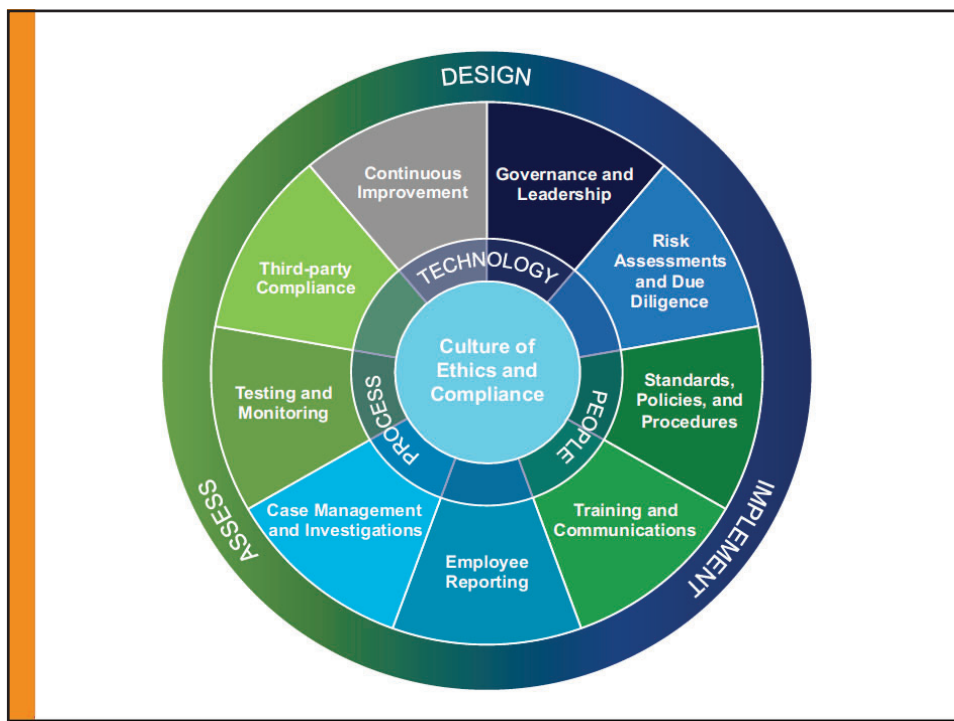


13

Simplify Corporate Compliance



14



15

Questions

If the business is in a highly regulated industry such as healthcare, legal, finance, education or insurance, the compliance program and audit procedures are held at a higher level. However, most small businesses with diligence can manage compliance requirements.

- **High-risk violations.** Which violations could close my business, risk the safety of employees or customers, might lead to litigation or could violate insurance requirements?
- **Profit and revenue.** What could cause me to lose business, lose customers or vendors? Are some low-risk compliance issues more costly to maintain than they could be?
- **Changing regulations.** How often do you update your policies or check for new regulations? Are you on the proper email lists to receive updated industry information?
- **Company culture and branding.** Do the current standards support how you want your customers to see your business? Do your employees fully understand what your branding is?
- **Training.** Do you need to conduct training more or less often? What kind of compliance training requires ongoing training? Do you need to post more information? Are your vendors and service providers well informed of your expectations?

See Appendix



16

What is “Business Ethics”

1. Knowing what is right or wrong in the workplace and then doing what is right
2. Fundamental ground rules of our work lives
3. The process of instilling into a company’s workforce a sense of how to responsibly conduct business
4. Keeping the company moral compass true in business dealings



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Benefits of GRC

1. Eliminate Redundancies and Eliminate Redundancies
2. Reputation Risk
3. Preventing Handcuffs and Jail
4. Single Version of Truth (SVOT) a **single** centralized database which stores all of an organization's data in a consistent and non-redundant form.



18

GRC Is Built on Ethics

Managing ethical behavior for GRC in the workplace is a **top-down process**.

The organization's ethical behavior begins inside the office of the organization's **highest ranking** officer and flows down through every manager to every employee regardless of that employee's hierarchal status or position.



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TWO QUESTIONS

Question 1: If you knew a woman who was thinking of becoming pregnant, who had seven children, three who were deaf, two who were blind, one with severe psychological issues, and one who died still born. She herself had tuberculosis and was on the brink of financial desolation. **Would you recommend that she not become pregnant?**

Question 2: It is time to elect a world leader and **you will cast the deciding vote**. Here are the facts about the three candidates:

Candidate A: Associates with crooked politicians and consults with psychics. He's had at least one mistress. He also chain smokes and drinks up to ten Martinis a day. He is viewed as patriotic.

Candidate B: He was ejected from office twice, stays in bed until noon, used drugs while traveling in college and drinks several shots of whisky every evening. He appears calm in a crisis.

Candidate C: Is a decorated war hero. He's healthy (mostly vegetarian), who doesn't smoke, drinks an occasional beer and hasn't had any extra-marital affairs. Has been recognized to have leadership skills and a gifted orator.

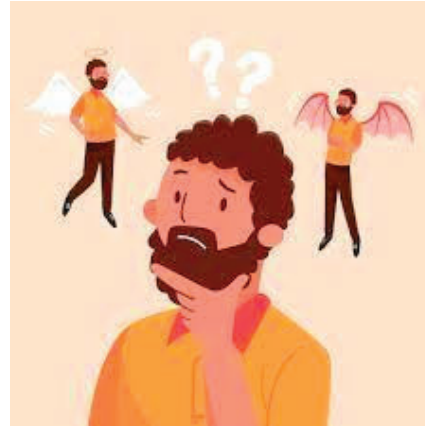
Which of these candidates would be your choice?



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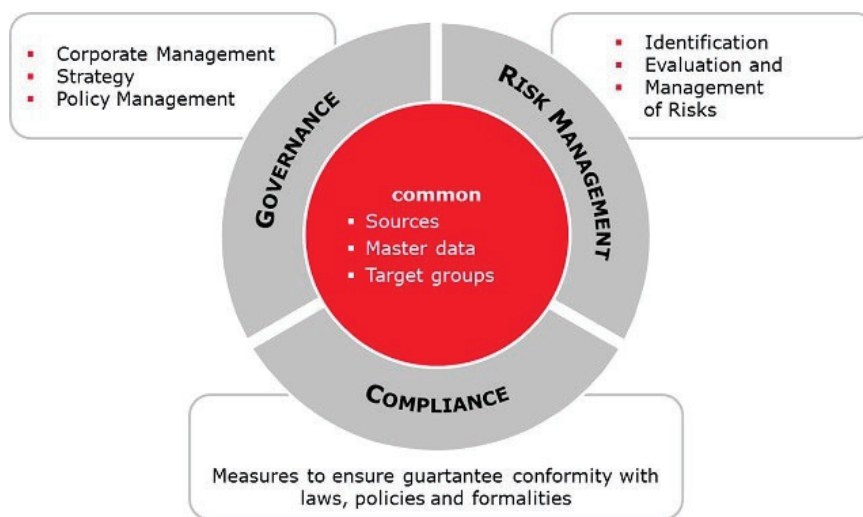
GRC Ethics

1. Code of Conduct
2. T&E
3. Values & Behavior
4. Social Responsibilities
5. Conflicts of Interest



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GRC Components



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GRC Components

GRC Leader and Committee

- CRO
- Chairman
- CEO
- Outside Director

* Silicon Valley Bank had no official chief risk officer for 8 months while the VC market was spiraling

Committee Membership

- CFO
- COO
- CIO
- Internal Audit
- Risk Management
- Compliance
- Board Member (Risk Committee)
- Ad hoc Participants

* Chief risk officer who blew the whistle awarded over £130k following unfair dismissal

* Fired Chief Compliance Officer accused of stealing \$480K, attempted to conceal scheme

** Hand-out



25

GRC Components

Communications

Deliver targeted communication and share GRC information with company business units, global functions, external partners, regulators, customers, vendors, and other stakeholder groups.

- Board
- Institutional Investors
- Shareholders
- Executive Management
- Company Wide

The single biggest problem in communication is the illusion that it has taken place.

– George Bernard Shaw



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GRC Components

Training

Deliver targeted training on GRC with Board members, Executive Committee, Select Company Business Units and other stakeholder groups.

Training should include but not be limited to:

- Defining the GRC framework
- Incorporating company policies to the IT platform
- Scoping the organization for ERM and applying policies
- Using the GRC process to draft, review, approve, publish, and retire policies
- Creating controls and reviewing controls
- Defining and applying GRC indicators
- Creating a test template
- Managing internal and external audit engagements
- GRC reporting dashboards



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GRC Components

Prevention

Risk control is inherent within GRC:

- IT
- Fraud
- Supply chain
- BCP & Process Continuity



Internal Audit

IA provides assurance and consulting to management, the board and other stakeholders that the organization is achieving objectives, addressing uncertainty and acting with integrity.

- Evaluate material risks and weaknesses
- Assess controls and accuracy
- Independent
- Promote ethics



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GRC Components

Enforcement & Discipline

In order to encourage employees to raise concerns regarding ethics and compliance, employees have to believe the system for investigating such violations and meting out discipline is fair and even-handed. If managers and employees perceive a disciplinary system as discriminatory, the company culture will suffer significant harm.

Discipline must also be swift. Companies have to commit to conducting a fair and timely investigation within a few months.

Finally, the company has to reiterate its commitment to protect the employee who raised the concern from any retaliation. This is just as important in a situation where the complaint was found to be without merit as it is when a complaint results in discipline against an offender.

NOTE: Regulatory, Federal, State or International authorities may mete out their own enforcement & discipline.



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Risk Management & Insurance



Risks & Controls

- Risk Identification
- Threats
- Vulnerabilities & Weaknesses (material)
- Deterrents (internal-external)
- Controls (internal-external)
- Impacts-Models-Risk Register-Dashboard
- Software



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Risk Management & Insurance

GRC Focused Types of Insurance Coverage

- Casualty (third party)
- Executive Liability
- Crime, Fiduciary
- EPL
- E&O
- Cyber-Privacy
- Employee Benefits
- M&A
- Others?



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Risk Management & Insurance

GRC Underwriting

Underwriters should be looking for companies and entities that are best in class for:

- Compliance
- Financial Reporting
- Operational Efficiency
- Performance Reporting
- Asset and IT Protection and Prevention
- Risk Management (Project and Enterprise)
- Risk Tolerance
- Risk Based Decision Making



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The Chief Risk Officer

Standard definition of the role:

CRO is responsible for the firm's risk management operations, including managing, identifying, evaluating, reporting and overseeing the firm's risks externally and internally to the organization. The CRO's responsibilities will vary depending on the size of the organization and industry.

- Salaries for a Chief Risk Officer position are between **\$90,000** and **\$250,000** per year.
- Current CRO by gender is 68% male and 32% female.
- 75% of current CROs have over 15 years experience.
- CROs typically have post-graduate education in accounting, economics, legal, risk management, finance or actuarial.
- CRO designations: CPA Certified Public Accountant, CIA Certified Internal Auditor, CRMA Certification in Risk Management Assurance, CCRO Certified Chief Risk Officer



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The Chief Risk Officer

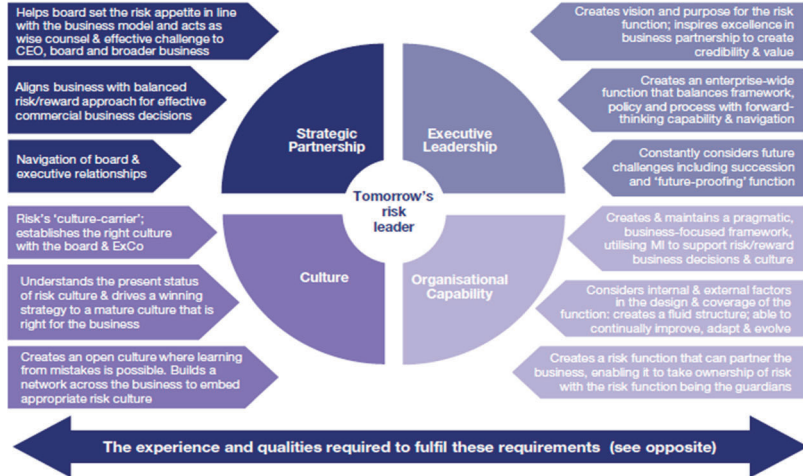
Financial institution CROs have higher requirements to meet for their roles (most banks, insurance companies, investment firms, etc. are required to have a CRO)

- Chief Risk Officers have been existence for nearly 20 years.
- The role has taken time to gain traction and is still most prevalent in Finance Services, Energy and Commodity businesses.
- 2008 crisis and corporate governance changes resulting have raised the CRO profile.
- CRO's are rarely Board-level appointments. The majority are senior executives reporting to the CEO and/or Risk or Audit Committee.



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The CRO's Challenge



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What is Business Resilience?

The ability to **rapidly adapt and respond** to risks, as well as opportunities, in order to maintain continuous business operations, be a more trusted partner, and enable financial growth.

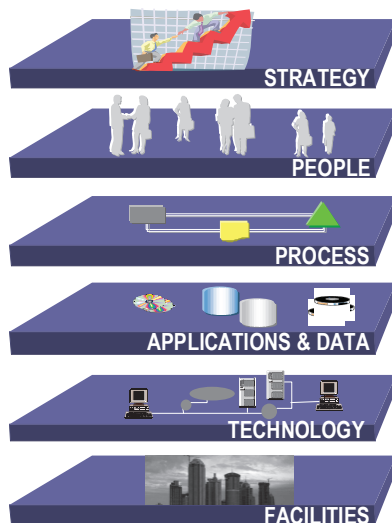
Business Resilience is about . . .

- Protecting the enterprise
- The ability to recover and adapt
- Proactive/preemptive management
- Effective management of complexity
- Rapid exploitation of opportunities
- Increasing competitive advantage



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A Holistic Approach to Risk Resilience is Required



- Recovery
- Security
- Continuity
- Availability
- Scalability



37

Challenges and the Path to Effective Risk Resiliency Management

- Balancing efficiency with resilience in the face of continuing volatility and heightened uncertainty.
- Continued growth in operations complexity and economic-induced supply/demand volatility, as well as increasing vulnerability of networks to disruptive events
- Limited visibility to vendors, networks and products across the supply chain
- Limited internal supply chain risk and resilience resources



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Risk Resiliency

Lloyd's, via Cambridge Company conducted an in depth analysis of 18 city level threats producing the "City Risk Index" to determine each city's risk resiliency.

The key trends identified by the index are:

- **Man-made threats are on the rise:** Man-made threats account for 59% of all global GDP@Risk. Financial market crash is identified as the biggest threat to the global economy, putting on average \$103B in global economic output at risk per year.
- **Climate is still a major risk driver:** Climate-related risks together account for \$123B of GDP@Risk, and this sum is expected to grow as extreme weather events become increasingly frequent and severe.
- **The majority of risk is concentrated in a few cities:** The 10 cities with the highest GDP@Risk together face \$126.8B in potential losses to economic output each year. This finding reflects the increasing concentration of wealth in certain geographic regions and, therefore, the vulnerability of the global economy to disruptive events.
- **Building resilience is an urgent priority:** The index scores each city's resilience based on criteria such as funding for emergency services and insurance levels. If every city in the index were to improve its resilience to the highest level then global GDP@Risk would decrease by as much as \$73.4B.



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Governance, Risk and Compliance (GRC) Is



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Compliance System Checklist and Insurance Underwriting Management System Manual

The purpose of this checklist is to encourage insurance companies to serve the public good and to confirm their systems for accomplishing this. It does this by re-articulating the roles that the board of directors, etc. and board of auditors, etc. are expected to play, describing the programs that will achieve compliance, seeking to make directors aware of compliance issues, and bringing about the company spirits that compliance is important for themselves. It is necessary to establish a proper insurance sales management system under which directors are aware of compliance issues and compliance-oriented corporate spirits are brought about, so that the interests of policyholders are not sacrificed in selling and concluding an insurance. Therefore, a manual to confirm such systems in specific terms on the basis of the checklist was also prepared. This checklist and manual are to be used to verify insurance-company compliance systems, including an insurance sales management system.

This checklist and manual apply to all insurance companies, including the foreign offices of Japanese insurance companies (foreign branch, foreign subsidiaries, and offices of the overseas workers, etc., though whether to include these offices in the inspection by this checklist and manual will be determined in light of applicable laws and ordinances, including applicable foreign-country laws and ordinances) and the Japan offices of foreign insurance companies.

[Notes on the use of this manual in inspections]

This manual is essentially a handbook to be used by inspectors in the inspection of insurance companies. It is expected that, as part of their efforts to ensure sound and proper operations and in accordance with the principle of self-responsibility, individual insurance companies will fully exercise their creativity and innovation to voluntarily create their own detailed manuals. These insurance company manuals should make note of the content of this manual and be adapted to the size and nature of the insurance company.

The check points in this manual represent standard to be used by inspectors in evaluating the compliance systems of insurance companies. They do not constitute direct statutory obligations to be achieved by insurance companies. Care must be taken that the manual is not adopted by rote and uniformly. If there may be cases in which the checklist description has not been fulfilled literally, by insurance company, in the light of ensuring the soundness and appropriateness of its operation only the time that the measures by insurance company are equivalent in their effects to the descriptions for the check point or are sufficient given the size and nature of the insurance company, these measures would not be deemed inappropriate.

Inspectors will therefore need to fully dialogue relevant points with insurance companies during on-site inspections.

Note: Explanation of check points

- ① Unless explicitly stated otherwise, items expressed in the question form such as “does the insurance company” or “is the insurance company” are minimum standards that are expected of all insurance companies. Inspectors, as they go through their checklists, need to fully verify the effectiveness of these items.
- ② Unless explicitly stated otherwise, items worded in the form of “it would be desirable that” constitute “best practice(sound practice)” for all insurance companies. Inspectors need only confirm these items.

Note: Distinction between “board of directors” and “board of directors, etc.”

- ① Items that are defined as roles of the “board of directors” are items for which the board of directors itself needs to determine all essential matters. This does not, however, preclude the board of directors from delegating consideration of draft documents to the management committee or similar bodies.
- ② The phrase “board of directors, etc.” includes the board of directors, the management committee, the management meeting, and similar bodies. Items that are defined as roles of the “board of directors, etc.” would ideally be determined by the board of directors itself, but may be delegated to the management committee, etc. provided that there has been a clear delegation of this authority from the board of directors, the management committee, etc. has kept minutes of its proceedings and other materials that would allow after-the-fact confirmation, and there are adequate internal checking by the measure the results are reported to the board of directors, or auditors are allowed to participate in the management committee, etc.

Note: Explanation of “business base”, “business bases”, “insurance sales”, “policyholders”

- ① The phrase “business base” refers to organizations other than the head office that constitute business bases, such as branch offices, business headquarters, foreign branch offices, and foreign subsidiaries. The phrase “business bases” refers to organizations other than the head office that do not engage in sales activities, such as operating bases, service centers, and foreign liaison offices.
- ② The phrase “insurance sales” refers to insurance agency or insurance agent and does not include insurance broker.
- ③ In this checklist and manual, the phrase “policyholders” refers to insured person, insurance beneficiaries, or person targeted in sales activities or other customers.

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
I. Arrangement and establishment of compliance structures	1. Functions of the board of directors as the body making decisions on business-execution and supervising director activities	<p>1. The responsibilities and obligations of directors for business execution</p> <p>(1) Do the directors, from the perspectives of checking and restraining arbitrary actions of the representative director in the execution of business activities, facilitating appropriate business execution and, maintaining and improving the trust of the financial institution, take active part in the decision-making process of the board of directors and in the supervision of business execution by directors?</p> <p>(2) Do the directors fulfill their obligations as good caretaker and as faith in the execution of business based on substantive discussions from the perspective of strengthening the institution's base of trust?</p> <p>(3) Does the board of directors position the formulation of corporate morals, as defined by social responsibilities, public duties, and similar considerations, as a priority task and does it erect structures to achieve this?</p> <p>(4) Does the board of directors discuss, not only ways to promote business, but also compliance issues related to the management and operation of the institution?</p>	Note: "Compliance" and "laws and ordinances" refer to compliance with internal rules and regulations in addition to the laws and ordinances listed in Section V of this checklist.
	2. Minutes of board of directors meetings	<p>2. Creation and storage of the minutes of board of directors' meeting</p> <p>(1) Are minutes of board of directors meetings kept?</p> <p>(2) Are the minutes of board of directors meetings stored for periods of time as specified by law?</p> <p>(3) Are materials of agenda created showing the issues on the board of directors' agenda?</p> <p>(4) Are the documents described in the above question stored for the same period of time as the minutes of board of directors meeting?</p> <p>(5) Do the minutes of board of directors meetings and base documents record compliance-related decisions by the representative directors, and confirm or assume verification of the status of various risks and problems related thereto, and reports of injustices and other problems?</p>	
	3. Management surveillance functions of board of auditors, etc.	<p>3. Are the auditors and board of auditors assured of their independence, do they perform effective operational audits of the directors and accounting audits, and the functions of policyholder representative displayed?</p> <p>(1) Does at least one auditor attend meetings of the board of directors when compliance issues are on the agenda? It is desirable that a full-time auditor attends such a meeting.</p> <p>(2) Is the board of auditors assured of its independence as intended by the law?</p> <p>(3) Does the board of auditors appropriately exercise the wide-ranging authority granted to it to perform operational audits in addition to accounting audits?</p> <p>Does the board of auditors have necessary and appropriate assistant staff?</p> <p>(4) Are accounting auditors used to complement the functions of the board of auditors, etc.? Does the institution use firms when necessary?</p> <p>(5) Do internal auditors understand that they are still independent structures even when there is a board of auditors, and do they actively perform audits on their own responsibility?</p> <p>(6) Are there systems in place to enable the board of auditors to check that the findings of external audits by accounting auditors are themselves appropriate and, if necessary, to take measures such as replacing accounting auditors?</p>	

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
	<p>(7) Is the board of policyholder representatives managed in accordance with laws and ordinances to fulfill its management surveillance functions properly?</p> <p>4. Check for basic compliance policies</p> <p>(1) Does the insurance company position compliance as one of its top managerial priorities? Has the board of directors formulated basic policies and standards for compliance practice?</p> <p>(2) Are all employee and insurance agents fully aware of basic policies and compliance standards? For example, are documents such as those listed below "reference" available in directors' offices, in individual business divisions, and in business bases?</p> <p>(3) Does the insurance company work in cooperation with the police and other relevant organization to take drastic measures against antisocial powers?</p> <p>(4) Do the basic policies and compliance standards articulate specific, concrete behavioral policies and standards, not just moral rules?</p> <p>Reference: "Keidanren Charter For Good Corporate" and "Keidanren Handbook Of Charter For Good Corporate Behavior" (17 December 1996) "Code of Conduct" (Life Insurance Association of Japan, 17 October 1997; Marine & Fire Insurance Association of Japan, October 1997)</p>		
	<p>5. Check for "specific actions as directors" related to compliance</p>	<p>5. Check of "director recognition"</p> <p>(1) Do the directors take the initiative in good-faith efforts to ensure compliance? Does the board of directors take responsibility for promoting strict moral and integrity standards, and for establishing a culture within the organization that emphasizes and demonstrates to all levels of employee the importance of internal controls?</p> <p>(2) Do the directors have specific programs for ensuring that employees understand compliance issues?</p> <p>① Do the representative directors use the new year's message, branch manager meetings, and other possible occasions to communicate the insurance company's efforts to ensure compliance?</p> <p>② Do directors position the compliance division on par with business divisions, ensure that it has appropriate staffing and adequate size, take an interest in its management, evaluate its results, and appropriately value its contribution in personnel evaluations?</p> <p>③ Do the directors themselves take fair, impartial, firm, rule-based attitudes towards internal and external compliance issues?</p> <p>④ Are compliance-related programs regularly evaluated?</p>	
<p>II. Formulation of compliance standards (code of conduct)</p>	<p>Check for "compliance manual"</p>	<p>(1) Has the insurance company formulated specific handbooks for compliance? (These handbooks should explain the laws and ordinances to be adhered to, and provide specific means of dealing with any illegal actions discovered. Referred to as the "compliance manual" hereinafter.) Does the board of directors approve the content of the compliance manual when it was formulated and does the board of directors approve all major revisions?</p> <p>(2) Does the compliance manual contain the matters listed in Section V of this checklist? Is the content of the compliance manual appropriate and specific, reflecting</p>	

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
<p>III. Establishment of checks to determine if compliance structures (systems) are functioning adequately</p>	<p>1. Check for “compliance program”</p>	<p>the social responsibilities and public duties of insurance companies as discussed in the “Code of Conduct” (Life Insurance Association of Japan; Marine & Fire Insurance Association of Japan) and other documents in the “Reference” materials above, and also reflecting the culture of the corporation? For example, has the insurance company formulated “compliance manuals” in accordance with the content of the duty of insurance agents?</p> <p>(3) Are all employee and insurance agents fully aware of the existence and content of the compliance manual?</p> <p>(4) Is the content of the compliance manual reviewed and revised as appropriate and necessary?</p> <p>(5) Are legal checks performed when basic policies and compliance standards are formulated and revised? Are legal checks performed when new activities are initiated or new products launched?</p> <p>1. Does the board of directors approve the content of specific programs for compliance (formulation of rules and regulations, internal control programs, employee and insurance agents training and the like, referred to as the “compliance program” hereinafter) and any major revision thereto?</p> <p>(1) Is the compliance program formulated at an appropriate timely and rationally? Is it formulated in yearly intervals at the longest?</p> <p>(2) Is there follow-up on the progresses and achievement of the compliance program?</p> <p>(3) Are the responsibilities of the division in charge of the compliance program clear? Do the representative directors and board of directors measure and evaluate programs and achievement?</p> <p>(4) In formulating the compliance program, does the insurance company take account of the size and nature of offices and does it fairly reflect implementation of the program in performance evaluations and personnel evaluations?</p>	

Item	Compliance Check Point 2. Check for "compliance environment"	Explanation of Compliance Check Points	Remarks
	<p>2. Is there a structure in place for centralized management of compliance and other legal affairs?</p> <p>(1) Have internal rules been formulated for systems to provide centralized management of compliance and other legal affairs?</p> <p>① Does the insurance company have a division to unify compliance? Does it clearly articulate the authority and role of this division?</p> <p>② Are compliance personnel stationed appropriately in each business division and office?</p> <p>③ Is a structure in place for dynamic response in the event that incidents occur?</p> <p>(2) Does the insurance company appropriately gather and manage legal information?</p> <p>① Are there clearly articulated rules for communicating, reporting, and discussion, etc. between the compliance division and business divisions and offices? Are there similar rules between business offices and insurance agents?</p> <p>② Are there ties and links between the compliance division and business division and offices? Are there ties and links between business offices and insurance agents? Is a structure in place for immediate reporting to the compliance division by compliance personnel in the event that problems are discovered?</p> <p>③ Do the competent directors have constant and accurate legal information?</p> <p>(3) Is the insurance company enhancing its compliance training structures?</p> <p>① Are the representative directors and the competent directors, as lecturers actively involved in training?</p> <p>② Does the insurance company provide compliance training, for example, rigorous training in the laws and ordinances to be complied with in specific areas of business? Does the insurance company provide compliance training suited to the class of business, including insurance agents?</p> <p>③ Does the insurance company encourage employees to acquire the minimum legal knowledge required for specific business areas?</p> <p>(4) Does the insurance company have a structure in place for dealing with incidents and complaints?</p> <p>① Does the insurance company have a record of complaints, customer requests, and the like?</p> <p>② Does the compliance division provide appropriate follow-up checking of complaints?</p> <p>③ Does the insurance company have a structure in place to confirm the facts regarding incidents, clarify the responsibilities of those involved, call to those involved accountable, and clarify supervisory responsibility for an incident? Are incidents investigated and analyzed by a division that is independent of the division in which the incident occurred? Does the insurance company inform the police and other relevant agencies, etc. in a timely manner of any facts that may violate criminal statutes?</p>		

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
<p>IV. Sanctions (punishments) for compliance violations, enforcement of compliance rules</p>	<p>Check for “compliance review structure”</p>	<p>Are the directors and auditors involved in the formulation of programs to prevent the recurrence of incidents, etc? Do they endeavor to ensure the effectiveness of these programs?</p> <p>(5) Does the insurance company have a structure in place to disclose information in an appropriate manner fully in conformity with the purpose of the information disclosure set forth in the Insurance Business Law?</p> <p>① Does the insurance company have a structure in place to disclose information in an appropriate manner fully in conformity with the purpose of the information disclosure set forth in the Insurance Business Law?</p> <p>② Does the insurance company have a structure in place to disclose information in an appropriate manner fully in conformity with the purpose of the timely disclosure set forth in the Securities and Exchange Law?</p> <p>(6) Does the insurance company engage in appropriate personnel rotation so that specific employees are not engaged in the same jobs in the same divisions for prolonged periods of time?</p> <p>If specific employees must be engaged in the same jobs in the same divisions for prolonged periods of time, does the insurance company have other appropriate measures to prevent incidents from occurring?</p> <p>(7) Does the insurance company have programs in place to require employees (including manager and insurance agents) to stay away from their jobs for a minimum of one continuous week per a year for the purpose of preventing incidents? This might include continuous vacation, training, internal reassignment, or any combination thereof. It is desirable that this period be at least two weeks.</p> <p>If, in independent business units a program to require employees to stay away from their jobs cannot be adopted by unavoidable reasons, or if such a program is not effective in preventing incidents, does the insurance company have other effective measures to prevent incidents from occurring?</p> <p>Does the insurance company have rules covering sanctions (punishments) for violations? Does it enforce these rules?</p> <p>(1) Should directors, etc. be discovered to be in violation of applicable laws and ordinances, are there mechanisms in place to enable the other directors, etc. to faithfully exercise the following authority as required by law, and to quickly make such response as is necessary to restore sound and proper operation?</p> <p>① Directors</p> <p>a. Convene a meeting of the board of directors (Commercial Law Article 259)</p> <p>b. Report to the auditors (Commercial Law Article 274-2)</p> <p>② Auditors</p> <p>a. Enjoin directors from committing illegal actions (Commercial Law Article 275-2)</p> <p>b. Convene a meeting of the board of directors (Commercial Law Article 260-3, Paragraph 3 and Paragraph 4)</p> <p>c. Report to the board of directors (Commercial Law Article 260-3)</p>	<p>Note: Laws referenced in (1) apply for mutual society company to Articles 51, 53, and 59 of the Insurance Business Law</p>

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
V. Laws and ordinances, etc. to be complied with by insurance companies and their managers	1. Outline of laws and regulations	<p>Paragraph 2)</p> <p>d. Issue an opinion to the general meeting of stockholders (Commercial Law Article 275)</p> <p>e. Make notations in the auditors report (Commercial Law Article 281-3, Subparagraph 2:10)</p> <p>(2) Are directors aware of the mutual watching obligation they incur as members of the board of directors, and do they take such actions as are required to faithfully discharge this obligation?</p> <p>(3) Does the insurance company call to accountable directors, etc. and accounting auditors who have committed illegal actions?</p> <p>(4) Does the insurance company select for its auditors personnel who are able to exercise their authority independently?</p> <p>(5) Do auditors perform compliance audits?</p> <p>(6) Is there a structure in place to report to directors when illegal acts are discovered?</p> <p>(7) Does the insurance company have rules in place regarding sanctions (punishments)? Does it enforce its sanction (punishment) rules rigorously and fairly?</p> <p>(8) Does the insurance company assign independent compliance officers to confirm compliance in business divisions (including business offices, etc.) that incur risks above fixed volume?</p> <p>(9) Do compliance officers function adequately?</p> <p>(10) Are there effective ties between compliance divisions and others?</p> <p>1. Laws and regulations regarding "insurance companies"</p> <p>(1) Laws</p> <ol style="list-style-type: none"> 1) Insurance Business Law 2) Law concerning Non-Life Insurance Rating Organizations 3) Automobile Liability Security Law 4) Law concerning Earthquake Insurance 5) Banking Law 6) Securities and Exchange Law 7) Law concerning Foreign Securities Brokers 8) Investment Trust Law 9) Investment Law 10) Money-lending Law 11) Investment Advisory Service Law 12) Mortgage-backed Securities Law 13) Commodities Fund Law 14) Real Estate Designated Cooperative Projects Law 15) Law concerning the Regulation of Businesses Involved in Specific Credits, Etc. 16) Law concerning Regulation of Pre-paid Certificates 17) Financial Futures Trading Law 18) Mutual Loan Association Law 19) Trusts Law 20) Building Lots and Buildings Transaction Business Law 21) Law concerning the Registration of Immovables 	

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
		<ul style="list-style-type: none"> 22) Building Standard Law 23) Law against Unjustifiable Premium and Misleading Representation 24) Unfair Access Prohibition Law (2) Government ordinances and regulations 2. Laws and ordinances related to joint-stock companies <ul style="list-style-type: none"> (1) Commercial Code Part 2 (2) Law concerning Special Exceptions to the Commercial Code 3. Laws and ordinances related to "economic order and market order" <ul style="list-style-type: none"> (1) Antimonopoly Law (2) Unfair Competition Prevention Law (3) Securities and Exchange Law (4) Commodities Exchange Law (5) Financial Futures Trading Law (6) Consumer Protection Law <ul style="list-style-type: none"> 1) Consumer Protection Basic Law 2) Interest Rate Restriction Law 3) Investment Law 4) Money-lending Law 5) Installment Sales Law 6) Door-to-door Sales Law 7) Law concerning the Prevention of Pyramid Schemes 4. Laws and Regulations concerning "Financial Transactions" <ul style="list-style-type: none"> (1) Civil Code, Commercial Code, Bills Law, Checks Law (2) Special Malfeasance (Commercial Code Article 486 Paragraph 1), Fraud (Penal Code Article 246), Malfeasance (Penal Code Article 247), and Embezzlement (Penal Code Article 253) (3) Interest Rate Restriction Law (4) Investment Law (5) Anti-Organized Crime Law (6) Law concerning the Regulation of Improper Contracts Related to Deposits, Etc 	<p>Note: In addition to laws and ordinances, the "Guidelines" describes the points that are aimed at and should be kept in mind in supervision. It is important to fully reflect this in the inspection of compliance system</p> <p>Note: The laws and ordinances, including the Insurance Business Law, that were referenced in "V." are examples. Take note that similar provisions apply mutatis mutandis (including application or paraphrasing of different articles) to Japan branches and offices of foreign insurance companies.</p>

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
	<p>2. Outline of laws and ordinances related to “management”</p>	<p>1. Violations of ban on concurrent service by directors (Insurance Business Law Article 8 and Article 333)</p> <p>2. Window dressing, illegal dividends (Insurance Business Law Article 15, Article 55, Article 58, and Article 324)</p> <p>3. Article of association provision violation (Insurance Business Law Article 52 and Article 333, Commercial Code Article 263)</p> <p>4. Violations of ban on other businesses (Insurance Business Law Article 100 and Article 333)</p> <p>5. Violations of regulations on transactions with specific affiliated parties (subsidiaries, etc.) (Insurance Business Law Article 100-3)</p> <p>6. Violations of limits on stock acquisition, etc. (Insurance Business Law Article 107 and Article 333, Anti-monopoly Law Article 11)</p> <p>7. Misstatements, etc. in operating reports (Insurance Business Law Article 110 and Article 317)</p> <p>8. Non-disclosure or false disclosure (Insurance Business Law Article 13, Article 59, Article 333, Article 111 and Article 317, Securities and Exchange Law Article 197 and Article 207)</p> <p>9. Violations of reserve requirements (Insurance Business Law Article 116, Article 117 and Article 333)</p> <p>10. Violations of requirement for reporting to supervisory authorities (Insurance Business Law Article 127, Article 128 and Article 333)</p> <p>11. Evasion of inspection (Insurance Business Law Article 129 and Article 317)</p> <p>12. Violation of business suspension orders (Insurance Business Law Article 132, Article 241 and Article 316)</p> <p>13. Malfeasance by directors, etc. (Insurance Business Law Article 322, Commercial Code Article 486)</p> <p>14. Borrow-and-deposit to disguise payment (Insurance Business Law Article 326, Commercial Code 491)</p> <p>15. Capital increase rule violations (Commercial Code Article 280-2 and beyond)</p> <p>16. Ban on relations with antisocial elements (providing benefits to “sokaiya”, Insurance Business Law Article 59 and Article 331, Commercial Code Article 294-2 and Article 497)</p> <p>17. Notification of dubious transactions (Anti-Organized Crime Law Article 54)</p> <p>18. Joint actions, collusion (Anti-monopoly Law Article 3)</p> <p>19. Leakage of customer information, abuse of confidentiality (Penal Code Article 247 Judicial precedent)</p>	

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
	<p>3. Outline of laws and ordinance related to "accounting"</p>	<p>1. Profit reserve requirement violation (Insurance Business Law Article 14 and Article 333) 2. Loss-compensation reserve requirements: Use of reserves for other than the purpose (Insurance Business Law Article 54, Article 57 and Article 333) 3. Fund depreciation reserve requirement: Use of reserves for other than the purpose (Insurance Business Law Article 56, Article 57 and Article 333) 4. Lack of reasonable accounting by characteristic of products; Violations of distribution exceeding surplus standard (Insurance Business Law Article 58 and Article 114) 5. Violations of reserving stock revaluation profits (Insurance Business Law Article 112 and Article 333) 6. Violations of reserve requirement on price fluctuations (Insurance Business Law Article 115 and Article 333) 7. Special account transfer violations (Insurance Business Law Article 118 and Article 333)</p>	
	<p>4. Outline of laws and ordinances related to "underwriting"</p>	<p>1. Explanation of important matters to policyholders (Insurance Business Law Article 100-2 and Article 300) 2. Violations of location of insurance contracts and restriction on things covered by insurance (foreigner insurers) (Insurance Business Law Article 186, Article 186 and Article 316) 3. Violations of ban on unregistered or unqualified underwriting of insurance (Insurance Business Law Article 275 and Article 317) 4. Falsified application for registration; Registration statement violations (insurance agents, non-life insurance agents) (Insurance Business Law Article 279, Article 280 and Article 337) 5. Underwriting on consignment from other companies (insurance agents) (Insurance Business Law Article 282) 6. Liability of one's company (insurance agents, non-life insurance agents) (Insurance Business Law Article 283) 7. Original register provision violation (insurance agents, non-life insurance agents) (Insurance Business Law Article 285) 8. Violation of ban on self-contract (non-life insurance agents, insurance brokers) (Insurance Business Law Article 295) 9. Violations of good faith obligations (insurance brokers) (Insurance Business Law Article 299) 10. Violations of prohibited acts concerning contract conclusion and underwriting (Insurance Business Law Article 300, Article 307 and Article 317-2) 11. Violations of prohibited acts on underwriting of insurance of subsidiaries (Insurance Business Law Article 301) 12. Reporting violations by directors or employees (non-life insurance agents, insurance brokers) (Insurance Business Law Article 302) 13. Violations of provisions of books and records (insurance brokers) (Insurance Business Law Article 302 and Article 320) 14. Violation in submission of business reports: misstatement (insurance brokers) (Insurance Business Law Article 304 and Article 320)</p>	<p>Note: The "4" lists matters related to insurance brokers for reference.</p>

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
		<p>15. Evasion of inspection (insurance agents, non-life insurance agents, insurance brokers) (Insurance Business Law Article 305 and Article 320)</p> <p>16. Violations of business improvement orders (insurance agents, non-life insurance agents, insurance brokers) (Insurance Business Law Article 306 and Article 320)</p> <p>17. Violations in refunding money on cancellation of applications for insurance contracts (Insurance Business Law Article 309)</p> <p>18. Money laundering (Notification of dubious transactions – Anti-Organized Crime Law Article 54, Concealment and receipt of illicit profits, etc. – Anti-Organized Crime Law Article 10 and Article 11)</p> <p>19. Misappropriation, etc. of insurance premiums, etc. (Fraud – Penal Code Article 246 and Article 246-2, Malfeasance – Article 247, Embezzlement – Article 252 and Article 253)</p>	
	<p>5. Outline of laws and ordinances related to “asset management”</p>	<p>1. Violations of asset management methods, etc. (Insurance Business Law Article 97)</p> <p>2. Violations of restrictions on large-lot lending (including lending for the purpose of circumvention) (Insurance Business Law Article 97-2)</p> <p>3. Lending for illegal uses</p> <p>(1) Prostitution Prohibition Law Article 13 and beyond</p> <p>(2) Accessory if involved in any way with criminal activities (Penal Code Article 60 and Article 62)</p> <p>(3) Violations of public morals (Civil Code Article 90)</p> <p>4. Lending in violation of authorization rules</p> <p>(1) Divided lending (loans to the same party but divided up into different names and formally loaned to different people in order to circumvent legal and internal restrictions)</p> <p>(2) Approval violations (loans made in violations of condition on approval)</p> <p>(3) Failure to seek approval (loans made without seeking approval even though approval is required)</p> <p>5. Loans to directors (Commercial Code Article 265, Insurance Business Law Article 51)</p> <p>Requires decision by the board of directors</p> <p>6. Violations of interest-rate restrictions (Interest Rate Restriction Law, etc.)</p> <p>7. Off-record lending (Investment Law Article 3 and Article 8, Penal Code Article 253, Commercial Code Article 486)</p> <p>8. Favoritism in lending (Commercial Code Article 486)</p> <p>9. Asset management by using insider information (Securities and Exchange Law Articles 163 to 167)</p>	

Item	Compliance Check Point	Explanation of Compliance Check Points	Remarks
	<p>6. Outline of laws and ordinances related to "ancillary businesses" ? Insurance proxy business: clerical work service ? Securities business ? Over-the-counter investment trust sales business</p>	<p>1. Insurance proxy business for other insurance companies: clerical work service (Insurance Business Law Article 98) 2. Securities business (1) Ban on improper solicitation (discretionary trading accounts, etc.) (Securities and Exchange Law Article 42) (2) Ban on loss compensation (Securities and Exchange Law Article 42-2) (3) Ban on fraudulent acts (Securities and Exchange Law Article 157, Article 158 and Articles 168 to 171) (4) Ban on market manipulation (Securities and Exchange Law Article 159, etc.) (5) Ban on insider trading (Securities and Exchange Law Articles 163 to 167)</p>	



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Section 4

Annuities



Annuities

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- I. Annuity Terminology
 - A. Owner -- controls the contract
 - B. Annuitant -- person on whose life annuity payments will be based
 - C. Beneficiary -- person who receives payment in the event of the annuitant's death prior to annuitization

- II. Annuity Phases – Insurance or Investment?
 - A. Accumulation Phase, or Pay-in Phase
 - B. Annuity Phase, or Pay-out Phase
 - C. Superannuation -- occurs when an individual outlives his/her income.
 - D. Nonforfeitable and Non-Attachable

- III. Classification of Annuities
 - A. Number of lives covered
 - 1. Single life annuity
 - 2. Joint life, or joint and survivorship annuity
 - B. Time when benefits begin
 - 1. Immediate
 - 2. Deferred
 - C. Method of purchase
 - 1. Lump sum (single premium)
 - 2. Installment (fixed or flexible premiums)
 - D. Qualified versus Nonqualified

IV. The Types of Annuities

A. Two general types of annuities:

1. Fixed Annuities

- a. Fixed Annuities must comply with guaranteed minimum account value rules in the Standard Nonforfeiture Law for Individual Annuities.
 - (1). Law states that single premium fixed annuities “...provide for a guaranteed minimum account value at all times no less than 90% of the single premium amount compounded by interest of no less than 3% per year.”
 - (2). In flexible premium annuities, the Guaranteed Minimum Account Value (GMAV) must be at least 65% of first year premiums, and 8.75% in subsequent years compounded at 3% (assuming level premium stream.)
- b. Accumulation phase -- premium payment methods
 - (1). Single premium (lump sum)
 - (2). Flexible premium
- c. Accumulation phase -- interest credits
 - (1). Declared or “Trust Me” rates
 - (2). Certificate or Guaranteed Rate Annuities
 - (3).
 - Guaranteed interest rate
 - + Excess interest rate
 - = Current interest rate.

THE TYPES OF ANNUITIES -- Fixed Annuities (cont.)

- d. Annuity phase -- benefit payments
 - (1). Immediate versus deferred annuities
 - (2). Benefits are payable to the annuitant with guarantees for annuitant's survivors, if desired.
 - (3). Benefit payments, once established, are fixed for the life of the annuitant
- e. Regulation -- fixed annuity sales are regulated by the state department of insurance; the salesperson must have a valid life insurance license to sell fixed annuity products.

2. Variable annuities

- a. Accumulation phase -- premium payment methods
- b. Accumulation phase -- separate account
- c. Accumulation phase -- interest credits
- d. Annuity phase -- benefit payments

THE TYPES OF ANNUITIES -- Variable Annuities (cont.)

- e. Regulation -- sales of variable annuity products, *which are classified as securities*, are regulated by the state department of insurance AND the Financial Industry Regulatory Authority (FINRA); sales person must have a valid life insurance license for the states in which he or she is doing business, AND he or she must also have a Series 6 or Series 7 registration with the NASD.
3. Indexed annuities -- a form of fixed annuities
 - a. Values in indexed annuities are tied to the Standard and Poore's 500 Stock Index.
 - b. Client's principal is guaranteed: if client holds the annuity for the guaranteed period (also known as the surrender period,) client is guaranteed to receive one hundred ten per cent (110%) of the principal amount if the index loses or does not gain.



CAUTION: *Remember Standard Nonforfeiture Law for Individual Annuities? “GMAV at all times no less than 90% of the single premium amount compounded by interest of no less than 3% per year.”*

- c. A high percentage of the client's original premium is invested in investments such as high-grade bonds to provide the guaranteed cash.
- d. The balance of the original premium is invested primarily in S&P 500 call options. At the end of the option period, the insurance company chooses whether to exercise the option. If the movement of the index is negative, the options are allowed to expire with no value due to the insurer. If the index is positive, the option is exercised, and the insurance company receives a percentage of the increased value.

THE TYPES OF ANNUITIES -- Indexed Annuities (cont.)

- e. Primary strategies used to calculate the returns:
 - (1). Long Term Point-to-Point -- is a very basic calculation method: there are only two dates used in this calculation method, the starting point and ending point. Whatever the market does between the issue date and the ending date is *irrelevant*. Only the first day and last day of the entire index term count.
 - (2). Average End -- sometimes referred to as the "Asian End," this method is similar to the Long-Term Point-to-Point method, but it employs a series of days (usually weekly or monthly) near the end of the annuity term to determine gains.

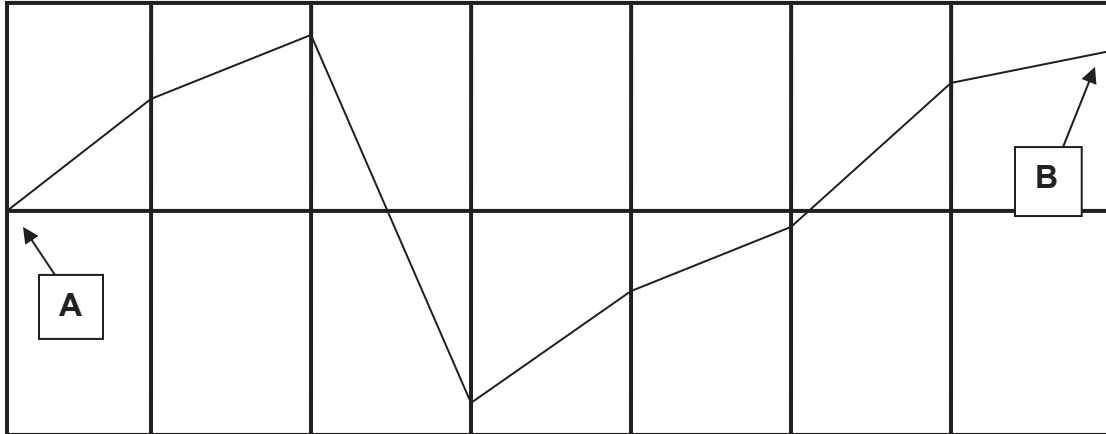
Primary strategies are continued on page 9.

Notes:

Exhibit I

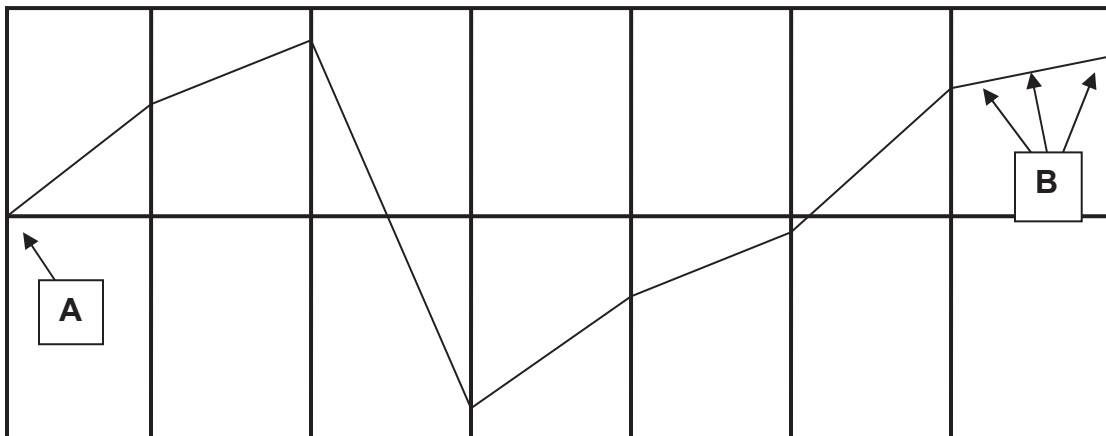
The following charts demonstrate how each of the major methods of determining interest credits would react in a market correction and recovery.

Long Term Point-to-Point



In Long Term Point-to-Point, only points *a* and *b* are considered in determining the interest amount to be credited. If, at the end of the guarantee period (typically seven years,) *b* is higher than *a*, a credit (*c*) would be applied, subject to any participation rate and/or rate cap. See page 11.

Average End (Asian End)



In Long Term Point-to-Point Average (or Asian) End, only points *a* and *b* are considered in determining the interest amount to be credited. However, point *b* is determined by taking an average of closing market values over a pre-determined period of time near the end of the guarantee period (e.g., two weeks,) or on a specified date in each of the last few months of the guarantee period (e.g. the fifteenth of each of the last six months of the guarantee period.) If the Average End value *b* is higher than point *a*, an interest credit is applied, subject to any participation rate and/or rate cap.

See page 11.

THE TYPES OF ANNUITIES -- Indexed Annuities -- Primary Strategies Used to Calculate Returns (cont.)

- (3). High-Water Anniversary Mark, Look-Back -- uses an Annual Point-to-Point method to recognize and lock in the annual index values. At the end of the term or index period, the *highest anniversary value* of a gain is used to compute the total index return for the index term.

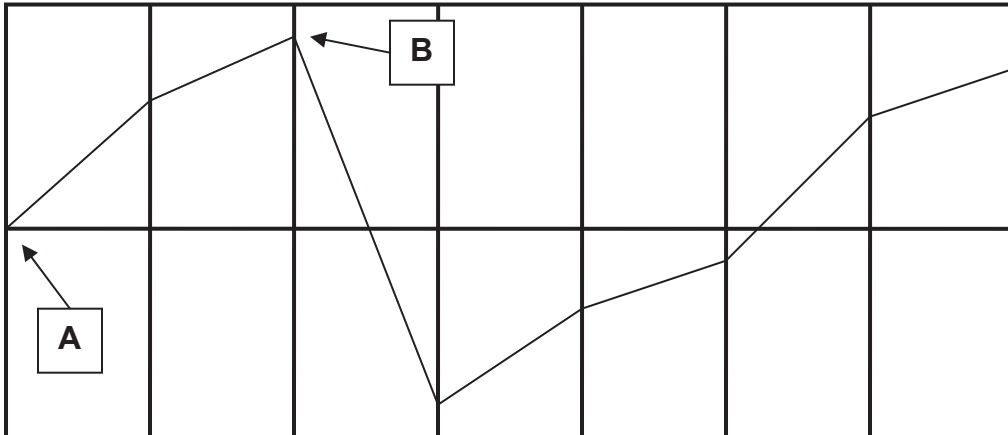
- (4). Low-Water Anniversary Mark, Look-Back -- similar to #3 above, however, instead of looking back to determine the highest anniversary value, this method looks back for the *lowest anniversary value* which becomes the starting value, and gains from that point to the end of the index period are used to calculate any return on the policy.

Notes:

Exhibit I (cont.)

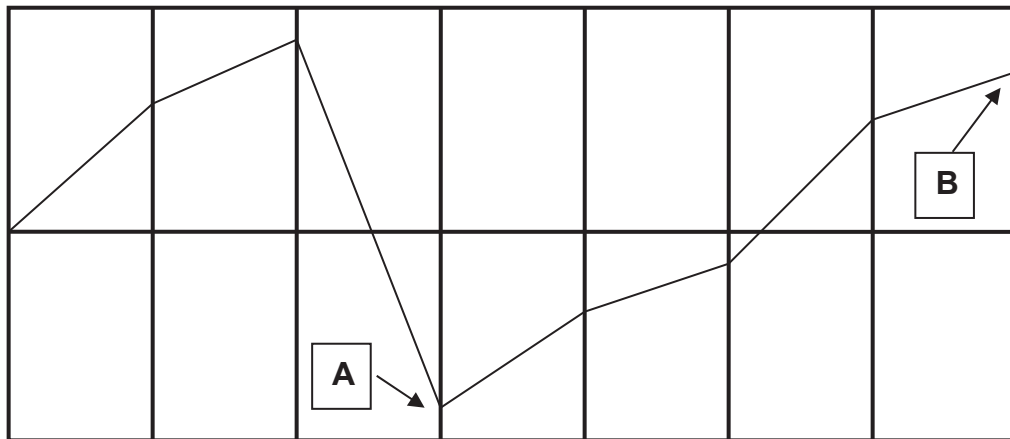
The following charts demonstrate how each of the major methods of determining interest credits would react in a market correction and recovery.

High-Water Anniversary Mark, Look Back



In High-Water Anniversary Mark, Look Back, an annual point-to-point is used to recognize and lock in the index values. However, at the end of the guarantee period, only the highest anniversary value *b* is used to determine the amount of interest to be credited to the policy. The difference between point *a* and the highest anniversary value *b* is credited, subject to any participation rate and/or rate cap. See page 11.

Low-Water Anniversary Mark, Look Back



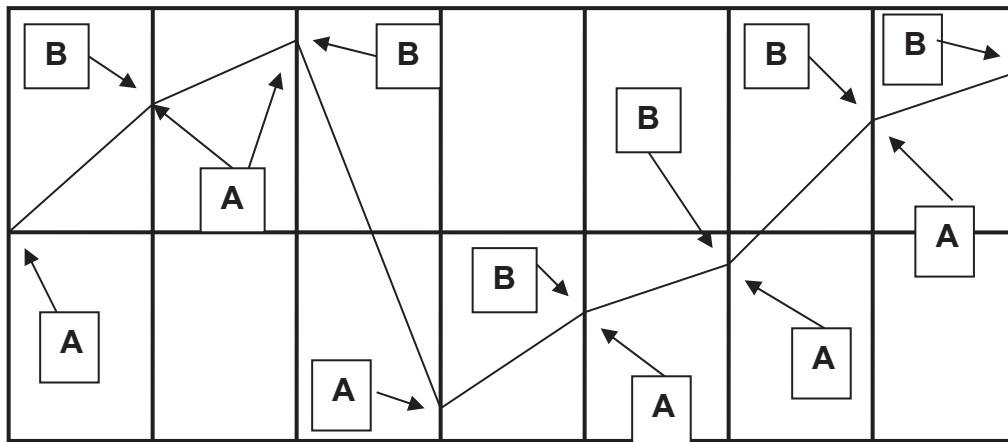
In Low-Water Anniversary Mark, Look Back, instead of looking back to determine the highest index values, the lowest anniversary date is determined. This lowest value becomes the index starting point, and gains from this point become the basis for calculating the gain to be credited to this policy, subject to any participation rate and/or rate cap. See page 11.

THE TYPES OF ANNUITIES -- Indexed Annuities -- Primary Strategies Used to Calculate Returns (cont.)

- (5). Annual Point-to-Point with Annual Reset -- also sometimes called the "Ratchet" method, applies the participation rate to any index growth and "resets" the annual return start point on each anniversary date.

Exhibit I (cont.)

Annual Point-to-Point with Annual Reset (Ratchet)



In the Annual Point-to-Point with Annual Reset method, index growth b is recorded on each policy anniversary during the guarantee period, the participation rate and/or rate cap is applied to the interest credit, and the amount is added to the account value. (See page 11.) This new value becomes the reset value a for the next year. If there is a year in which index value falls, or does not increase, no credit is applied on the anniversary date.

THE TYPES OF ANNUITIES -- Indexed Annuities (cont.)

- f. End of Index Period
 - (1). Similar to end of Surrender Charge Period on Declared Rate annuities
 - (2). Annuity owner has full access to annuity values, including to interest earned, subject to tax considerations.

- g. Three primary types of re-entry
 - (1). Automatic or “Forced” -- At end of Index Period, contract enters “free window” or “free out” period of 20-45 days -- Owner has access to entire contract value. Any values remaining in contract at end of “free window” are automatically renewed for another Index Period (7 years typically.)
GOOD NEWS: New period of potential high earnings.
BAD NEWS: Less flexibility again.
MORE GOOD NEWS (for agent): new commission!
 - (2). Variation of “Forced” -- Also forced, but renewals are for one declared year at a time -- Owner is not committed to a new 7-year period.
 - (3). Declared Interest Default or “Non-Forced” -- has no default or automatic re-entry -- At end of initial Index Period, policy declares annual interest rate for each successive year (like a declared rate annuity) -- interest is credited, values are accessible by owner without penalty -- Allows policyowners to re-enter for another Index Period if owner wishes -- Allows owner more control to select re-entry when owner is ready -- not forced by “free window” -- Market may be uncertain or owner may be cautious and this allows more time to decide to re-enter.

THE TYPES OF ANNUITIES -- Indexed Annuities (cont.)

- h. Participation rate -- insurer decides the percentage of annuity owner's participation in the rate of return from the options that are exercised.
- i. Rate cap -- insurer may impose a rate cap (e.g., 14%) to limit the owner's return.
- j. Asset fee -- insurer charges a percentage fee before any return is credited to owner's policy.

Notes:



Points to Remember



There are TWO primary types of annuities:

1. Fixed annuities
2. Variable annuities



Fixed Annuities guarantee principal; interest is credited on a fixed basis. Although the interest earned is considered fixed, the annuity company may, from time to time, adjust the rate of interest payable based on current assumptions of rate of investment return and/or mortality. **KEEP IN MIND** that even though the interest credited may fluctuate over time, the *principal is not at risk*.



Variable Annuities **DO NOT** guarantee principal for the most part; the individual investor assumes some risk in that he or she may lose principal if the market turns downward. **HOWEVER**, the attraction for many investors interested in Variable Annuities is that the dollars invested should be able to keep pace with inflation. By keeping pace with inflation, buying power of the dollars in the investment will not be eroded.

V. Annuity Contract Provisions

- A. Surrender charges, or deferred sales charges -- makes moving money out of the annuity less attractive to the owner.
 - 1. Charges, expressed as a percentage, are usually applied to surrenders (full or partial) made within a certain number of years (five to ten years is most common.)
 - 2. Many annuity contracts waive the charges in the event of the death or disability of the annuitant.
- B. Bailout provision
 - 1. Allows the contract owner to fully surrender the contract without surrender charges if the current interest rate drops below a certain percentage or level.
 - 2. This provision DOES NOT waive the ten percent (10%) penalty tax imposed by the IRS for early withdrawals.
- C. Issue ages
 - 1. This is more a function of the underwriting process than a policy provision, but most contracts will have maximum age limits over which a contract cannot be issued.
 - 2. Some contracts impose a lower maximum age for the annuitant than for the owner, and some contracts only impose maximum age requirements on annuities that will be paid out over the annuitant's lifetime.
- D. Maximum age for benefits to begin
 - 1. This provision states that the annuitant must begin receiving benefits before reaching the maximum age stated in the contract.
 - 2. This provision is apart from the requirements imposed by the IRS on qualified plans.

ANNUITY CONTRACT PROVISIONS (CONT.)

E. Nursing home waiver

1. Waives the contract surrender charges in the event the annuitant is hospitalized or confined to a nursing home for a specified period of time.
2. It allows the contract owner to receive cash from the annuity to pay expenses associated with the hospital stay or the nursing home stay.

VI. The Need for Annuities

A. Annuity -- the systematic liquidation of an estate or an amount of money.

1. Do Annuities Compete as Investments?
 - a. Fixed savings accounts
 - b. Mutual funds
 - c. Securities
2. Do Annuities Qualify as Insurance?
 - a. Superannuation -- occurs when an individual outlives his or her income.
 - b. Attitudes toward money
 - c. Lack of retirement or financial planning

VII. Annuities as a Financial Planning Tool

A. Retirement Planning

1. Accumulation tool

- a. Can be used to fund IRA's, Keogh's, etc. (Qualified)
- b. Can also be used to fund Nonqualified retirement accumulation

2. Conservation tool

- a. 401(k) rollovers, IRA rollovers, early retirement distributions
- b. Conserving and consolidating market gains

3. Distribution tool

- a. Liquidation of market position (or partial liquidation)
- b. Nonqualified retirement accumulations (non-annuity accumulations) e.g., certificates of deposit, proceeds from investment real estate sales, etc.

B. Structured Settlement Planning

1. Distribution tool -- qualified funding assets

- a. Used to pay benefits (settlement) for damages resulting from illness or injury
- b. Often negotiated directly with annuity carrier by attorneys for Plaintiff and/or Defendant.

ANNUITIES AS A FINANCIAL PLANNING TOOL (cont.)

2. Distribution tool -- NON-Qualified Funding Assets

- a. A lump sum payment for injury or illness can be structured by the injured party through the purchase of an annuity (or annuities.)
- b. Used when injured party decides income stream would be more beneficial than a lump sum payment.

C. Specific Funding Needs

1. College planning

- a. Immediate annuities can be structured to protect assets prior to completion of FAFSA (Free Application for Federal Student Aid) form.
 - (1). Cash assets of parent or student can be placed in an immediate annuity.
 - (2). Funding back to student or parent must be done over a minimum of five years to avoid some tax implications.
- b. The *deferred* annuity is not a good accumulation tool for education if the annuitant life is the student due to income tax implications and penalties.

2. Funding for other insurance products

- a. Transfer of a cash asset such as a certificate of deposit into an immediate annuity can fund the purchase of life insurance or Long-Term Care (LTC) insurance.
- b. Annuitize an existing annuity to buy Long Term Care (LTC) insurance and/or life insurance.

ANNUITIES AS A FINANCIAL PLANNING TOOL (cont.)

- (1). This three-part sale (annuity, LTC, and life insurance) uses annuity payments to purchase Long Term Care insurance to protect assets in the event of the need for long term care, and to purchase life insurance to restore the annuity value to the beneficiary (or estate) upon the insured's death.
- (2). If the annuity payments are used to purchase life insurance only, the effect is to pass benefits from the annuity which has income tax implications for the beneficiary through the life insurance policy which has no income tax implications for the beneficiary.

VIII. Accessing the Cash Value of an Annuity

A. Withdrawals

1. Withdrawals are received as interest out first. Therefore, payments are subject to income taxation as ordinary income in the year in which payments are received. In addition:
 - a. For persons under the age of fifty-nine-and-a-half (59 1/2), there is also a tax penalty of ten percent (10%) of the taxable amount received.
 - b. For persons over the age of fifty-nine-and-a-half (59 1/2), the tax penalty does not apply.
2. Systematic withdrawals are available as a method in which an owner may receive money from an annuity policy during the accumulation phase.
 - a. Annuity owner can elect to withdraw a set amount each month or year without any contract fee or surrender charges being applied.
 - b. This provision DOES NOT, however, prevent the income tax penalty from being applied; this provision only waives company fees or surrender charges in those policies that include this provision.

ACCESSING THE CASH VALUE OF AN ANNUITY (cont.)

B. Annuitization (Annuity Phase)

1. Straight life -- pays annuitant for balance of his/her life with no refund of principal if annuitant does not live to receive it all.
2. Refund life -- cash or installment -- refunds any principal balance left at annuitant's death to annuitant's beneficiary.
3. Installment certain -- pays income to annuitant for life, but if he/she dies before the end of the certain period, his/her beneficiary would receive payments for balance of certain period.
4. Joint life -- pays two or more annuitants until FIRST one dies.
5. Joint and survivorship life -- pays two or more annuitants until LAST one dies.
6. Temporary annuity certain -- guarantees payments to annuitant until the end of a specified period; if annuitant *lives* to end of period, payments stop; if annuitant *dies* before the end of the guaranteed period, annuitant's beneficiary receives payments for balance of the period.

Notes:

IX. Income Tax Aspects of Annuities

A. Premium payments

1. Premiums paid into a nonqualified annuity are generally not deductible.
2. Premiums paid into qualified annuities, such as IRA's or Keogh plans funded by annuities, or Tax Sheltered Annuities (TSA's), are deductible subject to IRS rules.

B. Loans

1. Amounts received as loans or as value of part of an annuity contract pledged or assigned to cover a loan are taxable.
2. Amounts assigned from the annuitant to another individual are still taxable as income to the original annuitant.

C. Withdrawals

1. For annuity contracts entered into before August 13, 1982, distributions are taxed under the "cost recovery" rule: first dollars out are considered to be a recovery of cost basis and are therefore not taxable until full cost basis is recovered.
2. For annuity contracts entered into after August 13, 1982, distributions are taxed under the "interest out first" rule: first dollars out are considered to be interest payments and are therefore taxable as income in the year in which they are received.
3. Cash value of the annuity is determined without regard to any surrender charges imposed by the insurance company. Because of this, the contract owner would conceivably face not only taxation of the amount (or part of the amount) received, but in addition may also face surrender charges imposed by the insurer, and if the distribution is considered to be premature, may also face the premature distribution penalty tax.

INCOME TAX ASPECTS OF ANNUITIES (cont.)

D. Cash accumulations

1. Natural persons -- for non-qualified annuities owned by natural persons, the interest credited to an annuity each year is generally not taxable at the time the interest is credited. Income tax WOULD, however, be due at the time annuity benefits are received, but tax would only be assessed on the interest portion of the benefit.
2. Nonnatural persons -- for contributions made after February 28, 1986, into annuities held by a corporation or other entity deemed by the IRS to be a nonnatural person, interest on those contributions is taxable in the year it is credited.
3. Exception to the nonnatural person rule -- when an annuity is held by a trust, corporation, or other nonnatural person AS AN AGENT FOR a natural person, the contract will be treated as an annuity and the interest earned will be income- tax deferred.

***For additional exceptions to the nonnatural person rule,
see Notes of Interest, page 23.***

Notes:

Notes of Interest

Exceptions to the Nonnatural Person Rule

Prior to 1986, interest earned inside an annuity was tax deferred regardless of who or what entity owned the annuity contract. However, in 1986, Congress enacted legislation designed to prevent corporations and other entities from taking advantage of this provision.

There are some exceptions to this rule:

- ✓ Any annuity contract which is acquired by a person's estate at the person's death;
- ✓ Any annuity contract which is held under a qualified retirement plan, a Section 403(b) Tax Sheltered Annuity (TSA), or an Individual Retirement Account (IRA);
- ✓ Any annuity contract which is purchased by an employer upon the termination of a qualified retirement plan or Tax Sheltered Annuity (TSA) program and held by the employer until all amounts under the contract are distributed to the employee for whom the contract was purchased or to his beneficiary;
- ✓ Any annuity contract which is an immediate annuity (an annuity which is purchased with a single premium and begins payments within a year);
- ✓ Any annuity contract which is a qualified funding asset (an annuity contract issued by a licensed insurance company which is purchased to fund payments for damages resulting from personal physical injury or sickness.)

INCOME TAX ASPECTS OF ANNUITIES (cont.)

- E. Ten percent (10%) premature distribution penalty tax
 - 1. Tax is imposed to discourage the use of annuity contracts as short term tax sheltered investments.
 - 2. The ten percent (10%) tax applies to the portion of any payment that is taxable.
 - 3. Tax is imposed on taxpayers under the age of fifty-nine-and-a-half (59 1/2) who receive distributions from annuities.

***For exceptions to taxation of early distributions,
see Notes of Interest, page 25.***

Notes:

Notes of Interest

Exceptions to the Early Distribution Penalty Rule Imposed by the IRS

- ✓ **Distributions made as result of the death of the annuity owner;**
- ✓ **Distributions made as result of the disability of the taxpayer;**
- ✓ **Distributions made under an immediate annuity;**
- ✓ **Distributions from a qualified retirement plan (IRA's, TSA's, etc.,) but it should be noted that these plans are subject to a similar ten percent (10%) penalty;**
- ✓ **Distributions made under a qualified funding asset (structured annuity purchased to pay for damages as a result of a liability resulting from a physical injury or illness;)**
- ✓ **Distributions made under an annuity purchased and held by an employer upon the termination of a qualified retirement plan; or**
- ✓ **Distributions which are part of a series of substantially equal periodic payments, made not less frequently than annually, for the life or life expectancy of the taxpayer or the joint lives or joint life expectancies of taxpayer and his designated beneficiary.**

INCOME TAX ASPECTS OF ANNUITIES (cont.)

F. Section 1035 Exchanges

1. Section 1035 exchanges permit annuity owner to exchange an annuity contract for another annuity contract without incurring any current income taxation on the event if the requirements of the section are met.
2. Section 1035 also permits exchange of life insurance policies or of endowment policies.

G. Taxation of annuity benefit payments

1. Payments are considered to be part principal (cost basis) and part interest.
2. Interest portion of each payment is considered to be taxable as income in the year in which it is received.

H. Taxation of annuity death benefits

1. Death of the owner -- for contracts issued after January 18, 1985, IRS requires that the contract will not be treated as an annuity, and therefore receive the income tax deferral associated with an annuity unless it provides two things:
 - a. First, it must provide that if an owner dies after the annuity has begun annuity payments but before the entire interest in the contract has been distributed, the remaining portion must be distributed at least as rapidly as the method of distribution being used at the owner's death.
 - b. Second, the annuity must provide that if the owner dies before the annuity payments have started, the entire interest in the contract must be distributed within the five years following the owner's death.
 - c. If the beneficiary annuitizes the contract proceeds within one year of the death of the owner, the five-year distribution requirement will be deemed as met.

INCOME TAX ASPECTS OF ANNUITIES -- Taxation of Death Benefits (cont.)

2. Death of the annuitant
 - a. If the annuitant dies before the annuity payments begin, the beneficiary will be paid a death benefit equal to the amount of premiums paid or the accumulation value of the contract.
 - b. Any gain in the contract is considered to be taxable income to the beneficiary in the year in which it is received.

X. Annuity Suitability

A. What Is Suitability?

1. The process of applying standard principles to determine whether a recommended product is appropriate for any given consumer
2. Based on consumer's objectives and needs in light of:
 - a. Risk tolerance
 - b. Financial holdings
 - c. Investment experience
 - d. Income
3. Suitability requires a producer to ensure that a recommended product is consistent with a consumer's financial profile and financial objectives.
4. The Best Interest rule requires insurance agents to act in the best interest of the consumer when making recommendations regarding purchase of an annuity.
5. The rule also requires insurers, including fraternal benefit societies, to establish and maintain a system to supervise recommendations so that the insurance needs and financial objectives of consumers are effectively addressed at the time of the transaction,

ANNUITY SUITABILITY (cont.)

B. Best Interest Suitability

1. Sales Practices

- a. Prior to the enactment of current Best Interest rules, variable annuity sales regulation was handled by Financial Industry Regulation Authority (FINRA).
- b. Fixed annuities sales regulation was handled by individual State departments of insurance.
- c. Under the Best Interest rules, sales standards applying to fixed annuities and variable annuities are more closely aligned, treating all annuity sales with the same standards in regard to sales, suitability, and disclosure.

2. Annuity Disclosures – Annuity agents must deliver specific documents and specific information to their annuity prospects and buyers, thereby encouraging informed buying decisions. Disclosure is required in the following areas of information:

- a. the generic name of the annuity contract being proposed or recommended (such as "single premium deferred annuity" or "variable deferred annuity");
- b. the name given to the contract by the issuing company, if different;
- c. an explanation that the product is, in fact, an annuity;
- d. the insurer's name and address;
- e. a description of the contract and its benefits, including its guaranteed and nonguaranteed elements, how these elements operate, and their risks and limitations;
- f. an explanation of the initial interest crediting rate (specifying any bonus), how long that rate will apply, and notice that the rate may change;
- g. an explanation of periodic income options, both on a guaranteed and nonguaranteed basis;

ANNUITY SUITABILITY – Best Interest (cont.)

- h. an explanation of the reductions in the contract's values when withdrawals are made;
 - i. an explanation of the penalties assessed and the reductions in the contract's values when a surrender is made during the surrender charge period;
 - j. the ways in which contract values can be accessed.
 - k. an explanation of the product's death benefit and how it is calculated;
 - l. a summary of the contract's federal tax status and an explanation of any federal tax penalties that might apply upon withdrawal or surrender of the contract's values;
 - m. an explanation of the impact of any rider, such as a long-term care rider;
 - n. an explanation of the product's insurance and investment components;
 - o. an explanation of any specific charges (such as mortality and expense fees or investment advisory fees) and whether a dollar amount or percentage of values applies; and
 - p. a notice that any current guaranteed declared rate is subject to change after the crediting period ends.
3. The annuity disclosure regulation applies to all group and individual annuity contracts *EXCEPT*:
- a. registered or non-registered variable annuities or other registered products
 - b. immediate and deferred annuities that contain no nonguaranteed elements;

ANNUITY SUITABILITY – Best Interest (cont.)

- c. annuities used to fund plans or arrangements:
 - (1). An employee pension plan covered by ERISA
 - (2). A plan described by Sections 401(a), 401(k), or 403(b) of the Internal Revenue Code, where the plan, for purposes of ERISA, is established or maintained by an employer
 - (3). A governmental or church plan defined in Section 414 or a deferred compensation plan of a state or local government or a tax-exempt organization under Section 457 of the Internal Revenue Code; or
 - (4). A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor.

- d. HOWEVER – this regulation **applies** to annuities used to fund a plan or arrangement:
 - (1). Funded solely by contributions that an employee elects to make whether on a pretax or after-tax basis; and
 - (2). Where the insurer has been notified that plan participants may choose from among two or more fixed annuity providers and there is a direct solicitation of an employee by a producer for the purchase of an annuity contract.
 - (3). Direct solicitation does not include any meeting held by a producer solely for the purpose of educating or enrolling employees in the plan or arrangement;
 - (4). Structured settlement annuities.
 - (5). Charitable gift annuities.
 - (6). Funding agreements.

ANNUITY SUITABILITY – Best Interest (cont.)

4. Definitions

- a. Recommendation – means advice provided by an insurance agent to an individual consumer that was intended for or results in a purchase, an exchange, or a replacement of an annuity in accordance with that advice.
 - (1). Just about anything an agent might say in meeting with a prospect or client that results in the purchase of an annuity of any type constitutes a recommendation and is, therefore, subject to the suitability requirements.
 - (2). This definition applies equally to agents and to insurance companies that deal directly with consumers.
 - (3). It applies equally to the sale of new annuities and to the replacement or exchange of existing contracts.
 - (4). Recommendation does not include general communication to the public or generalized consumer services assistance or administrative support, general educational information and tools, prospectuses, or other products and materials.

ANNUITY SUITABILITY – Best Interest – Definitions (cont.)

- b. Consumer Profile Information – means information that is reasonably appropriate to determine whether a recommendation addresses the consumer’s financial situation, insurance needs, and financial objectives, including ***at a minimum*** the following:
- (1). Age;
 - (2). Annual income;
 - (3). Financial situation and needs, including financial debts and other obligations;
 - (4). Financial experience;
 - (5). Insurance needs;
 - (6). Financial objectives;
 - (7). Intended use of the annuity;
 - (8). Financial time horizon;
 - (9). Existing assets or financial products, including investment, annuity and insurance holdings;
 - (10). Liquidity needs;
 - (11). Liquid net worth;
 - (12). Risk tolerance;
 - (13). Financial resources used to fund the annuity;
 - (14). Tax status

ANNUITY SUITABILITY – Best Interest – Definitions (cont.)

- c. Replacement – means a transaction in which a new policy or contract is to be purchased, and it is known or should be known to the proposing agent, or to the proposing insurer if there is no agent, that by reason of the transaction, an existing policy or contract has been or is to be:
 - (1). Lapsed, forfeited, surrendered or partially surrendered, assigned to the replacing insurer or otherwise terminated;
 - (2). Converted to reduced paid-up insurance, continued as extended term insurance, or otherwise reduced in value by the use of non-forfeiture benefits or other policy values;
 - (3). Amended so as to effect either a reduction in benefits or in the term for which coverage would otherwise remain in force or for which benefits would be paid;
 - (4). Reissued with any reduction in cash value;
 - (5). Used in a financed purchase.
- 5. Replacement of Annuities – for transactions involving exchanges or replacements, most states require that a Notice Regarding Replacement of Life Insurance or Annuities be given to the client and a signed copy of the form be submitted with a new application for the replacement product. The notice outlines what the customer should consider and the potential consequences of a replacement.

ANNUITY SUITABILITY – Best Interest (cont.)

6. Recordkeeping – Customers' situations change, memories dim, and financial products that appeared suitable when purchased might later seem far less suitable.
 - a. Producers must document their suitability determinations and maintain that documentation in the customer's file.
 - b. Necessary documentation should include the completed initial and any renewal fact-finding forms, illustrations signed by the customer, and copies of any illustration certifications made.
 - c. Suitability documentation and accurate record-keeping meet several needs:
 - (1). they enable the producer agent to recall, at the time of annual reviews, the facts and insights that formed his or her initial suitability determination;
 - (2). they facilitate ongoing suitability analyses;
 - (3). they provide important evidence in the event of a later claim by a customer or beneficiary that a life or annuity recommendation was unsuitable
 - d. . Recordkeeping –
 - (1). Insurers, independent agencies, business entity agents and insurance agents shall maintain or be able to make available to the superintendent records of the information collected from the consumer and other information used in making the recommendations that were the basis for insurance transactions for **eight years** after the insurance transaction is completed by the insurer. An insurer is permitted, but shall not be required, to maintain documentation on behalf of an insurance agent.

ANNUITY SUITABILITY – Best Interest – Record Keeping (cont.)

- (2). Records required to be maintained by this rule may be maintained in paper, photographic, micro-process, magnetic, mechanical or electronic media or by any process that accurately reproduces the actual document.
7. Duties of the Insurers – insurers cannot issue an annuity that was recommended by one of its producers unless there is a **reasonable basis to believe** the product is suitable (based on the prospect's suitability information).
 - a. In the event that no recommendation was made or when a consumer refuses to provide the necessary suitability information, yet insists on purchasing an annuity, the product's issue should still be "reasonable" based on the circumstances known to the insurer at the time.
 - b. Should any violation occur by either the insurer or producers, the insurer must take corrective action or face possible sanctions and penalties.
 - c. Annuity insurers must establish supervision systems that are designed to comply with suitability requirements. These systems must provide:
 - (1). procedures to inform producers of annuity suitability requirements;
 - (2). product training for producers;
 - (3). processes that confirm consumer suitability information to identify and deter submission of inaccurate information;
 - (4). a review of each annuity recommendation before contract issue to ensure that a reasonable basis exists to determine the recommendation is suitable;
 - (5). procedures to detect recommendations that are not suitable

ANNUITY SUITABILITY – Best Interest – Duties of the Insurer (cont.)

- d. Insurer supervision requirements:
- (1). An insurer may not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives based on the consumer's consumer profile information.
 - (2). An insurer shall establish and maintain a supervision system that is reasonably designed to achieve the insurer's and its insurance agents' compliance with this rule, including, but not limited to, the following:
 - (a). The insurer shall establish and maintain reasonable procedures to inform its insurance agents of the requirements of this rule and shall incorporate the requirements of this rule into relevant insurance agent training manuals;
 - (b). The insurer shall establish and maintain standards for insurance agent product training and shall establish and maintain reasonable procedures to require its insurance agents to comply with the requirements of this rule;
 - (c). The insurer shall provide product-specific training and training materials that explain all material features of its annuity products to its insurance agents;
 - (d). The insurer shall establish and maintain procedures for the review of each recommendation prior to issuance of an annuity; procedures are to be designed to ensure that there is a reasonable basis to determine that a recommendation is suitable, and the recommended annuity would effectively address the particular consumer's financial situation, insurance needs, and financial objectives.

ANNUITY SUITABILITY – Best Interest – Duties of the Insurer (cont.)

- (e). The insurer shall establish and maintain reasonable procedures to detect recommendations that are not suitable in compliance. These may include, but are not limited to, confirmation of consumer's suitability profile information, systematic customer surveys, agent and consumer interviews, confirmation letters, agent statements or attestations and programs of internal monitoring. Nothing in this paragraph prevents an insurer from complying with this paragraph by applying sampling procedures, or by confirming suitability of the consumer profile information of this rule after issuance or delivery of the annuity; and
- (f). The insurer shall establish and maintain reasonable procedures to assess, prior to or upon issuance or delivery of an annuity, whether an agent has provided to the consumer the information required to be provided.
- (g). The insurer shall establish and maintain reasonable procedures to identify and address suspicious consumer refusals to provide consumer profile information;
- (h). The insurer shall establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific annuities within a limited period of time. The requirements of this paragraph are not intended to prohibit the receipt of health insurance, office rent, office support, retirement benefits or other employee benefits by employees as long as those benefits are not based upon the volume of sales of a specific annuity within a limited period of time; and
- (i). The insurer shall annually provide a written report to senior management, including to the senior manager responsible for audit functions, which details a review, with appropriate testing, reasonably designed to determine the effectiveness of the supervision system, the exceptions found, and corrective action taken or recommended, if any.

ANNUITY SUITABILITY – Best Interest (cont.)

8. Duties of the Agent –
 - a. The insurance agent shall prominently disclose information to the consumer on a form for this rule. Insurance agent can also include the insurance company or its intermediary if no agent is involved.
 - b. A description of the scope and terms of the relationship with the consumer and the role of the agent in the transaction;
 - c. An affirmative statement on whether the agent is licensed and authorized to sell the following products.
 - Fixed annuities
 - Fixed index annuities
 - Variable annuities
 - Life insurance
 - Mutual funds
 - Stock and bonds
 - Certificates of deposit;
 - d. A statement that the agent is authorized, contracted or otherwise appointed to sell insurance products for the insurer.
 - e. Upon request of the consumer, agent is to provide a description of the sources and types of cash and non-cash compensation to be received by the agent. Cash compensation means any discount, concession, fee, service fee, commission, sales charge, loan, override or cash benefit received by the agent.
 - f. An agent shall identify and avoid or reasonably manage and disclose material conflicts of interest.

ANNUITY SUITABILITY – Best Interest – Duties of the Agent (cont.)

9. Agent Documentation – an Agent shall, at the time of the recommendation or sale:
 - a. Make a written record of any recommendation and the basis for the recommendation subject to this rule;
 - b. Obtain a consumer signed statement on an approved form documenting:
 - (1). a customer's refusal to provide the consumer profile information, if any; and
 - (2). a customer's understanding of the ramifications of not providing his or her consumer profile information or providing insufficient consumer profile information.
 - c. Obtain a consumer signed statement on an approved form acknowledging the annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the agent's recommendation.


10. Insurance Agent or Producer Training
 - a. An insurance agent shall not solicit the sale of an annuity product unless the insurance agent has adequate knowledge of the product to recommend the annuity and the insurance agent is in compliance with the insurer's standards for product training.
 - b. Insurance agents shall comply with the following continuing education requirements:
 - (1). An insurance agent who engages in the sale, solicitation or negotiation of annuity products shall complete a one-time four credit training course provided by a department of insurance approved continuing education provider.
 - (2). The minimum length of the training required of this rule shall be sufficient to qualify for at least four CE credits but may be longer.

ANNUITY SUITABILITY – Best Interest – Duties of the Agent (cont.)

- (3). An insurer shall verify that an insurance agent has completed the four-hour annuity training course required before allowing the agent to sell an annuity product for that insurer.

11. Disclosure Forms – **See Exhibits following Page 38**

C. Insurance Aspects of Annuities

1. Asset protection during Accumulation phase
 - a. Annuity assets are protected from attachment by creditors
 - b. Fixed annuity values are guaranteed – **CAUTION** 
 - c. Variable annuity values may be guaranteed by rider or endorsement
2. Income for life –An annuity insures income for life based on life expectancy as shown in insurance industry annuity mortality tables. This is the true insurance aspect of the annuity.

XI. Conclusion

Exhibit 1

INSURANCE AGENT (PRODUCER) DISCLOSURE FOR ANNUITIES

Do Not Sign Unless You Have Read and Understand the Information in this Form

Date: _____

INSURANCE AGENT (PRODUCER) INFORMATION (“Me”, “I”, “My”)

First Name: _____ Last Name: _____

Business/Agency Name: _____ Website: _____

Business Mailing Address: _____

Business Telephone Number: _____

Email Address: _____

National Producer Number in [state]: _____

CUSTOMER INFORMATION (“You”, “Your”)

First Name: _____ Last Name: _____

What Types of Products Can I Sell You?

I am licensed to sell annuities to You in accordance with state law. If I recommend that You buy an annuity, it means I believe that it effectively meets Your financial situation, insurance needs, and financial objectives. Other financial products, such as life insurance or stocks, bonds and mutual funds, also may meet Your needs.

- I offer the following products:
- Fixed or Fixed Indexed Annuities
- Variable Annuities
- Life Insurance

Exhibit 1 (cont)

I need a separate license to provide advice about or to sell non-insurance financial products. I have checked below any non- insurance financial products that I am licensed and authorized to provide advice about or to sell.

Mutual Funds
 Stocks/Bonds
 Certificates of Deposits

Whose Annuities Can I Sell to You?

I am authorized to sell:

Annuities from Only One (1) Insurer
 Annuities from Two or More Insurers
 Annuities from Two or More Insurers although I primarily sell
Annuities From: _____

How I'm Paid for My Work:

It's important for You to understand how I'm paid for my work. Depending on the particular annuity You purchase, I may be paid a commission or a fee. Commissions are generally paid to Me by the insurance company while fees are generally paid to Me by the consumer. If You have questions about how I'm paid, please ask Me.

Depending on the particular annuity You buy, I will or may be paid cash compensation as follows:

Commission, which is usually paid by the insurance company or other sources. If other sources, Describe: _____
 Fees (such as a fixed amount, an hourly rate, or a percentage of your payment), which are usually paid directly by the customer.
 Other (Describe) _____

If you have questions about the above compensation, I will be paid for this transaction, please ask me.

I may also receive other indirect compensation resulting from this transaction (sometimes called "non-cash" compensation), such as health or retirement benefits, office rent and support, or other incentives from the insurance company or other sources.

By signing below, you acknowledge that you have read and understand the information provided to you by this document

Exhibit 2

CONSUMER REFUSAL TO PROVIDE INFORMATION

Do Not Sign Unless You Have Read and Understand the Information in this Form

Why are You being given this form?

You're buying a financial product – an annuity.

To recommend a product that effectively meets Your needs, objectives and situation, the agent, broker, or company needs information about You, Your financial situation, insurance needs and financial objectives.

If You sign this form, it means You have not given the agent, broker, or company some or all the information needed to decide if the annuity effectively meets Your needs, objectives and situation. You may lose protections under the Insurance Code of Ohio if You sign this form or provide inaccurate information.

Statement of Purchaser:

- I **REFUSE** to provide this information at this time.
- I have chosen to provide LIMITED information at this time.

Customer Signature

Date

Exhibit 3

Consumer Decision to Purchase an Annuity NOT Based on a Recommendation

Do Not Sign This Form Unless You Have Read and Understand It

Why are You being given this form? You're buying a financial product – an annuity.

To recommend a product that effectively meets Your needs, objectives and situation, the agent, broker, or company has the responsibility to learn about You, Your financial situation, insurance needs and financial objectives.

If You sign this form, it means You know that you're buying an annuity that was not recommended.

Statement of Purchaser:

I understand that I am buying an annuity, but the agent, broker or company did not recommend that I buy it. If I buy it **without a recommendation**, I understand I may lose protections under the Insurance Code of Ohio.

Customer Signature

Agent (Producer) Signature

Date

Date



James K. Ruble Seminar

a proud member of Risk & Insurance Education Alliance

Section 5

There Cannot be a Crisis this Week



There Cannot be a Crisis This Week. My Schedule is Full.



LANCE J. EWING ARM, CRM, ERMP

1

Lance's Safe Harbor Statement

Certain information in this presentation may be considered forward-looking information within the meaning of the Private Securities Litigation Reform Act of 1995. This information is based on the Company's current expectations and actual results could vary materially depending on risks and uncertainties that may affect the Company's operations, markets, services, prices and other factors as discussed in filings with the Securities and Exchange Commission. These risks and uncertainties include, but are not limited to, industry and economic conditions, competitive, legal, governmental and technological factors. There is no assurance that the Company's expectations will be realized. The Company assumes no obligation to update any forward-looking information contained in this presentation should circumstances change, except as otherwise required by securities and other applicable laws.

Market data and other statistical information used throughout this presentation are based on independent industry publications, government publications, reports by market research firms or other published independent sources. Some data are also based on our good faith estimates which are derived from our review of internal surveys, as well as the independent sources listed above. Although we believe these sources are reliable, we have not independently verified the information and cannot guarantee its accuracy and completeness

**YOU CANNOT SUE ME IF
YOU BLINDLY BELIEVE
EVERYTHING YOU SEE HERE.**



2

What is the Upside of Crisis?



3

We Learned About Crisis at an Early Age



4



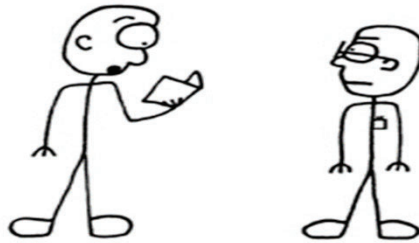
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6

What is Your Definition of Crisis?

Crisis Management Center



I'm not sure "everyone dies" is a great emergency plan.

10

Audience Interaction Time



Your Definition of Crisis?

11

Definition of Crisis

The Chinese character for "crisis" consists of two words, **danger** and **opportunity**.

The Greek definition of "crisis" means **decision**.

An **unstable or crucial time or state of affairs** whose outcome will make **a decisive difference for better or worse. A "turning point"**. (Webster's Dictionary).

Specific and non-routine events or series of events that create high levels of **uncertainty and threat or perceived threat** to an organization's **high priority goals**. (Wikipedia)

Any unplanned event or series of events that can cause **death or injury** to employees or the public or that can **disrupt operations, cause physical or environmental damage, shut down the organization, or threaten the organization's financial standing or public image**. (IRMI)

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Other Terms in Crisis Management

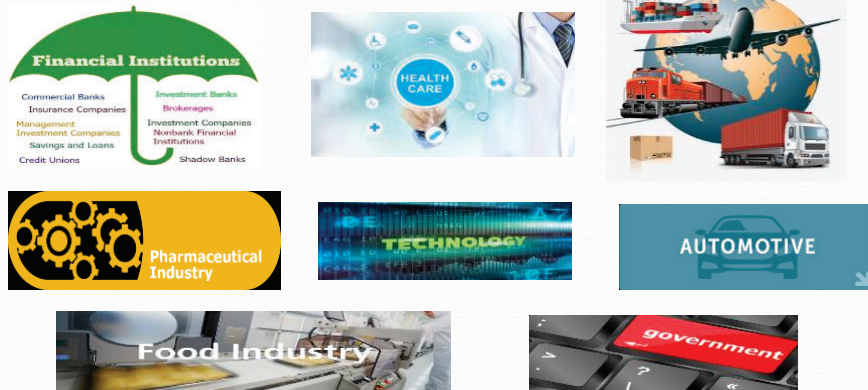
Crisis Management is the umbrella term that encompasses all activities involved when an organization prepares for and responds to a significant critical incident. The study of crisis management originated with the large-scale industrial and environmental disasters in the 1980s.

- **Emergency Response**
- **Disaster Recovery**
- **Business Continuity**
- **Crisis Communications**
- **Crisis Management Team**

13

What Industries are Most Crisis Prone?

The EIGHT most crisis-prone industries according to the Institute of Crisis Management are:



14

What are the TOP Concerns When a Company has a Crisis?

- Survival**
- Financial Impact**
- Reputation**
- Employee/Customer/Community**
- Insurance**
- Legal**
- Government**



15

Categorizing Crisis

Types of Crisis



Creeping Crises – foreshadowed by a series of events that decision makers don't view as part of a pattern.

Slow-Burn Crises – some advance warning, before the situation has caused any actual damage.

Sudden Crises – damage has occurred and will get worse the longer it takes to respond.

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Categorizing Crisis

1. Specific to Management (Examples):

- Violations of Rules, Laws & Regulations
- Financial/Stock Crisis
- Litigation/Defense
- Stupidity—Double Down

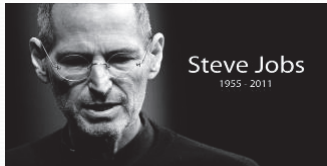
With its market capitalization cut by \$119 billion on Jul. 26, 2018, social media giant Facebook Inc. (FB) became the largest company to see a one-day decline in its stock price wipe more than \$100 billion from its [market cap](#).

17

Categorizing Crisis

2. Business Events (Examples):

- Employee death(s)
- Shortage of Product
- Loss of sole or main customer or supplier
- Product Recall/Defect



18

Categorizing Crisis

3. Criminal Events (Examples):

- Bombing
- Terrorist Act
- Kidnap or hostage situation
- Violence
- Civil Disturbance
- Live Shooter



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Categorizing Crisis

4. Disease or Epidemic (Examples):

- Outbreaks
- Water or Food contamination
- Quarantines



20



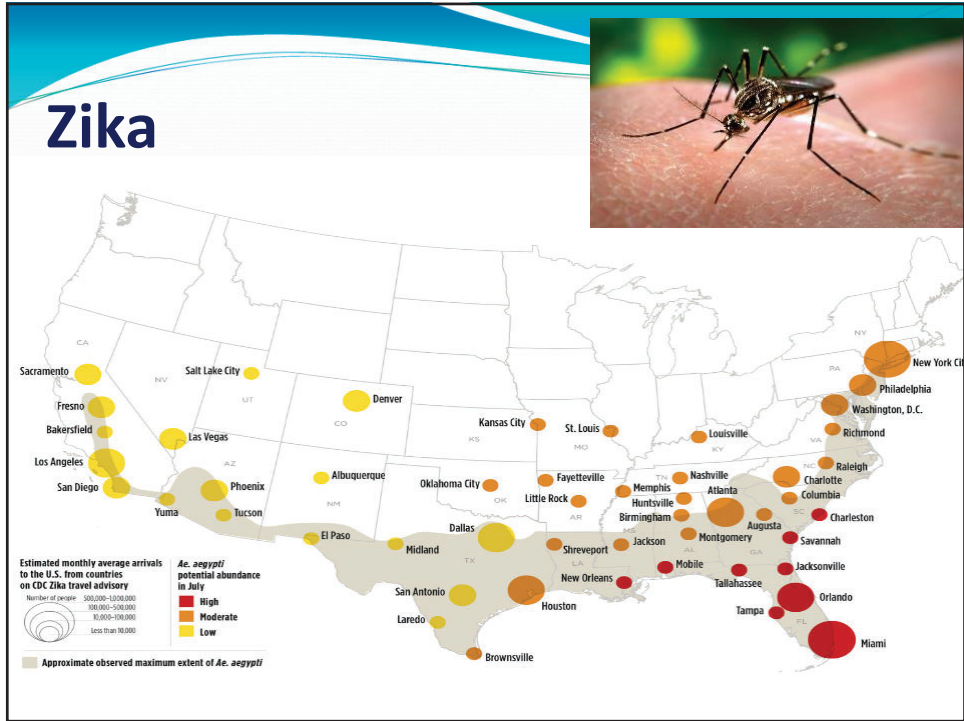
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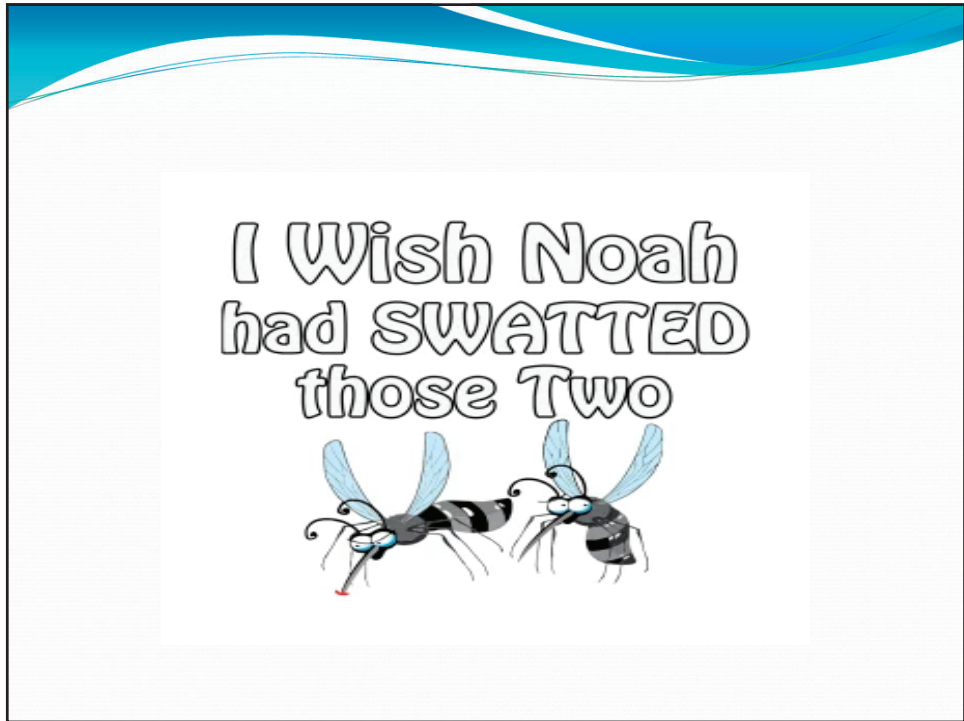
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23



24



25

Zika



**Workers Comp
Cancellation
Travel Insurance
GL Defense**



26

The Coronavirus Epidemic

**If you need 144 rolls
of toilet paper for
a 14 day quarantine
you probably should've
been seeing a Doctor
long before
COVID-19**



Daily UPDATES & information
SCHOOL CLOSURES
Continue to check this website for the latest information we are sharing about school closures.
www.fcusd.org/coronavirus



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Audience Interactive Time



Business Interruption
Workers Compensation
Property
GL

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Categorizing Crisis

5. Human Resources (Examples):

- Union rules/organization drives
- Walk outs
- Layoffs
- Closures
- Discrimination
- Franchisees

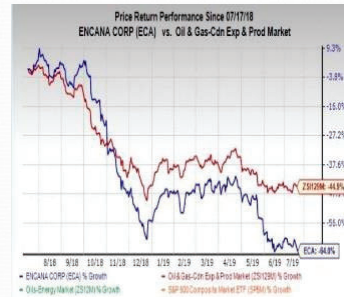


29

Categorizing Crisis

6. Operational Events (Examples):

- Property perils
- Utility failure
- Communications
- Governmental closures
- Market fluctuations



30

Categorizing Crisis

7. Technological (Examples):

- Cyber risks
- Drones
- Hacking
- ID Theft
- AI/Wearable Tech



- \$575,000,000+ settlement
- Free credit monitoring and identity theft services
- Strong data security requirements



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Categorizing Crisis

8. Nature Driven (Examples):

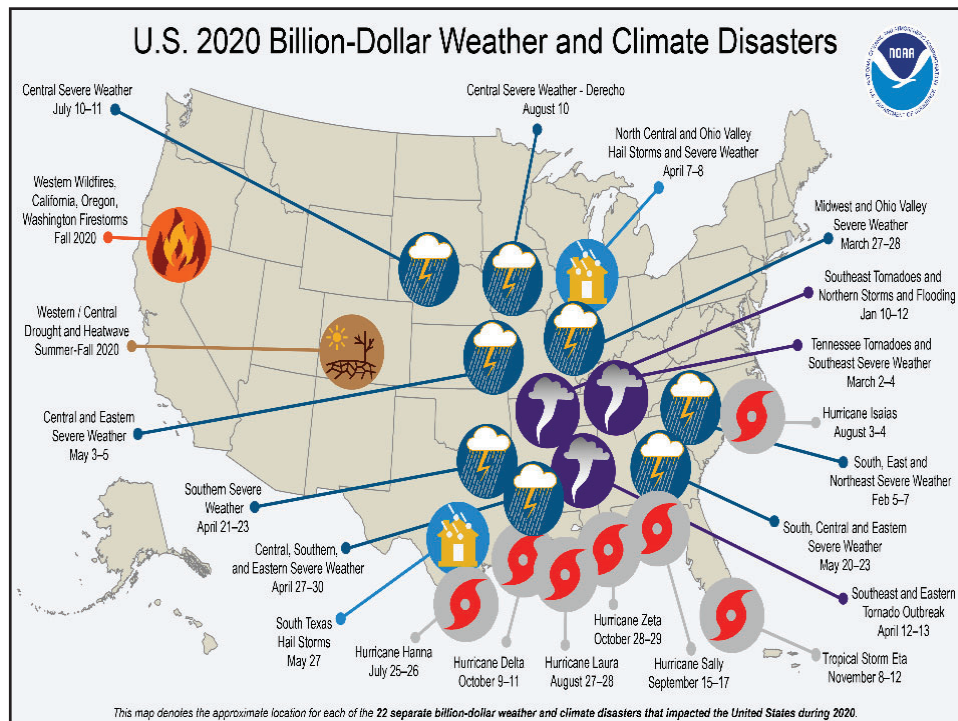
- Fire, Quake, Hurricane, Flood, Wind
- Inclement weather delays
- Crop losses



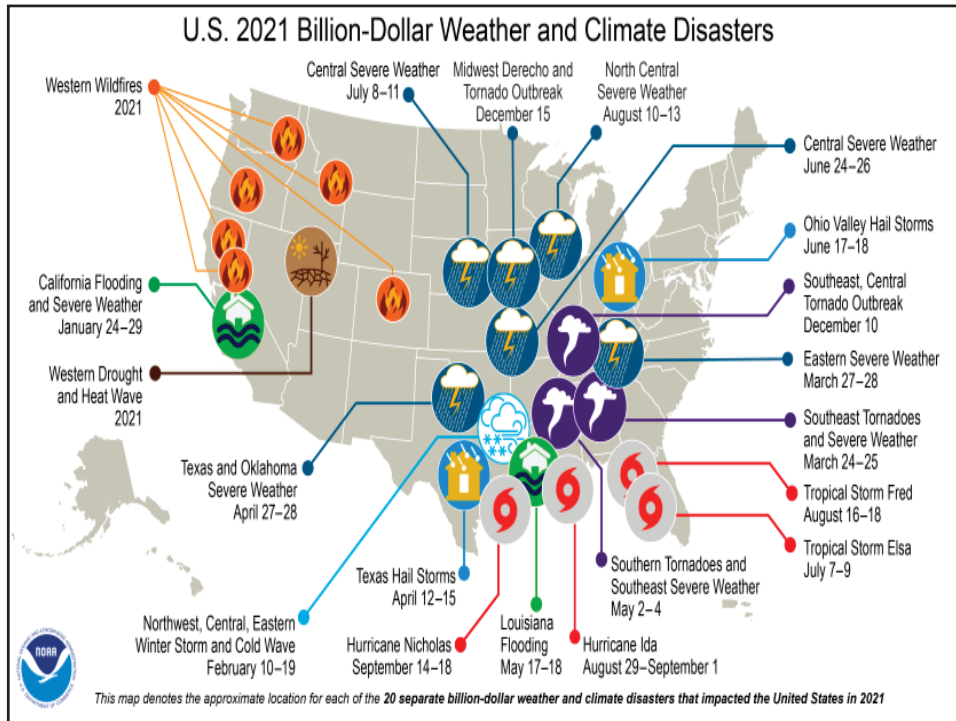
Bee decline threatens US crop production



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33



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No Matter the Category of the Crisis, Keep Your Sense of Humor

35

What Your Company and Your Clients Need for a Crisis

Leadership
Planning
Implementation & Prioritization of Plan
Expecting the Unexpected
Ethical Behavior (transparency)
Communication
Follow Up/Closure

**MOSTLY THEY NEED
YOUR ASSISTANCE**



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Start With Leadership

YOUR CRISIS MANAGEMENT TEAM (CMT)

The **Internal** CMT is comprised in most major companies of:

Risk Management
Finance (Accounting, Treasury, Investor Relations)
Design & Construction
IT
Communications
Human Resources
Marketing
Operations
Legal

**I'm a leader
not a follower.
unless it's a
dark place,
than you're
going first.**

37

Start With Leadership

YOUR CRISIS MANAGEMENT TEAM (CMT)

The **External** CMT is comprised in most major companies of:

- Brokers & Agents
- Insurance Carriers
- Service providers & vendors
- Utility companies
- Hospitals and Health care facilities
- Non-profit agencies (Red Cross)
- Emergency Response (police, fire, EMT)
- Governmental Agencies
- Public Relation Companies



38

Start With Leadership

YOUR CRISIS MANAGEMENT TEAM (CMT)

The EMT must be comprised of team members who possess:

- Knowledge & expertise of their areas
- Equipment & supplies
- Resourcefulness
- Decision making abilities
- Authority
- People skills (empathy)



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Start With Leadership

YOUR CRISIS MANAGEMENT TEAM (CMT)

Communication & Management styles vary in a crisis

No one person will be one type in a CRISIS

The four types to be aware of:

1. The Intimidator
2. The Relater
3. The Tactician
4. The Sanguine



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The Intimidator

*I LEAD
YOU FOLLOW*

Strong Personality

Very Direct and to the Point

Expert in ALL Areas

Results Only

“Time is Money”

MY BOSS SAID
I INTIMIDATE
COWORKERS.
I STARED
AT HIM
UNTIL HE
APOLOGIZED.



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The Relater

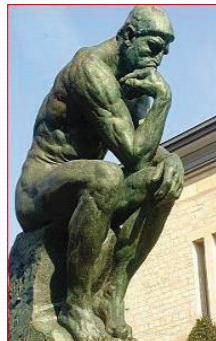
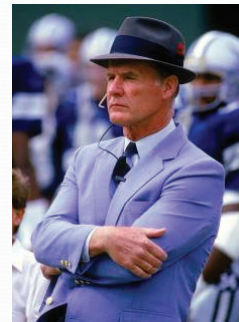
Team Builder
Personality
Consensus is Key
Supportive
Works Behind the
Scenes
"Why Can't We All
Just Get Along"



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The Tactician

Detail Oriented
Personality
Analytical Skill Set
Systems Work Best
Bit of Perfectionist
"Data and Numbers
Equal Knowledge"



43

The Sanguine

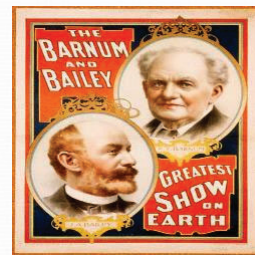
Charismatic & Charming

Opportunity Seeking Skill Set

Reaction Seeker

Works best with an Audience

“Leadership by Party”



SANGUINE

- | | |
|-------------|------------|
| CREATIVE | IMPULSIVE |
| SOCIABLE | FLEXIBLE |
| CHARISMATIC | EASY-GOING |
| SARCASTIC | FORGETFUL |
| SENSITIVE | TALKATIVE |

44

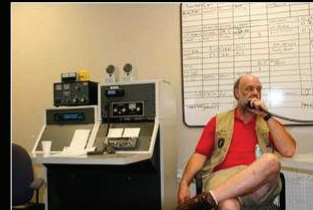
Emergency Manager



What my friends think I do



What my mom thinks I do



What my boss thinks I do



What the world thinks I do



What I think I do



What I actually do

45

Planning

YOUR CRISIS MANAGEMENT PLAN

Preparation: Ask what are the "black swans."

- Interview with the organization's executives and operations-level leaders
- Review of the company's past crises (and how they were handled)
- What peer or industry incidents have occurred
- Open-source research for geography, industry, weather, etc.
- Federal, State, regulatory issues
- Litigation
- Agents, brokers and carrier benchmarking



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Planning

YOUR CRISIS MANAGEMENT PLAN

Prioritize: Heat Map and Classify

- Tier all threat classifications
- Outline the best and worst responses approach and the follow-on tactical implementation appropriate for each tier.
- MUST have objective metrics such as the number of customers or visitors, time of day, external parties involved, potential financial impact, feedback/input from authorities, expected duration, and reputation risk factors
- Anticipate real-life situations in which new information or scenarios that changes the response dynamics.



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Planning

YOUR CRISIS MANAGEMENT PLAN

Practice: Organizations are best served when they “pressure test” the crisis plan and protocols through the implementation of crisis response drills or tabletop exercises.

These opportunities simulate the pace, multiplicity of issues, expecting the unexpected, resources and back ups as well as potential roadblocks requiring crisis management nimbleness.



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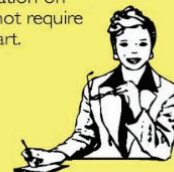
Planning

YOUR CRISIS MANAGEMENT PLAN

Rules for Conducting a Crisis Management Tabletop Exercise

- Rule 1 – SET OBJECTIVES. SIZE AND SCALABILITY.
- Rule 2 – WHO? INTERNAL AND EXTERNAL.
- Rule 3 – FACILITATOR IS A MUST.
- Rule 4 – KEEP THE SCENARIO REAL AND RELEVANT.
- Rule 5 – ADD THE UNEXPECTED.
- Rule 6 – DOCUMENT.
- Rule 7 – HOT WASH. SET ACTION PLAN AND TIMELINE.

A lack of preparation on your part does not require a crisis on my part.



your eCards
someecards.com

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Implementation and Prioritization of the Plan

“You know, I’d like my life back.”



Tony Hayward—one of the worst examples

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Implementation and Prioritization of the Plan

Launch Your Plan

- Personnel
- Resources
- Finances
- Support Partners
- Communications
- FACTS
- Prioritize/Re-prioritize



*"A good plan
violently
executed now is
better than a
perfect plan
executed next
week."*

George S. Patton

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Implementation and Prioritization of the Plan

Priority

- 1. An art
- 2. Risk Appetite
- 3. Cost Benefit Analysis
- 4. Synergy
- 5. Emergency and Time Constraint
- 6. Regulation
- 7. Reputation
- 8. Reducing Transaction Cost *

* Rent, mortgage, utilities, etc.



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Implementation and Prioritization of the Plan

The Eisenhower Priority Matrix

The matrix consists of four squares:

The first square contains the most important and urgent tasks that should be finished ASAP.

The second square includes very important but not so urgent tasks.


The third square represents a set of urgent but not very important tasks and activities.

The fourth square contains the tasks of the lowest priority both for their urgency and importance.

Important & Urgent	Urgent & Not important
Not urgent & Not important	Important & Not Urgent

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Expect the Unexpected



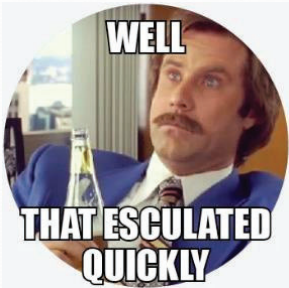
Plan for possible game changing events and have your team ready with an alternative play.

54

Expect the Unexpected

Remember These?

- Personnel
- Resources
- Finances
- Support Partners
- Communications
- FACTS
- Prioritize/Re-prioritize



Any of the above will not work, not show up, not produce, not cooperate, not be truthful, be delayed and be unplanned for by your team.

AND will come at the WORST possible time in the Crisis.

55

Expect the Unexpected

PLAN ON

- Situations to Change Hourly
- Crisis Team Members to Make Mistakes
- Outside Support Partners to Fail
- Facts to Have Inaccuracies
- The Media to Vilify You
- The Government to Blame You
- Other



Even After Tabletop or Actual Practice Crisis Exercises and "What If" Sessions Conducted Prior to the Crisis---**THE UNEXPECTED AND UNPLANNED WILL OCCUR**

56

Expect the Unexpected



Sorry, Madam. Your policy doesn't cover your house being swept away in a flood and burning down at the same time

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58



59

Expect the Unexpected

When someone says "expect the unexpected" slap them and then say "you didn't expect THAT did you?"

60

Ethical Behavior in Crisis Management

Bob Murray CEO..2007 Crandall Mine Disaster

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Ethical Behavior in Crisis Management

Build a solid foundation for your company with a robust compliance program

Code of Conduct	<ul style="list-style-type: none"> • Walk the walk • Not just talk the talk
Sunshine Rule	<ul style="list-style-type: none"> • Demand transparency • Expect problem solving
Right tone at the TOP	<ul style="list-style-type: none"> • Chief compliance officer • Regional compliance officers

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Ethical Behavior in Crisis Management

Strengthen your company's solid foundation of legal & ethical compliance with continuous training

Financial Reporting	Insider Trading	Export Compliance
Anti-Corruption/Gifts & Entertainment		Sexual Harassment
Code of Ethics		

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Ethical Behavior in Crisis Management



During the late 1970s, Beech-Nut Nutrition Corporation found out that it was the victim of a scam when it discovered its apple juice concentrate supplier was providing bogus apple juice.

This discovery was especially troublesome because Beech-Nut advertised its apple juice as "100% fruit juice, no sugar added," a claim that was, in fact, not true, given the fraudulent supplier.

At that point, Beech-Nut could have reported the incident, pleaded ignorance, and most likely escaped any prosecution since it was an innocent victim.

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Ethical Behavior in Crisis Management

However, this particular supplier was providing its product at 25 percent below the market rate, and the cost savings was too attractive for Beech-Nut executives to pass up.

The incident escalated to a smoldering crisis where Beech-Nut top executives concocted **an elaborate cover up scheme** and continued using the supplier. From 1977 to 1983, Beech-Nut sold its juice as 100% pure when, in fact, it was nothing more than a "100% fraudulent chemical cocktail," according to an investigator of the USDA.

What should have been a decision to change suppliers became an ethical misconduct crisis. Beech-Nut president Neils Hoyvald, and John Lavery, vice president for operations, were the main parties who instigated the cover up. **When the crisis was finally over, both men were found guilty of violating federal food and drug laws.**

The crisis that never should have happened cost Beech-Nut an estimated \$25M in fines, legal costs, and lost sales.

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Communication

Tips for Communicating with Employees During a Crisis

1. Be proactive. Prepare your message ahead of time (aka Holding Messages). Anticipate and plan for the communication to the employees prior to a crisis.
2. Get a team together. During the planning phase, identify your PR and communication leaders who will make up the crisis management communication team.
3. Don't expect employees to come to you. Implement a notification system that quickly reaches out to employees with accurate information and guidance.
4. Don't put up roadblocks. Trying to keep employees from communicating about crises via social media is futile. Instead, shape the message by giving them correct information in a timely manner.

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Communication

5. Act fast. But only say what you know to be true. Speed is of the essence when it comes to crisis communications, but it shouldn't come at the price of accuracy. Your employees will know when you are lying.
6. Don't go silent. If your organization is not yet ready to respond to an emergency, PR leaders should let staff know that the organization is gathering information and will follow up as soon as it can.
7. Test the message. Then test again. The most well-crafted communication plan won't be very helpful if employees have no idea what it is or how to use it. At least once a year, test the process to find out from workers what it does and doesn't do well, and then adjust accordingly.
8. Evaluate. Post-crisis communication assessments are as important as pre-crisis plans. After a crisis, review how the internal communication plan was executed. Determine what succeeded and what can be improved.

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Communication

Tips for Communicating with the Media During a Crisis

1. Establish sound relationships with the media in advance
2. Speaker must maintain credibility (CEO?)
3. Speaker must control the media dialogue
4. Employees and customers are important advocates and must be guided to follow same rules as other speakers
5. Do not discuss blame or shift responsibility for the situation

70

Communication

6. Forgetfulness can be forgiven, lies will not
7. Demonstrate empathy in the messaging
8. Emphasize the organizational measures being taken to protect lives and mitigate damage
9. Anticipate questions
10. Never say "no comment" or "off-the-record"

**'No comment'
is a comment.**

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Follow Up & Closure

This too shall pass... Painfully, like a kidney stone, but remember it'll pass!



your e cards
someecards.com

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Follow Up & Closure

Steps to Take After a Crisis

Make the review a standard, mandatory part of your crisis management efforts. Let team members and any others involved in managing the crisis know that you plan to seek their input when the crisis has passed.

That way, they can begin to record their observations during the event.

Timing is critical. Hold the review "after the smoke has cleared." Many organizations wait a week or four. This gives your team an opportunity to reflect on what happened and gain perspective.

It also allows you to see if any crisis-related developments surface shortly after the event (e.g. community outrage, sustained media coverage, litigation, etc.).

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Follow Up & Closure

Participants in the review should include all members of your crisis management team and any “seconds” to those individuals, appropriate executives (even if they weren’t on the team), and any others who were responders to the crisis. Top executive participation is especially important. If your leadership is too busy to attend, think of the message that sends out to others in the company.

Allow enough time for a meaningful review. For example, arbitrarily allotting thirty minutes for the meeting might be a mistake. Depending on the nature of the crisis and scope of the response, you might need several hours.

Monitor whether anything is being said about your company in the media. Include traditional news, social media and among customers and employees.

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Follow Up & Closure

Agendas review elements:

Review the event or issue, along with the key developments that led up to it and factors that accompanied it.

Examine whether the crisis was preventable. Was there anything that could have or should have been done differently?

Evaluate the team’s performance in managing the crisis. This involves looking at the two inseparable aspects of most crises: operations and communications. For example, did the team follow established procedures as outlined in the company’s crisis management plan? No fixing the blame but rather fixing the issues.

Identify the changes needed (e.g., in policies, procedures, plans, etc.). Establish timelines and action plans for their implementation.

75

Crisis Tabletop Teamwork



TEAMWORK

Working together towards a common goal... until a 'difference of opinion' gets someone dropped into molten lava.

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You are about to participate in a *Team Tabletop Exercise !!!!*

Objective

- Assess you and your company's readiness to respond to potential critical incident.

Tabletop Exercise

- Simulates a situation/incident in an informal, *stress-free* environment.
- Is designed to elicit discussion as participants examine and resolve problems based on existing programs, procedures and knowledge
- Is scenario driven
- Focuses on roles and responsibilities

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Assumptions

In any exercise, some assumptions and make believe are necessary to complete the process in the time allotted. During this exercise, the following apply:

- The scenario could *actually* occur
- Events occur as they are presented
- There are no “hidden agendas” or trick questions
- All participants receive scenario information at the same time.

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Stage 1 – Narrative

- It is 2:15 PM on a Tuesday, June 16th at the Ewing & Others Insurance Agency located at 115 Broad St., Erie, PA.
- The Agency is the largest independently owned and operated agency in town by volume.
 - The Agency has 12 shareholder producers, 9 non-shareholder producers and a total of 40 additional support employees.
 - The Agency occupies both floors of a reasonably new two-story building owned by the Agency.

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- A middle-aged white male enters the reception area of the agency. He brandishes a semi-automatic handgun and demands to know where Dudley DoRight is. Dudley is the agency's claims manager.
- Upon seeing the gun, the receptionist screams and is immediately shot in the chest. The gunman proceeds through the door to his right, yelling for DoRight. The commotion draws several people out of their offices, and he opens fire on each. In all, he fires 15 rounds from his handgun, before swapping the empty clip for a full one.
- Many office staffers and agency management quickly duck for cover while others run for exits on the side and rear of the main floor.

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- Workers on the agency's second floor hear the shots and quickly call 911 reporting a shooting in progress. They also attempt to barricade themselves into available offices.
- Before the first police units arrive, the gunman runs out a side door, into a blue SUV with PA plates and escapes from the scene.
- In addition to the receptionist, four other members of the agency are dead on the scene and four others are transmitted to area hospitals in critical condition.
- The list of victims include the Agency's Managing Partner, the CFO, the receptionist and an insurance carrier underwriter (non-employee who was in for a meeting), all were pronounced dead at the scene.

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Upon evacuating all survivors, the police immediately secure the entire facility as a “Crime Scene”.

Questions –

You are the ranking member of the firm that has not been injured. What is your...

- 1st Priority?
- 2nd Priority?
- 3rd Priority?
- With whom and how will you communicate following the incident?

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Stage 2 - Narrative

- The police commander in charge of the scene contacts the ranking member of the staff and advises that the entire agency building is considered an active crime scene and no one will be permitted into the building until they have completed their on-scene investigation, which is expected to be Monday of the following week.
- The local and national media are clamoring for interviews with the agency's employees.



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Stage 2 – Questions

You serve on the Agency's Management Committee

- What are your next steps?
- What information and instructions do you give to your producers and staff?
- With whom and how will you communicate following the incident?

84

Hot Wash

Now that the "situation" is over, let's conduct a **AFTER ACTION** review.

- Is it "reasonable" to assume that such an event could occur to a local independent insurance agency?
- Was this agency adequately prepared for this critical incident?
- How well did the agency's management team respond to issues involved?
- Communication is a critical requirement during and following a critical incident. How well did the agency manage the need to communicate with employees, customers, and vendors?

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Final Thought



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James K. Ruble Seminar

a proud member of Risk & Insurance Education Alliance

Section 6

Senior Insurance Solutions



Senior Insurance Solutions

Richard L. Goolsby, CIC
Loveland, OH

rickgoolsby@yahoo.com

I. Introduction

- A. The "Graying of America," (or "Who's Your Market?")
- B. Pressures on our health-care system
- C. Pressures on our ability to pay the costs
- D. Governmental reaction
 - 1. Medicare concerns
 - 2. Medicaid concerns

II. Medicare – How Does It Work?

FYI-- www.medicare.gov
The Official U.S. Government site for people with Medicare

- A. Four Parts of Medicare
 - 1. Medicare Part A – Hospital Insurance (HI) – premiums are paid by Social Security if the Medicare recipient is fully insured under Social Security (40 quarters of coverage, or 10 calendar years coverage) – if recipient has 30 to 40 quarters of coverage, monthly premium for Part A is \$285 – if recipient has less than 30 quarters of coverage, monthly premium is \$518.
 - 2. Medicare Part B – Supplemental Medical Insurance (SMI), or simply Medical Insurance (MI) – Part B is a voluntary program meaning recipient must pay a monthly premium for Part B – for 2025, monthly premium is \$185. Premiums are increased for recipients with higher income – See table on Page 2.

Find out if you'll pay a higher Part B premium in 2025:

If your yearly income in 2023 (for what you pay in 2025) was

File individual tax return	File joint tax return	File married & separate tax return	You pay each month (in 2025)
\$106,000 or less	\$212,000 or less	\$106,000 or less	\$185.00
above \$106,000 up to \$133,000	above \$212,000 up to \$266,000	Not applicable	\$259.00
above \$133,000 up to \$167,000	above \$266,000 up to \$334,000	Not applicable	\$370.00
above \$167,000 up to \$200,000	above \$334,000 up to \$400,000	Not applicable	\$480.90
above \$200,000 and less than \$500,000	above \$400,000 and less than \$750,000	above \$106,000 and less than \$394,000	\$591.90
\$500,000 or above	\$750,000 or above	\$394,000 or above	\$628.90

FOUR PARTS OF MEDICARE (cont.)

3. Medicare Part C – Medicare Advantage – Medicare Managed Care – Recipient relinquishes Original Medicare (Parts A and B) and enrolls in a Medicare participating HMO or PPO in his or her service area – Medicare becomes a premium payor to the HMO or PPO – Recipient owes premiums subject to HMO or PPO premiums charges in addition to Medicare capitations. **Note: plans may not charge a premium to recipient.**
4. Medicare Part D – Prescription Drug Coverage – offered through private insurance companies – premiums and covered formularies vary by plan.

B. Medicare Part A, Hospital Insurance (HI) – How Does It Work?

1. Inpatient hospital care
 - a. A 90-day Benefit Period starts on the first day of hospitalization, and ends on the 61st day after release from .
 - b. During the first 60 days of hospitalization, the **full current deductible** is payable by the patient one time – the full current deductible for 2025 is \$1,676.
 - c. From the 61st day to the 90th day, **one fourth of the current deductible** is payable **per day** – or **\$419 per day**.
 - d. If the patient exhausts a 90-day benefit period, he or she has 60 lifetime reserve days.
 - e. If used, lifetime reserve days are not renewable.
 - f. During lifetime reserve days, **one half the current deductible** is payable **per day** by the patient – or **\$838 per day**.

MEDICARE PART A – HOW DOES IT WORK? (cont.)

2. Skilled Nursing Facility care
 - a. Medicare pays for up to 100 days in a Medicare-approved Skilled Nursing Facility.
 - (1). Reasonable charges (approved by Medicare) for the first 20 days are paid in full with no deductible applied.
 - (2). Reasonable charges for the 21st through 100th days are paid subject to a coinsurance amount equal to **one eighth the current deductible per day** – patient pays **\$209.50 per day**.
 - b. Skilled Nursing Facility Care is available only if the patient is first hospitalized for *three days* prior to being transferred to the Skilled Nursing Facility.
 - (1). Treatment the patient is receiving must be medically necessary care as prescribed by a doctor.
 - (2). AND patient's prognosis must be improving health.
3. Home health care – as long as you need part-time intermittent nursing care and are homebound.
 - a. Eligible expenses include: intermittent *part-time* nursing care (such as wound care for pressure sores or surgical wound, patient and caregiver education, intravenous or nutrition therapy, injections, or monitoring serious illness and unstable health status); physical, occupational, or speech therapy; home health aides; medical social services; medical supplies; 80% of certain durable medical equipment.
 - b. *Ineligible* expenses include: housekeeping services, meal preparation or delivery, shopping, full-time nursing care, blood transfusions, drugs, or biologicals; CUSTODIAL CARE IS NOT COVERED.

MEDICARE PART A – HOW DOES IT WORK? (cont.)

- c. Home care must still be “part time and intermittent”; part time is defined as less than eight hours per day and less than 28 hours in any week (up to 35 hours per week can be ordered on a case-by-case basis); intermittent means care that is given *less* than seven days per week, or a period of care (including seven-day-per-week care) lasting less than 21 days.
 - 4. Hospice care
 - a. Medicare pays virtually all costs for hospice treatment, with no deductible.
 - b. Recipient must be diagnosed as terminally ill with six months life expectancy.
 - b. Payments are made for pain relief and symptom management; *NO PAYMENTS FOR CURATIVE TYPE TREATMENTS.*
 - c. Two services require co-payments:
 - (1). Prescription drugs have a 5% or \$5 deductible, whichever is less;
 - (2). Respite care is subject to a copayment of 5% of the Medicare-approved rate up to a specified dollar amount which changes annually.
- C. Medicare Part B -- Supplemental Medical Insurance (SMI)
 - 1. Part B provides benefits for three types of medical services:
 - a. Doctors' services
 - b. Home health care (if not covered by Part A)
 - c. Outpatient medical services and supplies

MEDICARE -- HOW DOES IT WORK? -- Medicare Part B, SMI (cont.)

2. Part B is an optional benefit program of medical services – premium for Part B is deducted from recipient's Social Security benefits.
3. Part B has a calendar-year deductible and a copayment percentage (20%) of *all* covered charges, plus a three-pint deductible for blood – 2025 deductible is \$257.
4. Part B covers most physicians' services, regardless of setting in which services are rendered. See Exhibit I, page 7.
5. Home Health Care Services are covered by Part B only if the patient is NOT covered by Medicare Part A.
6. Outpatient Medical Services and Supplies are covered by Medicare Part B. See Exhibit II, page 8.

Exhibit 1

Doctors' Services specifically covered by Medicare Part B:

1. Medical and surgical services, including anesthesia;
2. Office visits, house calls, and hospital calls;
3. Radiological and pathological services provided by a physician;
4. Medical supplies;
5. Second surgical opinions;
6. Diagnostic tests that are part of patient's treatment;
7. X-rays;
8. Physical, occupational, and speech therapy;
9. Blood transfusions;
10. Drugs and biologicals that cannot be self-administered

Doctors' Services specifically excluded by Medicare Part B:

1. Routine physical exams and related tests;
2. Routine foot care, including treatment for flat feet and for subluxations of the foot;
3. Eye exams, including fitting of eyeglasses or contact lenses;
4. Hearing exams, including fitting of hearing aids;
5. Most types of dental care;
6. Most immunizations;
7. Drugs or biologicals which can be *self-administered*;
8. Cosmetic surgery, unless required as result of injury or congenital defect

Exhibit 2

Outpatient Medical Services and Supplies specifically covered by Medicare Part B:

1. Outpatient clinic services;
2. Emergency room services;
3. X-rays for therapy or diagnosis;
4. Medically necessary ambulance services;
5. Purchase or rental of durable medical equipment;
6. Artificial limbs and eyes;
7. Braces, casts, splints, and surgical dressings;
8. Blood transfusions;
9. Outpatient physical, occupational, and speech therapy;
10. Drugs that cannot be self-administered

Outpatient Medical Services and Supplies specifically excluded by Medicare Part B:

1. Routine physical exams and related tests;
2. Eye exams, including fitting of eyeglasses and contact lenses;
3. Hearing exams, including fitting of hearing aids;
4. Most immunizations;
5. Routine foot care

MEDICARE -- HOW DOES IT WORK? (cont.)

- D. Medicare Part C, known as Medicare Advantage, was created by the Balanced Budget Act of 1997.
1. This is an expansion of Medicare managed care.
 2. Medicare Advantage plans can be structured as HMOs, PPOs, and other coordinated care plans; plans that coordinate with Medical Savings Accounts; and as private fee-for-service plans.
 3. Benefits offered are similar to Medicare Parts A and B, with the exception of hospice benefits.
 4. These are capitated plans with the senior paying premiums set by the managed care organization; the federal government then makes monthly payments to the Medicare Advantage plan in the capitated amount.
- E. Medicare Part D – Prescription Drug Coverage – Can be added to Original Medicare (Parts A and B) – ***not available in conjunction with Medicare Part C – Medicare Advantage***
1. Standard Coverage is the minimum coverage drug plans must provide.
 2. How the plan works:
 - a. Two ways to get Medicare prescription drug coverage
 - (1). Medicare Prescription Drug Plans
 - (2). Medicare Advantage Plans
 - b. Joining a Plan
 - (1). Initial Enrollment Period
 - (2). General Enrollment Period (April 1 - June 30, with coverage beginning July 1)
 - (3). Open Enrollment (Oct 15 – Dec 7, with coverage beginning Jan 1)
 - (4). Special Enrollment (move out of service area, lose other creditable coverage, live in an institution, have Medicaid, or qualify for Extra Help)

MEDICARE PART D – PRESCRIPTION DRUG COVERAGE (cont.)

- c. Monthly premiums are based on the drug plan chosen and recipient's annual income

Find out if you'll pay a higher Part D premium in 2025:

If your filing status and yearly income in 2023 was

File individual tax return	File joint tax return	File married & separate tax return	You pay each month (in 2025)
\$106,000 or less	\$212,000 or less	\$106,000 or less	your plan premium
above \$106,000 up to \$133,000	above \$212,000 up to \$266,000	not applicable	\$13.70 + your plan premium
above \$133,000 up to \$167,000	above \$266,000 up to \$334,000	not applicable	\$35.30 + your plan premium
above \$167,000 up to \$200,000	above \$334,000 up to \$400,000	not applicable	\$57.00 + your plan premium
above \$200,000 and less than \$500,000	above \$400,000 and less than \$750,000	above \$106,000 and less than \$394,000	\$78.60 + your plan premium
\$500,000 or above	\$750,000 or above	\$394,000 or above	\$85.80 + your plan premium

Premium amounts listed don't include any late enrollment penalties.

MEDICARE PART D – PRESCRIPTION DRUG COVERAGE (cont.)

- d. Benefits – Medicare drug plans and Medicare Advantage Plans with drug coverage have 3 stages (*the following information was taken from the [Medicare.gov](https://www.medicare.gov) website*):

Deductible stage: If your Medicare plan has a deductible, you pay all out-of-pocket costs until you reach the full deductible. No Medicare drug plan may have a deductible more than \$590 in 2025. Some Medicare drug plans don't have a deductible.

Initial coverage stage: After you reach your full deductible (if your plan has a deductible), you'll pay 25% of the cost as coinsurance for your generic and brand-name drugs until your out-of-pocket spending on covered Part D drugs reaches \$2,000 in 2025 (including certain payments made on your behalf, like through the Extra Help program). Then, you'll automatically get "catastrophic coverage."

Catastrophic coverage stage: You won't have to pay out-of-pocket for covered Part D drugs for the rest of the calendar year.

Visit [Medicare.gov/find-a-plan](https://www.medicare.gov/find-a-plan) to get information on specific drug plan costs, and call the plans for more details

F. Medicare Supplement (Medigap) Coverage

1. Sources of coverage
 - a. My nest egg (paid out of retirement savings)
 - b. Medicaid -- Do I REALLY want to go there?
 - c. Group coverage through the retiree's employer-sponsored benefit plan
 - d. Group coverage through an association-sponsored benefit plan (e.g. AARP)
 - e. Coverage through an HMO
 - f. Private insurance plan
2. Standardized Medicare Supplement Benefits – Chart on Page 13

How do I compare Medigap policies?

The chart below shows basic information about the different benefits that Medigap policies cover. If a percentage appears, the Medigap plan covers that percentage of the benefit, and you're responsible for the rest.

Medicare Supplement Insurance (Medigap) plans										
Benefit	A	B	C	D	F*	G	K	L	M	N
Medicare Part A coinsurance and hospital costs (up to an additional 365 days after Medicare benefits are used)	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Medicare Part B coinsurance or copayment	100%	100%	100%	100%	100%	100%	50%	75%	100%	100% **
Blood (first 3 pints)	100%	100%	100%	100%	100%	100%	50%	75%	100%	100%
Part A hospice care coinsurance or copayment	100%	100%	100%	100%	100%	100%	50%	75%	100%	100%
Skilled nursing facility care coinsurance			100%	100%	100%	100%	50%	75%	100%	100%
Part A deductible		100%	100%	100%	100%	100%	50%	75%	50%	100%
Part B deductible			100%		100%					
Part B excess charges					100%	100%				
Foreign travel emergency (up to plan limits)			80%	80%	80%	80%			80%	80%
							Out-of-pocket limit in 2018			
							\$5,240	\$2,620		

* Plan F also offers a high-deductible plan in some states. If you choose this option, this means you must pay for Medicare-covered costs (coinsurance, copayments, and deductibles) up to the deductible amount of \$2,240 in 2018 before your policy pays anything.

** Plan N pays 100% of the Part B coinsurance, except for a copayment of up to \$20 for some office visits and up to a \$50 copayment for emergency room visits that don't result in an inpatient admission.

MEDICARE -- HOW DOES IT WORK? (cont.)

- G. Medicare Advantage Plans (Medicare C)
 - 1. Sometimes referred to as Medicare Managed Care
 - 2. Medicare recipient must have Part A and B
 - 3. Medicare recipient must live in the service area of a participating HMO.
 - 4. If Medicare recipient enrolls in a Medicare Advantage Plan and he/she has a Medigap policy, he/she should drop the Medigap policy.

NOTE: If covered by a Medicare Advantage Plan, and participant enrolls in a Medicare Part D, Prescription Drug Plan, participant will be dis-enrolled in the Medicare Advantage Plan.

III. Long Term Care

A. Medicaid -- How Does It Work?

1. Federal-State program -- pays health care benefits for low-income persons.
 - a. Individuals become eligible for Medicaid by having income and assets at or below poverty level; amounts vary by state.
 - b. Approximately 57% of Medicaid's costs are funded federally; 43% are funded by the states.
2. Availability of Medicaid
 - a. Medicaid is available to Americans who can satisfy the eligibility requirement of low income and little or no assets.
 - b. Prior to the Medicare Catastrophic Act of 1989, low income and asset requirements included both spouses; the healthy spouse (at-home spouse) was often left near bankruptcy.
 - c. Medicare Catastrophic Act of 1989 established a minimum monthly income and shelter allowance for the at-home spouse.
 - (1). Income and shelter allowance is based on whether recipient(s) is/are single (\$2,250) or married (\$3,000), and varies from state to state.
 - (2). Half the couple's assets up to \$157,920 (for 2025) are protected for the at-home spouse; the figure is indexed to inflation and will change in future years.
 - (3). **Numbers shown here are based on Ohio Medicaid eligibility.** (Refer to your home state's eligibility rules for your numbers.)

2025 Min. and Max. Monthly Maintenance Needs Allowance Figures by State – Effective Jan. 1, 2025

Alabama	\$2,555 – standard figure
Alaska	\$3,948 – standard figure
Arizona	\$2,555 – \$3,948
Arkansas	\$2,555 – \$3,948
California	\$3,948– standard figure
Colorado	\$2,555 – \$3,948
Connecticut	\$2,555 – \$3,948
Delaware	\$2,555 – \$3,948
District of Columbia	\$3,948– standard figure
Florida	\$2,555 – \$3,948
Georgia	\$3,948 – standard figure
Hawaii	\$3,948– standard figure
Idaho	\$2,555 – \$3,948

Illinois	\$3,948- standard figure
Indiana	\$2,555 - \$3,948
Iowa	\$3,948- standard figure
Kansas	\$2,555 - \$3,948
Kentucky	\$2,555 - \$3,948
Louisiana	\$3,948- standard figure
Maine	\$2,555 - \$3,948
Maryland	\$2,555 - \$3,948
Massachusetts	\$2,555 - \$3,948
Michigan	\$2,555 - \$3,948
Minnesota	\$2,555 - \$3,948
Mississippi	\$3,948 - standard figure
Missouri	\$2,555 - \$3,948
Montana	\$2,555 - \$3,948

Nebraska	\$2,555 – \$3,948
Nevada	\$3,948– standard figure
New Hampshire	\$2,555 – \$3,948
New Jersey	\$2,555 – \$3,948
New Mexico	\$2,555 – \$3,948
New York	\$3,948– standard figure
North Carolina	\$2,555 – \$3,948
North Dakota	\$2,555 – standard figure
Ohio	\$2,555 – \$3,948
Oklahoma	\$3,948– standard figure
Oregon	\$2,555 – \$3,948
Pennsylvania	\$2,555 – \$3,948
Rhode Island	\$2,555 – \$3,948
South Carolina	\$3,948– standard figure

South Dakota	\$2,555 – \$3,948
Tennessee	\$2,555 – \$3,948
Texas	\$3,948– standard figure
Utah	\$2,555 – \$3,948
Vermont	\$2,555 – \$3,948
Virginia	\$2,555 – \$3,948
Washington	\$2,555 – \$3,948
West Virginia	\$2,555 – \$3,948
Wisconsin	\$3,406.66 – \$3,948
Wyoming	\$3,948– standard figure

Long Term Care – Availability of Medicaid (cont.)

- d. Exempt assets
 - (1). The house (given that the Medicaid applicant or spouse resides in the house), and value is under \$730,000 in 2025;
 - (2). One automobile;
 - (3). Household and personal belongings;
 - (4). Irrevocable Burial Trusts

3. Qualifying for Medicaid benefits

- a. The individual needs and receives long term care in a nursing home, at a private residence (e.g. a relative's house,) or in an assisted living facility;
- b. The patient files for Medicare benefits in the event Medicare will reimburse costs;
- c. If private insurance exists, a claim must be filed with the insurer;
- d. The patient then starts spending and exhausts his/her money and assets;
- e. The patient files a claim for Medicaid benefits.

Long Term Care – Availability of Medicaid (cont.)

4. Reconfiguration (asset transfer)
 - a. Medicare Catastrophic Act of 1989
 - (1). Required assets to be transferred *30 months* before the need for care;
 - (2). Imposed a waiting period of 30 months before Medicaid would begin to pay.
 - b. Omnibus Budget Reconciliation Act of 1993
 - (1). Changed the time period for property transfers (shifting assets) from 30 months to *36 months* before applying for Medicaid benefits;
 - (2). Assets transferred to an irrevocable trust must be accomplished *60 months* before applying for Medicaid;
 - (3). The maximum penalty period of 30 months is replaced by a penalty period of any length as determined by the amount of assets involved in the transfer. **See Exhibit III**
 - (4). The states are granted greater powers of recovery: they can recover against a Medicaid beneficiary's entire estate, including his or her share of "financial assets" such as trusts.

Exhibit 6

Under OBRA 1993 (Omnibus Budget Reconciliation Act of 1993,) Medicaid was granted authority to impose penalty periods of any length when property transfers were completed to gain eligibility for Medicaid. When the transfer is completed within thirty-six months *prior* to the need for long term care (the look-back period,) Medicaid can impose a penalty period determined by the amount of assets transferred compared to the cost of nursing home care in the patient's area of residence.

Example

Robert Jones transfers assets on January 15, 2003, of \$300,000
Mr. Jones must be placed in a nursing home on January 1, 2004
Average cost of long term care in Mr. Jones's state of residence is \$4,000 (mo.)
Mr. Jones must wait seventy-five (75) months from the date of transfer before Medicaid will begin paying for long term care
(\$300,000 transferred assets divided by \$4,000 monthly cost of long term care equals **75 months**)
Mr. Jones begins receiving benefits from Medicaid after April 15, 2009, or seventy-five months after the transfer of assets has been completed

Long Term Care – Availability of Medicaid – Reconfiguration (cont.)

- c. Health Insurance Portability and Accountability Act of 1996
 - (1). HIPAA makes asset transfers, in some cases, a federal crime if the transfer is completed to qualify for Medicaid.
 - (2). The law establishes three conditions:
 - (a). Transfer must be to someone other than the individual's spouse;
 - (b). The transfer must be done willingly and purposefully to qualify for Medicaid;
 - (c). The transfer must trigger an ineligibility period (36 or 60 months.)
 - (3). The penalty was a possible jail sentence and/or fines for the person whose assets were transferred.
- d. Balanced Budget Act of 1997
 - (1). The act relieves the responsibility of the person whose assets are transferred.
 - (2). The penalties are now directed to the planner who assists in asset transfer.

Long Term Care (cont.)

B. Sources of Long Term Care Benefits

1. My nest egg (paid out of retirement savings or other assets);
2. Medicaid -- Do I REALLY want to go there?;
3. Group coverage through the employer -- IF the employer makes it available;
4. Group coverage through an association-sponsored plan (e.g. AARP);
5. PPO or HMO coverage;
6. Private insurance
 - a. Long Term Care
 - (1). Nursing home care
 - (2). Home health care
 - b. Living benefits from life insurance policies;
7. Viatical settlements;
8. State Partnership Plans

Long Term Care (cont.)

C. How Does Long Term Care Work?

1. Levels of Long Term Care

- a. Skilled Nursing Care -- 24-hour nursing service subject to periodic review by a physician and nurse; care is provided in a state-licensed facility which provides nursing care and related services to inpatients with a licensed physician available for emergency medical care; facility has at least one full-time nurse, and a nurse always on duty or on call, to appropriately handle and administer drugs and biologicals, and to maintain clinical records for all patients.
- b. Intermediate Nursing Care -- care provided only on an OCCASIONAL basis and in a state-licensed facility which provides nursing care and related services to in-patients with a licensed physician available for emergency medical care; facility has at least one full-time nurse, and a nurse on duty or on call, to appropriately handle and administer drugs and biologicals, and to maintain clinical records for all patients.
- c. Custodial Care -- adult day care provided in a legally operated and state-licensed (if required) facility which provides such care at least five days a week; facility's staff must include a full-time director, one or more nurses present at least four hours per day and enough full-time staff for a client-to-staff ratio of 8 to 1 or less; not an over-night facility.
- d. Home Care -- may include all the levels of care discussed above, but performed in the patient's home rather than in a nursing facility; in addition to providing help with Activities of Daily Living (ADLs), may also include help with housework and certain types of therapy.

Long Term Care – How Does Long Term Care Work? (cont.)

2. Activities of Daily Living (ADLs)
 - a. Transferring;
 - b. Bathing;
 - c. Toileting;
 - d. Continence;
 - e. Dressing;
 - f. Eating;
 - g. Assistance with medication
3. Cognitive Impairment (Alzheimer's Disease) – benefits can be triggered by diagnosis of cognitive impairment. Certain standardized tests may be required to identify the extent or progression of the impairment before benefits are triggered.
4. Long Term Care Policy Provisions
 - a. Guaranteed renewability
 - b. Premiums -- policies are typically issued with level premiums.
 - c. Premium increases may be permitted in the states as long as premium increases are based on claims experience of the insurer, and premiums are increased as a class.
 - d. Thirty-day free look
 - e. No prior hospitalization requirement
 - f. Covered level of care -- CAUTION!
 - g. Home health care
 - h. Adult day care
 - i. Respite care

Long Term Care – How Does Long Term Care Work? (cont.)

- j. Benefit amount
- k. Benefit periods
- l. Elimination periods
- m. Waiver of premium
- n. Inflation protection
- o. Exclusions
 - (1). Pre-existing conditions -- usually limited to conditions for which treatment was sought or received within the six months prior to application for coverage; coverage for those conditions does not apply until six months after policy issue have elapsed. *Some plans do not exclude pre-existing conditions at all.*
 - (2). War, or acts of war;
 - (3). Intentionally self-inflicted injuries;
 - (4). Mental illness and nervous disorders;

NOTE: Alzheimer's Disease and other *organically-based* mental illnesses or disorders **MAY NOT** be excluded from coverage.
 - (5). Alcohol or drug dependency;
 - (6). Treatments provided to the insured without cost (e.g., Veterans benefits)
 - (7). Out-of-country confinements
 - (8). Coordination of benefits -- maybe

Long Term Care – How Does Long Term Care Work? (cont.)

D. Insurance Options -- Qualified vs. Nonqualified Long Term Care Plans

1. HIPAA HIPAA Hooray – ???

a. Health Insurance Portability and Accountability Act of 1996 provided, in addition to health insurance portability, tax clarification of long term care insurance plans. A qualified plan provides:

- (1). Premiums are deductible as a medical expense to individuals who itemize, subject to limitations;
- (2). Benefits received by a claimant are tax-free subject to some per diem limitations;
- (3). Employers paying premiums on behalf of an employee are entitled to deduct those premiums as a business expense;
- (4). Premiums paid by an employer on behalf of an employee will not be treated as income to that employee.
- (5). There's a catch:
 - (a). The taxpayer must itemize, which means that total expenses for medical purposes must exceed 7.5% of adjusted gross income;
 - (b). Deductible premiums for Tax Year 2024 are limited as follows:

<i>Attained Age*</i>	<i>Limitation**</i>
Less than 41	\$ 470
41 - 50	880
51 - 60	1,760
61 - 70	4,710
over 71	5,880

***Age is defined as age attained before the close of the taxable year.**

****Limitation amounts are indexed annually.**

NOTE: The limit on premiums is for each person.

HEALTH INSURANCE PORTABILITY AND ACCOUNTABILITY ACT (cont.)

- (6). HIPAA also allows self-employed individuals to deduct (subject to limitations) the cost of their health insurance, *which now includes long term care premiums.*
- b. HIPAA also added more rules to define long term care insurance for the purposes of standardizing what expenses (including distributions from a long term care policy) would qualify under this new tax status:
 - (1). A per diem cap is imposed on the amount of long term care expenses that are deductible. The per diem amount is adjusted annually for inflation.

CAUTION -- Indemnity (per diem) vs. expense incurred: insureds who purchase coverage amounts on indemnity policies in excess of \$190 per day will incur a taxable event at claim time because indemnity policies pay benefits *regardless* of the amount of the actual costs of care; an exception would occur in the event the actual expenses exceed the amount of coverage. If an insured owns both an indemnity contract and an expense incurred contract the \$190 amount is reduced by any amounts paid under the expense incurred plan. SEE EXHIBIT 7, ON PAGE 30.

- (2). Long Term Care insurance is excluded from use in Section 125 Cafeteria Plans.

LONG TERM CARE -- HIPAA Definitions (cont.)

- (3). Long Term Care policies which pay on an expense-incurred basis may coordinate benefits with Medicare to avoid duplicative reimbursement. This overrides an initiative from the Health Care Financing Administration which required LTC insurance to be primary and to pay first before Medicare.
- (4). Insurers must offer a non-forfeiture benefit for plans to be considered as tax-favored if the policy has no cash surrender value in the event of policy lapse or death of the insured.
- (5). HIPAA establishes benefit triggers in Long Term Care insurance that is to be qualified (*italics added for emphasis*):
 - (a). Inability to perform two out of six Activities of Daily Living (ADLs) due to loss of functional activity *that will last at least 90 days*;
 - (b). Requiring substantial supervision to protect the insured from threats to health and safety due to *severe* cognitive impairment;
 - (c). *Having a similar level of disability as determined by the Secretary of the Treasury in consultation with the Secretary of Health and Human Services.*
 - (d). The six ADLs are: transferring, bathing, toileting, continence, dressing, and eating.

NOTE: The seventh ADL recognized by many insurers is Assistance with Medication and is not recognized by HIPAA as an ADL.

E. Partnership Programs

1. In 1987, the Robert Wood Johnson Foundation funded a study by the state of Connecticut to explore the feasibility of a long term care program funded by a partnership between the state and private insurers. The reasoning behind this study was that Medicaid would not be able to continue to fund long term care for an aging American population. Therefore, to prevent bankruptcy of the Medicaid system, such a partnership involving the state, consumers, and the insurance industry was perceived as a means to keep Medicaid in place to provide long term care benefits for the beneficiaries for which it was originally intended: the poor.

2. The KEY to Partnership Plan success is *asset protection*.

a. Individuals purchasing Partnership policies receive dollar-for-dollar asset protection in the event long term care is needed.

FOR EXAMPLE: a person purchases a Partnership policy with benefits of \$50,000, and then needs long term care. The Partnership policy responds first, and pays until it is exhausted. Once Partnership benefits are exhausted, the patient spends down assets to qualify for Medicaid benefits, but the patient may keep \$50,000 of assets which were protected by the Partnership policy.

b. The obvious benefit is to the patient who has protected some or all of his assets.

c. The state benefits because Partnership benefits must be exhausted *before* any Medicaid funding is provided. Because some patients will not outlive policy benefits, no Medicaid funding would be needed.

Exhibit 8

How Does Asset Protection Work in State Partnership Plans?

	Personal Assets	Partnership Benefits	Medicaid Countable Assets
<i>Patient #1</i>	\$75,000	\$75,000	-0-
<i>Patient #2</i>	\$200,000	\$200,000	-0-
<i>Patient #3</i>	\$500,000	\$250,000	\$250,000
<i>Patient #4</i>	\$500,000	-0-	\$500,000

LONG TERM CARE -- Partnership Programs (cont.)

3. Partnership Plans were originally established in only five states: Connecticut, California, Indiana, Iowa, and New York.
4. These five states had Partnership Plans in effect before OBRA 1993 was passed, so these states were permitted to continue to offer Partnership policies.
5. The OBRA window re-opened in 2008, and all states with the exception of Mississippi, New Mexico, and Hawaii have made Partnership protections available.
6. The Partnership Plans have common goals in the states in which they have been established. *SEE EXHIBIT 9.*
7. There is a major drawback to Partnership Plans: to receive asset protection, the patient must receive long term care in the state in which the Partnership policy was purchased.

FOR EXAMPLE: An Indiana resident purchases an Indiana Partnership policy, and subsequently retires to Florida. To receive asset protection from Medicaid spend down, the individual must return to Indiana at the time long term care is needed. The State of Florida would not recognize the asset protection provided by the Indiana policy.

Exhibit 9

Goals of the Partnership Program

- A. Require New Product and Consumer Protection Standards**
- B. Reduce the Fear of Impoverishment**
- C. Slow the Growth of Medicaid Expenditures**
- D. Encourage Public Understanding and Participation**

IV. Ethics and Long Term Care Insurance

A. Suitability

1. National Association of Insurance Commissioners addresses the concept of suitability in its Long Term Care Insurance Model Act and Regulation
 - a. NAIC requires agent and issuer to develop procedures that consider:
 - (1). Applicant's ability to pay premiums for the proposed coverage and other pertinent financial information related to the purchase of the coverage;
 - (2). Applicant's goals or needs with respect to long term care and the advantages and disadvantages of insurance to meet these needs;
 - (3). Values, benefits, and costs of applicant's existing insurance, if any, when compared to values, benefits, and costs of the recommended purchase or replacement
 - b. Insurer and producer are expected to make "reasonable efforts" to obtain the information necessary to answer basic questions of suitability
 - c. The model regulation requires that applicants be asked to complete a "Long-Term Care Insurance Personal Worksheet"

ETHICS AND LONG TERM CARE INSURANCE – Suitability (cont.)

2. The Model legislation requires insurers to develop and use suitability standards to determine the purchase or replacement of long term care insurance is “appropriate for the needs of the applicant.”
 - a. Insurer is charged with defining suitability standards
 - b. Insurers are required to maintain a copy of their suitability standards and to make them available for inspection upon request by the insurance commissioner.
 - c. Insurers are responsible for producer training regarding application of suitability standards.

3. Producers are responsible for making suitable recommendations
 - a. Producers are required to use the suitability standards developed by the insurer in marketing long term care insurance and making insurance recommendations
 - b. Producers must give applicants a copy of the NAIC disclosure form entitled “Things You Should Know Before You Buy Long-Term Care Insurance” at the time the personal worksheet is provided to the applicant

4. Suitability is determined at the time of the sale. Suitability topics can be separated into two broad categories:
 - a. Individual’s understanding of the coverage being discussed
 - (1). “A Shopper’s Guide to Long Term Care”
 - (2). “Things You Should Know Before You Buy Long-Term Care Insurance,” which is a list of issues and concerns the applicant should consider before buying LTC coverage
 - (3). An outline of coverage

ETHICS AND LONG TERM CARE INSURANCE – Suitability (cont.)

- b. Individual's need for the coverage being discussed
 - (1). Does the individual need this coverage?
 - (2). Can the individual afford the premium for this policy?
 - (3). In consideration of a Partnership policy, does the individual have assets to protect?

- 5. Insurance companies reinforce the suitability process by reviewing applications during the underwriting process and by verifying that the requested coverage matches applicant's goals and needs.
 - a. An LTC Insurance worksheet used with all applicants for individual coverage
 - (1). Discloses modal premium, policy renewability features, and any past premium increases for the type of policy being applied for; additionally, it asks applicant to identify sources of premium funds and whether he/she could keep the policy if premiums should increase by 20%
 - (2). Asks applicant to disclose annual income and future income changes over the next 10 years
 - (3). Asks applicant to disclose the approximate value of personal savings and investments and any expectations for changes in the total value of the assets over the next ten years

 - b. Suitability letter utilized in cases where underwriter questions the suitability of the requested coverage

ETHICS AND LONG TERM CARE INSURANCE – Suitability (cont.)

- c. Impact of insurer's suitability efforts is assessed by regulators through the requirement that companies annually report:
 - (1). total number of apps in this state;
 - (2). number of declinations to provide information on the worksheet;
 - (3). number of applicants who did not meet suitability standards;
 - (4). And number of those who chose to confirm continuance of underwriting process after receiving a suitability letter

B. Suitability and State Partnership Programs

- 1. The Deficit Reduction Act requires insurer Partnership reporting of additional suitability factors:
 - a. Ratio between personal assets and maximum policy benefits
 - b. Desire to avoid Medicaid at all costs
 - c. Too few personal assets
- 2. Other Partnership suitability considerations
 - a. Choice of care provider is limited – Medicaid does not provide coverage for home and community care in all states, and it does not cover assisted living facilities; insured may be required to move to a Medicaid-approved facility when insurance benefits are exhausted.
 - b. Total asset preservation is not guaranteed.
 - c. Moving to another state does not guarantee Medicaid asset protection.

ETHICS AND LONG TERM CARE INSURANCE – Partnership Suitability (cont.)

- d. Asset protection is limited to policy's lifetime maximum benefit.
 - e. Application for Medicaid benefits is required – Medicaid benefits do not begin automatically when Partnership benefits are exhausted, and Medicaid eligibility is not guaranteed, even if the insured qualified for benefits from the Partnership policy.
- C. Standards for Marketing
- 1. Marketing standards are set by the Insurance Commissioner in each state in which Long Term Care Insurance is sold
 - 2. Typical marketing standards:
 - a. Insurers must establish marketing procedures and agent training requirements to ensure that all marketing activities are fair and accurate, and that excessive insurance is not sold or issued.
 - b. Prominent notices on first page of the policy outline and policy that state: **“Notice to buyer: This policy may not cover all of the costs associated with long term care incurred by the buyer during the period of coverage. The buyer is advised to review carefully all policy limitations.”**
 - c. Provide copies to the applicant of the appropriate disclosure forms required.
 - d. Make every reasonable effort to identify whether a prospective applicant for long term care coverage already has coverage for long term care and the amounts of such insurance.
 - e. Establish procedures for verifying compliance with marketing standards.

**ETHICS AND LONG TERM CARE INSURANCE – Marketing Standards
(cont.)**

- f. At the time of solicitation, provide written notice to the applicant of any available senior insurance counseling programs, including name, address, and phone number of the program.
3. Outline of Coverage
- a. A description of the principal benefits and coverage provided in the policy;
 - b. A statement of the principal exclusions and limitations contained in the policy;
 - c. A statement of the terms under which the policy may be renewed and the terms under which cancelation is permitted;
 - d. A description of the terms under which the policy or certificate may be returned and the premium refunded;
 - e. A brief description of the relationship of the cost of care and benefits;
 - f. A statement that the outline of coverage is merely a summary and that the policy should be consulted to determine governing contractual provisions;
 - g. A statement that discloses whether the policy is intended to be a federally tax-qualified long term care insurance contract.

ETHICS AND LONG TERM CARE INSURANCE – Marketing Standards (cont.)

4. Unfair and Deceptive Practices
 - a. Misrepresentation;
 - b. Untrue, deceptive, or misleading statements;
 - c. Making false statements as to the financial condition of an insurer that are calculated to injure any person engaged in the business of insurance;
 - d. Discrimination in rates charged among individuals of the same class and equal expectation of life;
 - e. Offering rebates or special favors or anything of value not specified in the contract;
 - f. Making statements to induce a customer to purchase, amend, lapse, forfeit, change, or surrender a contract of insurance;
 - g. Refusing coverage or canceling or declining to renew coverage based on sex or marital status;
 - h. **Twisting** – knowingly making any misleading representation or incomplete or fraudulent comparison of any insurance policies or insurers in order to induce, or tend to induce, any person to lapse, forfeit, surrender, terminate, retain, pledge, assign, borrow on, or convert any insurance policy, or to take out a policy of insurance with another insurer;
 - i. **High pressure tactics** – using any method of marketing having the effect of or tending to induce the purchase of insurance through force, fright, threat (whether explicit or implied,) or undue pressure to purchase or recommend the purchase of insurance;

**ETHICS AND LONG TERM CARE INSURANCE – Marketing Standards
(cont.)**

- j. **Cold lead advertising** – making use, directly or indirectly, of any method of marketing that fails to disclose in a conspicuous manner that a purpose of the method of marketing is to solicit insurance and that contact will be made by an insurance agent or insurance company;
- k. **Misrepresentation** – misrepresenting a material fact in selling or offering to sell a long term care insurance policy.

V. Retirement Distribution Planning

- A. The U. S. Retirement System
 - 1. Social Security

Exhibit 10
Age to Receive Full Social Security Benefits

<u>Year of Birth</u>	<u>Full Retirement Age</u>
1937 or earlier	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943-1954	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 and later	67

Retirement Distribution Planning (cont.)

2. Employer-sponsored retirement plans
 - a. Defined Benefit -- contributions are actuarially determined to provide the specified benefit
 - (1). Flat Amount formula - provides a stated dollar amount to each plan participant
 - (2). Flat Percentage formula
 - a. Career Average
 - b. Final Average
 - (3). Unit Credit
 - a. Based on employee's service with the employer
 - b. For example, may provide 1.5 per cent of earnings for each year of service, with total percentage applied to average earnings
 - c. Therefore, employee with 30 years of service would receive 45% of average earnings. ($1.5 \times 30 = 45$)
 - b. Defined Contribution -- contribution is specified; benefit amount is uncertain because of fluctuations in interest or performance
 - c. 401(k) Plan

Exhibit 11

What is a Qualified Plan?

A qualified plan is one that has met the qualification requirements established by the Federal Government.

The plan must be non-discriminatory and for the benefit of the employees and their beneficiaries. In other words, you may not pick and choose who will participate in the plan.

It must be established with the intent that it will be ongoing.

You may establish a minimum entry age of up to twenty-one and a service requirement of one year. You may exclude part-time employees (those who work less than 1,000 hours per year,) and union employees subject to collective bargaining where pensions have been a subject of the bargaining.

The assets of the plan must be legally segregated.

Neither contributions nor benefits may discriminate in favor of stockholders, officers, or highly compensated employees. Contributions and benefits may be allocated on a basis of salary and length of service. Therefore, compensation and age can play a significant role in designing your plan.

The contributions to the plan must be actuarially determined, taking into account the expected effects of mortality, interest earnings, and reasonable expenses of operation.

The plan must be in writing. The written document sets forth all the provisions of the plan necessary for qualification.

Retirement Distribution Planning (cont.)

3. Individual Retirement Account (IRA)
 - a. Distributions made before the individual's age 59 ½ are subject to a TEN PERCENT PENALTY in addition to any tax liability.
 - b. Distributions made after age 59 ½ are subject to income tax only. No penalty applies.
 - c. Surviving Spouse - all or part of the IRA may be rolled over to the surviving spouse. All other inherited IRA's are denied (TEFRA).
4. Roth IRA - distributions are income tax free because contributions were non-deductible.
5. Individual's private initiative
 - a. Individual savings
 - (1). Personal discipline
 - (2). Personal responsibility
 - b. Post-retirement employment

VI. Distribution of Qualified Funds

A. Lump Sum Distributions

1. Individual must be over age 59 1/2 to avoid paying ten percent penalty tax in addition to ordinary income tax.
2. Once the tax is paid, there is no further involvement with the government.
3. Lump sum distribution results in loss of shelter of non-needed funds.

B. Annuity Options

1. Straight Life or Life Only option -- pays a monthly income until the annuitant's death and then pays no more. Usually pays the highest monthly benefit, but if annuitant dies before receiving the total principal in the contract, insurer keeps the balance.
2. Life Income with Refund Options -- pays the annuitant until death, but if annuitant dies before receiving all the principal in the annuity, the remaining principal is refunded to annuitant's beneficiary.
 - a. Refunds are refunds of principal only -- no interest is payable to beneficiary.
 - b. Refunds may be in the form of lump sum or installments.
3. Life Income with Period Certain -- pays the annuitant until death, but if annuitant dies before the end of the Certain (Guarantee) period, payments are made to annuitant's beneficiary for the balance of the guaranteed time.

DISTRIBUTION OF QUALIFIED FUNDS -- Annuity Options (cont.)

4. Joint and Survivor -- pays benefits in a fixed monthly amount for life with benefits continuing for the life of surviving co-annuitant.
 - a. The continued benefit may be for the same amount, or for a lesser amount, depending upon the continuance option chosen.
 - b. Payment amounts under this option are dependent upon the ages of the co-annuitants.

C. Systematic Withdrawal

1. Amount of withdrawal is calculated each year; minimum income for that year is based upon remaining life expectancy.

Exhibit 12

REMAINING LIFE EXPECTANCY AT ATTAINED AGE

<u>ATTAINED AGE</u>	<u>YEARS</u>	<u>ATTAINED AGE</u>	<u>YEARS</u>
60	24.2	70	16.0
61	23.3	71	15.3
62	22.5	72	14.6
63	21.8	73	13.9
64	21.6	74	13.2
65	20.0	75	12.5
66	19.2	76	11.9
67	18.4	77	11.2
68	17.6	105	1.8
69	16.8	110	1.0

DISTRIBUTION OF QUALIFIED FUNDS -- Systematic Withdrawal (cont.)

2. Systematic Withdrawal is best suited for people who:
 - a. Desire flexibility to change income;
 - b. Want protection against inflation;
 - c. Are concerned about leaving maximum amounts for heirs;
 - d. Want to minimize income taxes;
 - e. Are age 70 1/2 or under age 59 1/2 to avoid penalties.

D. Comparison of Systematic Withdrawal to Other Available Alternatives:

Exhibit 13

	<u>IMMEDIATE ANNUITY</u>	<u>LUMP SUM DISTRIBUTION</u>	<u>SYSTEMATIC WITHDRAWAL</u>
Full Right to Principal	NO	YES	YES
Inflation Protection	NO	YES	YES
Guarantee of Principal	MAYBE	NO	YES
Preservation of Tax Deferral	YES	NO	YES
Guaranteed Asset Appreciation	NO	NO	YES
Full Options Available to Beneficiary	NO	NO	YES
Estate Preservation	NO	MAYBE	YES
Liquidity	NO	YES	YES
Customized Income Flow	NO	YES	YES

VII. Conclusion

Thank You!

