EMERSON, REID'S
Vol. 7 • No. 3 INSURANCE OBSERVER August 1995

Do You Sincerely Want to Be Rich?

World Gone Mad

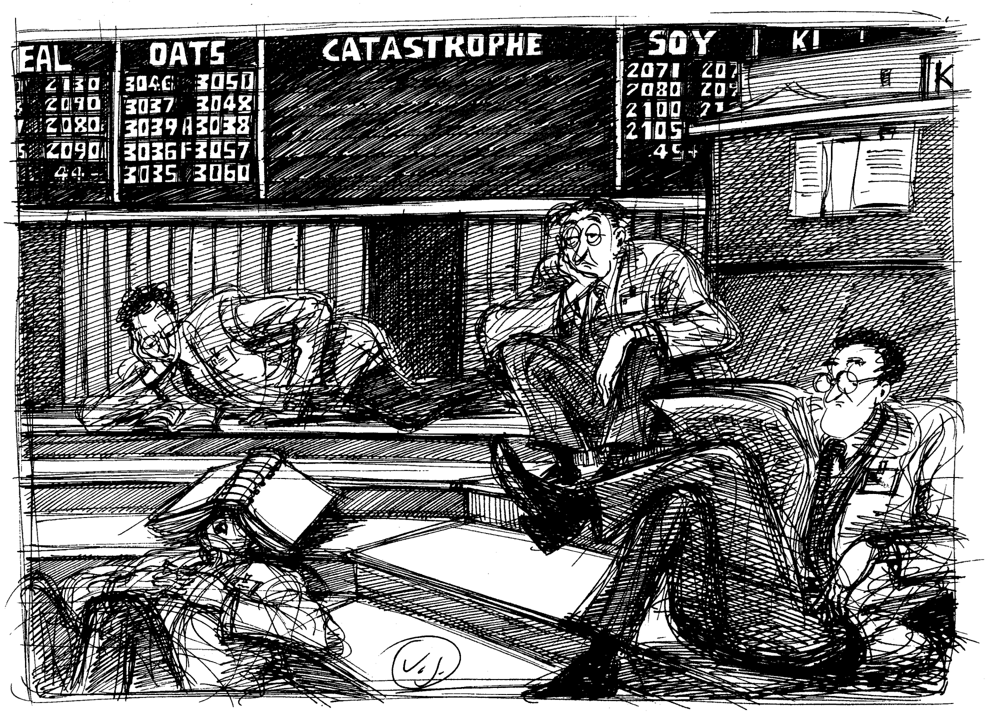
How stupid are insurance agents? According to Connie Palacios, the assistant controller of United Insurance Cos., they are morons. Two months ago, United Insurance, whose stock was trading at $42 per share, announced a 4-for-1 stock split. The purpose of the split, Ms. Palacios told the *Wall Street Journal*, was to allow insurance agents to buy more shares at a lower price. Why insurance agents—or anyone, for that matter—would prefer four $10.50 shares to one $42 share, was not explained, because there is no rational explanation. (Perhaps if agents pay for each share with 105 dimes instead of 10 dollars and two quarters, they'll really feel that they're getting a bargain.)

In May, the total capitalization of the New York Stock Exchange hit $5 trillion, and just the other week a respected Wall Street analyst (is that an oxymoron?) made the case for Dow 7,000. The NASDAQ market is up 33% so far this year. For investors who find U.S. markets too tame, a new world of investment opportunities has surfaced. Calvert Group, a division of Acacia Mutual Life Insurance Co., recently unveiled the New Africa Fund. "Discover the ultimate emerging market," suggested an ad, which bandied about the phrase "*aggressive* capital appreciation."

In Japan, however, where life insurance companies own 12.7% of all outstanding shares, capital appreciation, aggressive or otherwise, would be a welcome relief: the Nikkei has plunged 60% since 1989. (Japanese life insurers have historically made long-term investments in companies that, in turn, encouraged their employees to buy policies from those insurance companies.) Chiyoda Life Insurance Co. reported a loss last year, the first by a major Japanese insurer in almost fifty years, and Sumitomo Life Insurance Co. plans to reduce its administrative work force from 12,000 to 10,000 over the next three years.

Back in America, where insurance-company balance sheets have been fattened by massive bond-and-stock-market rallies, Aetna was shocked, shocked to discover what everyone else already knew: that its environmental loss reserves were seriously deficient. The company's management had steadfastly maintained that it was "unable to make a reasonable estimate as to the ultimate amount" of reserves because of "significant uncertainties." After a $750 million addition in July, its environmental reserves stood at $1.087 billion.

Insurance stocks have risen sharply since last fall, but they have lagged the general market this year. That is not to say that they have performed poorly. The *Business Insur-*



The catastrophe insurance futures pit at the Chicago Board of Trade.

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ance index is up a robust 16.5%. Although insurance stocks are no longer cheap, they don't sport the sky-high price-earnings ratios of technology stocks, which are currently in vogue. Unlike technology companies, which tend to have little in the way of underlying value outside their technology, insurance companies are basically pools of capital, most of which is invested in bonds and stocks. Given investors' infatuation with mutual funds, it would seem logical that the way to sell stock in a newly formed insurance company would be to pretend that it is a mutual fund.

The insurance-company-cum-mutual-fund isn't a new concept. In fact, it's kind of what Warren Buffet's Berkshire Hathaway has been doing for decades. Although Berkshire is a large player in the "super-cat" reinsurance market, it's really an investment company. Its $11 billion of surplus far exceeds its $915 million in premium.

Since everyone in America is now of the belief that common stocks will always rise, perhaps it's not surprising that someone has finally decided to merge the surefire profits of a mutual fund with the thrills of a reinsurance company. Normandy America, a brand new company with $122,724 in the bank, plans to raise $210 million by selling 8.4 million shares at $25 a piece. Assuming that the deal is completed, it will be the 18th-largest reinsurance company in America. The deal's underwriters are Salomon Brothers, Alex. Brown & Sons, and Wertheim Schroeder.

Normandy plans to write business through brokers, especially business that "provides attractive pricing relative to the risk assumed." (What company *doesn't* try to do this?) Since Normandy is an investment company disguised as an insurance company, it will specialize in lower-layer excess-of-loss long-tail casualty business that generates a significant amount of *float* to invest. The company expects to maintain a premium-to-surplus ratio of .5 to 1.

What separates Normandy from virtually every other reinsurer is its investment strategy, which sounds like a page out of the best seller, *The Warren Buffet Way*. Normandy's management, which employs what might be called value-oriented approach to investing, is of the belief that "over time, investments in equity securities can provide a greater total return through capital appreciation and dividends than investments in fixed income securities," and therefore plans to invest the company's assets "primarily in equity securities." In keeping with the Buffet style of investing, Normandy will view the stocks it buys as "positions to be held indefinitely." There are risks, as the prospectus freely admits. Volatility may be "exacerbated to the extent that [the] portfolio is concentrated in relatively few issuers or industries."

Normandy America, a Warren Buffet wannabe, plans to write long-tail casualty treaties and invest its assets in stocks.

Normandy will be domiciled in Nebraska (Berkshire Hathaway's home), presumably because the insurance department there is used to dealing with insurance companies that own a lot of stocks. William McCartney, who until last year ran the Nebraska insurance department, will serve on Normandy's board.

Christopher Bagdasarian, Normandy's Chairman and CEO, has several things going for him. Because he is a mere 29 years old, he will undoubtedly approach his work with more vigor, energy and, well, *youth*, than old-timers such as Warren Buffet are capable of. Furthermore, his track record is nothing to sneeze at. Over the past ten years (he started young), he managed a large portfolio that averaged a 29.11% annual rate of return, versus 14.38% for the Standard & Poor's index.

Investors will be hoping that Bagdasarian can duplicate his past investment success. If he does, the $210 million they put in will grow to $2.7 billion in ten years, $34 billion in 20 years, and $447 billion in 30 years. Bagdasarian, however, is most concerned with the next ten years. As part of the deal, he and his wife received 2,581,945 restricted shares of stock. These shares will vest over ten years if the company achieves certain results. The restricted shares are divided into two equal classes: 1) "Annual eligible shares," which vest depending upon the company's annual increase in stockholders' equity (for example, if the increase is less than 15%, none of the shares vest; if the increase is 17.5%, half vest; if the increase is 20%, all vest); and 2) "10-year eligible shares," which vest in 2006 if the company achieves a ten-year annual rate of return between 15% and 20%; the return must hit 20% for all the shares to vest.

There is a flaw in this formula. It is possible that Mr. Bagdasarian could achieve mediocre results, let's say 8%, yet still receive as many as 1,341,662 shares worth $53.6 million, depending upon how these results were achieved (he would have to have a number of 20%+ years and one big losing year).

Although Mr. Bagdasian won't be taking a salary, a firm he owns will handle Normandy's investment transactions and be paid the customary institutional brokerage fees.

Mr. Bagdasarian's investment approach will be familiar to anyone who has ever read a Berkshire Hathaway annual report. He likes companies that can be easily understood, can expand their margins and increase their return on equity with little additional capital, have good balance sheets, and have excellent management.

Mr. Bagdasarian's final criterion, pricing, may be his biggest obstacle, at least in the near term. "Management believes that attractive stock prices often exist during periods of economic or political uncertainty, or misinterpretation by the market of information affecting an issuer." In other words, the time to buy is when the blood is running in the streets.

It strikes us that now is certainly not one of those times. ■

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The Worst Insurance Brokerage in America

BRI Coverage aka Underwriters Financial Group

To win the title of the worst insurance brokerage in America, a firm must meet certain criteria: It must be big enough to have meaning in the marketplace; its financial statements must be inaccurate and confused; it must be losing money, and its premium escrow fund must be barren. If the firm is also involved in dubious reinsurance transactions in the Cayman Islands, deals in curious financial guarantees from a South Pacific atoll and has defaulted on millions of dollars of debt, so much the better.

Underwriters Financial Group, a New York-based firm formerly known as BRI Coverage, not only fulfills these requirements, it exceeds them.

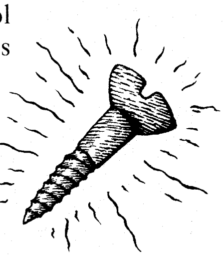
BRI has long had a questionable reputation in New York City insurance brokerage circles. In 1970, it was purchased by Integrated Resources, a wheeler-dealer tax-shelter syndicator that went bankrupt 15 years later. In 1974, BRI's principals, Donald Ferrarini, Bruno Rumignani, Burton Matfus and Howard Miller, bought the firm from Integrated Resources and—by their account—built it into a sizable company. In 1991, *Business Insurance* listed BRI as the 14th-largest insurance brokerage in the United States, with $35.2 million in gross revenues and 212 employees.

BRI handled commercial accounts and some risk-management business (it was famous for its parties at RIMS' annual conference), and specialized in the garment, freight-forwarding, asbestos-abatement, demolition and fur industries. Through Transportation Fleet Managers, a firm in which BRI's principals had a 50% interest (the other shareholders were Carmine Fiore and Reliance Group), BRI was involved in long-haul trucking risks, which were then reinsured by its Cayman Islands subsidiary, International General Insurance.

Had BRI continued as a private company, its troubled finances, questionable dealings and inaccurate disclosures might never have come to light. But, on Oct. 21, 1992, it engineered a reverse stock purchase with Chippewa Resources, a publicly held company with a mess of oil and gas interests, in which BRI's principals became the controlling shareholders of the combined company, renamed Underwriters Financial Group. In 1994, the insurance brokerage subsidiary, BRI, became UFG International.

It's hard to imagine a strategic reason for a supposedly profitable insurance firm to merge with an indebted oil and gas concern. On the other hand, suppose that BRI were neither profitable nor valuable. The firm's principals might have figured that backing into an AMEX-listed company would afford them easy access to the public's deep pockets.

Several aspects of the Chippewa deal were most unusual. Somewhere along the way, Richard Campanaro and Andres Romero, who control what they describe as "an Irish insurance-holding company," Underwriters Insurance Group (UIG), introduced BRI to one William Stehl, who promised to deliver to BRI, in return for a fee, $35 million in Kwajalein-island financial guarantees supposedly backed by U.S. land-use payments. BRI would then merge with Chippewa and UIG and contribute the guarantees to the combined company (Underwriters Financial Group), which, in return, would issue a $10 million promissory note to Ferrarini, Rumignani, Matfus and Miller.



That BRI proceeded with this nebulous transaction is revealing. Why, after all, would someone with $35 million of bona fide guarantees seek out an obscure firm like BRI rather than a major bank or Wall Street house? Furthermore, were Kwajalein islanders in any position to guarantee $35 million?

Kwajalein, a small South Pacific atoll that rises a few feet above sea level, is one of a number of dots in the ocean that make up the Republic of the Marshall Islands. (Another Marshall atoll, Bikini, was a testing site for the hydrogen bomb.) Per capita annual income for the Marshall Islands' 50,000 inhabitants is $1,500, and the gross domestic product is $63 million. Copra, dried coconut meat, accounts for 90% of the republic's $2 million in annual exports.

Underwriters Financial soon began using the guarantees as if they were real money. It put $5 million of them into its Cayman Islands reinsurance company and bid $500 million for Frank B. Hall, then owned by Reliance Group. According to Ferrarini, Underwriters Financial was the high bidder until Aon topped it.

Although the guarantees never materialized and Ferrarini, Rumignani, Matfus and Miller returned the $10 million promissory note, Underwriters Financial continued to think big, its negative net worth notwithstanding. A 1993 private-placement memorandum spoke of "acquiring a major insurance underwriting company through a leveraged buyout," and, as recently as a few months ago, the company had, incredibly, hoped to issue $60 million in preferred stock through Coleman & Co.

Perhaps as curious as the Kwajalein guarantees were the promoters who brought them to BRI's attention. Richard Campanaro and Andres Romero, whose office was in the same building as BRI's office, also ran a firm called Underwriters Capital Corp. (UCC) which has advertised that it raises capital for insurance companies. UCC, which has issued screwy statements to us in the past, operates on the fringe of the over-the-counter market and deals in penny-stock shell companies. Campanaro and Romero also have links with at least two other stock peddlers, Cameron Phillips and Gold Coast Brokers.

Information on Campanaro and Romero is sketchy. Campanaro, who was president of Royal Tandem Life, a joint venture of Equitable Life and Merrill Lynch, until 1990, didn't return our calls. In a brief conversation, Romero said that if we had questions we could write to their lawyers in the Dominican Republic but refused to give us their name or fax number.

In 1994, Campanaro, through Century Industries, a tiny publicly held steel fabricator of which he is chairman, signed a letter of intent to purchase Prestige Casualty Insurance Co. for $3 million to $4 million. Century then took the unusual step of issuing a press release projecting $3 million in earnings from the deal, perhaps hoping to give its stock a boost. The deal, not surprisingly, never materialized, and Prestige was declared insolvent several months later. Century, whose major "asset" is 100,000 shares of UIG that it carries on its books at $1 million, also had plans to buy Republic Bankers Life, but they fell apart when Stratton Oakmont, a notorious penny-stock firm, didn't raise the required funds.

Underwriters Financial's dealings with Campanaro and UIG ended in litigation, with Underwriters Financial alleging that UIG had "fail[ed] to perform" and had committed "breaches." The lawsuit was settled in March 1993, with Underwriters Financial transferring 150,000 shares of its stock to UIG as a finder's fee for the Chippewa deal.

Despite the litigation, Underwriters Financial had one more dealing with UIG. In the second quarter of 1993, Underwriters Financial discovered that its Cayman Islands reinsurer, International General Insurance (IGI), was $2.3 million underreserved, a significant figure for cash-strapped Underwriters Financial. On the last day of the year, however, IGI entered into an excess of loss reinsurance and portfolio transfer agreement with Covent Insurance Co. in Bermuda, whereby, for a $250,000 fee (of which only $100,000 was paid), IGI managed to reduce its loss reserves by $2.6 million. Covent, it turns out, was a subsidiary of Campanaro's UIG. On Dec. 29, 1994, the IGI-Covent transaction was terminated and IGI's recognition of the $2.6 million gain was reversed because the transaction did not actually transfer risk.

As a public company, Underwriters Financial Group is required to file reports with the Securities and Exchange Commission disclosing material information about its business and finances. Although it has made these filings, they have often been inaccurate, misleading, or garbled.

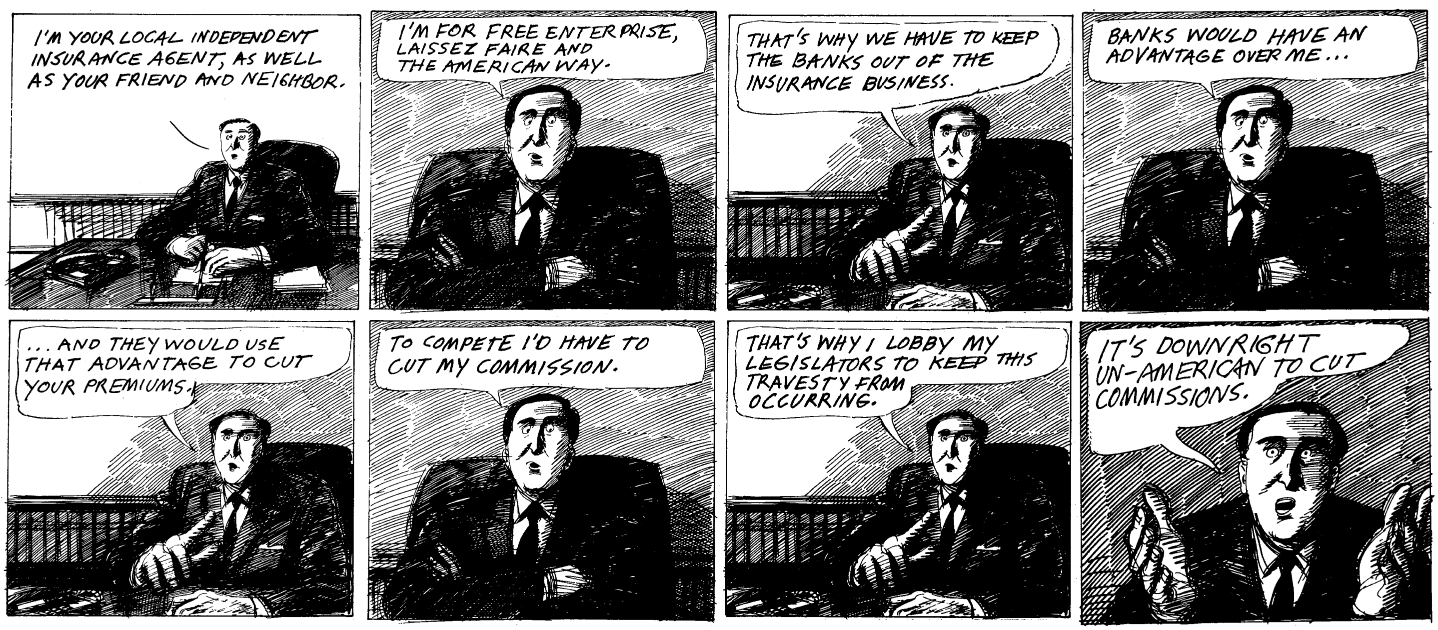
For example, in a 1993 private-placement memorandum for a stock offering through which it raised $3,916,000, Underwriters Financial stated that "an independent appraisal of [BRI] was prepared by Arthur M. Ostrow, Inc., which valued [BRI] at $24,215,000. This valuation was determined in part by applying a multiplier of 1.5 to [BRI's] revenues of $16,143,000." Investors reading this statement would have gained confidence that there was considerable underlying value in the company's insurance operations. What wasn't disclosed, however, was that the "independent" appraiser, Arthur M. Ostrow, formerly had been a senior vice president and shareholder of BRI and still maintained an office there.

The 1.5 multiplier as well as the figures that Ostrow used are also strange. Recent filings show that, in 1992, BRI's insurance brokerage operations generated $12,534,000 in revenues. Its reinsurance business, which ceased operating two-and-a-half months after the appraisal was made, generated $3,053,000 in revenues. As the reinsurance operations were losing money, they probably had a *negative* value. Therefore, Ostrow effectively valued the insurance brokerage activities at almost two times commissions to arrive at the more than $24 million valuation. That's an unusually high multiple for any insurance broker, much less one of BRI's stature.

There are many other inaccuracies in Underwriters Financial's documents. The 1993 private-placement memorandum misled investors by describing the company as "a full service insurance firm with *an international network of service offices*." When queried about this, Ferrarini admitted that there was no "international network," merely various independent firms with which Underwriters Financial worked on an ad hoc basis.

Underwriters Financial Group has literally zero dollars in its premium escrow fund and is in default on millions of dollars of debt.

Underwriters Financial's financial statements are also a moving target. Its 1993 10-K listed insurance brokerage revenues of $14,432,870, but that was restat-



ed in the 1994 10-K as $13,529,342. The bottom line discrepancy was more extreme: 1993's profit of $2,155,693 was restated as a loss of $1,363,768.

Another Underwriters Financial hallmark, a persistent lack of cash, raises troubling questions. Given its premium volume (Ferrarini said it was $150 million), one would expect that, at any given moment, the company would have several million dollars in cash from premiums that it had received from insureds but not yet been forwarded to insurance companies. (State laws require that these funds be held in escrow and not be commingled with other funds.) At Dec. 31, 1993, Underwriters Financial's "restricted cash" was $1,814,749, considerably less than what one would have expected. There is even less to this than meets the eye: $1.2 million of the cash represented the proceeds of a recent private placement and was being held in escrow until January 1994, and $614,750 was a certificate of deposit used to secure a standby letter of credit issued by International General Insurance, its Cayman Islands reinsurer. The private-placement escrow fund and certificate of deposit represented the entire amount of cash belonging to Underwriters Financial. There was, apparently, nothing in the premium escrow fund.

Of course, that doesn't mean that Underwriters Financial raided its premium escrow fund. It's conceivable that its many commercial insureds paid their insurance carriers directly, or that no premium checks had come in that month, or that checks had come in and were—voila!—instantly turned over to the insurance companies. Ferrarini says that Underwriters Financial was in compliance with the law.

Given Underwriters Financial's bewildering financial statements, unusual disclosures, severe liquidity crisis, losses and negative net worth, one wonders how it could get an unqualified statement from a certified public accountant. To find out, we checked in with its auditor, the two-man Denver firm of Louis Weiss & Associates (now defunct). Although Louis Weiss did not answer most of our questions, he provided *incorrect* answers for two of them. First, he said that Underwriters Financial's receivables represented the "face value of policies." Later, he insisted that the company's $7 million in receivables represented *commissions* rather than *premiums*. After a brief conversation, Louis Weiss said he didn't have time to talk and hung up the phone.

Underwriters Financial's senior vice president, Howard Miller, a conservatively dressed 63-year-old with neat white hair and a pleasant manner, was more forthcoming but gave us innacurate information. When asked why BRI had told *Business Insurance* that it had $35 million in gross revenues ($30 million of which were retail brokerage), when, in fact, its financial statements subsequently showed about half that figure, he had a simple explanation: "We reported BRI plus all the other things. BRI Holding didn't put everything into the public corporation."

What businesses weren't put into the public company?

Miller said he didn't want to get into that but reiterated that these other businesses accounted for the difference in reported revenues. When asked why, if BRI's principals had other insurance businesses and didn't devote full time to Underwriters Financial, wasn't this disclosed in the proxy statement or 10-K, Miller offered a new explanation and said that the businesses had all been closed down.

At a meeting with us a couple weeks later, Don Ferrarini, who was wearing brown slacks, a striped shirt open at the collar, a large gold cross, a gold Rolex on his left wrist, and a gold bracelet on his right, admitted that the $35 million *Business Insurance* figure was not correct. He was vague about the numbers but said they included BRI, Transportation Fleet Managers, offshore premiums and other things.

Whatever the truth about its past, Underwriters Financial Group's present is not attractive. The company has been sued by numerous former clients including Merit Distribution Centers, George Campbell Painting, Sunset Asphalt Products, Leap Inc., Raycomm Transworld Industries, Belfer Realty & Development, Automanage, I. Appel Corp., Frigitemp, Potamkin Cadillac, Crown American and William H. Sadlier. It is also involved in litigation with Lloyd's of London and former employees.

Too Long in the Wasteland
Underwriters Financial Group
March 31, 1995

Assets		Liabilities	
Current Assets		Current Liabilities	
Cash	$0	Accounts payable	$6,143,654
Accounts Receivable	7,963,149	Bank overdraft	131,740
Other	124,441	Income taxes	1,748,087
Total Current Assets	8,087,590	Accrued Liabilities	1,656,891
		Notes payable	3,177,384
Property and Equipment	117,672	Reserve for unpaid claims	59,971
Investment in Delta Petroleum	4,306,245	Notes payable—affiliates	736,932
Deferred Taxes	424,514	Advances from related parties	260,000
Intangibles	408,790	Total Current Liabilities	13,914,659
Other Assets	711,738	Notes payable	1,080,000
Total Assets	$14,056,549	Deferred credits	1,288,104
		Commitments and Contingencies	970,000
		Total Liabilities	17,252,763
		Stockholders' Equity	($3,196,214)

One lawsuit that was settled involved Harold K. Ross, one of Underwriters Financial's largest producers. In the settlement, Underwriters Financial admitted that it had agreed not to borrow against a life policy that was to benefit Ross but that, nonetheless, it had borrowed $620,000. The settlement, which was guaranteed by Ferrarini, Rumignani, Matfus and Miller, calls for the company to repay the policy loan and issue to Ross—who has since left the firm—an option to purchase 500,000 Underwriters Financial shares at $2 per share.

It is unclear where Underwriters Financial would get the funds to repay the loan. As of March 31, it had literally zero dollars in its general account and its premium escrow fund, and its $8.1 million of current assets were dwarfed by current liabilities of $14.9 million. The company's tangible net worth was a *negative* $3.6 million. In addition, it is in default on millions of dollars of debt and has received a qualified opinion from its new auditors. In the first quarter of 1995, the company lost $388,446 as reported commissions declined from $3.3 million to $3.1 million.

Whether any number in Underwriters Financial's financial statements can be relied upon is another matter altogether. While its past financials would give anyone cause for concern, the current situation might be even worse. During the first quarter of 1995, the company's director of administration and its controller "suffered severe health problems which led to their terminating their employment with the company." Both men had been responsible for approving and recording all of the company's transactions, as well as its cash management and budgeting. As of May, the company was, in its own words, "operating with a minimal, inexperienced accounting staff."

The latest indications are that Underwriters Financial is disintegrating. Over Memorial Day weekend, Burton Matfus, the treasurer who presided over the company's abysmal finances, committed suicide. Although the company reported 80 employees in May, by July 12 it was down to about 20.

Despite Underwriters Financial's dismal state of affairs, as of May it said that it was still placing business directly with many major insurance companies, including Reliance National, Aetna Casualty & Surety, AIG, Atlantic Mutual, Home Insurance Co., Fireman's Fund, Kemper, Wausau, Zurich and General Accident. Despite the massive evidence—easily available from public documents—that something was seriously amiss at Underwriters Financial, these insurance companies continued to do business with a firm that had no money in its premium escrow fund and had admitted that it was in "a severe liquidity crisis."

Whether Underwriters Financial's clients, and the insurance companies with which it dealt, will come out whole, is not known. But the questions remain: How bad must an insurance brokerage's finances be, and how questionable must its conduct be, before insurance companies cease doing business with it?

If Underwriters Financial is any indication, being a deadbeat that files downright nutty documents with the Securities and Exchange Commission is no impediment to doing business with many of the best-known insurance companies. ■

Above All in SERVICE®

The Erie Insurance Exchange

Jamestown, New York lies about sixty miles southwest of Buffalo and thirty miles east of Lake Erie. With a slowly shrinking population that now measures 34,500, it's the biggest city in Chautauqua County, which, depending upon whom you talk to, is either the largest or second largest producer of concord grapes in the country.

The environs are scenic: rolling fields, vineyards, dairy farms, apple and cherry orchards. Jamestown is not a bad-looking place, either, especially in late spring and summer when the weather is warm and the days are long.

Jamestown's industrial base, however, has been on a languorous decline since its heyday in the early twentieth century. Many of the old machine-tool shops and metal benders have closed their doors and the furniture manufacturers have long since packed up and moved to High Point, North Carolina.

This is not an easy economic environment for insurance agents, and the fact that there are more than a hundred of them in the area doesn't help. In Jamestown, just as in the rest of the country, agents complain about soft markets, declining commissions, and increasing competition.

Not all agents suffer from this malaise, however. For Dan Johansen, an energetic thirty-nine year old who runs the Johansen Agency—a three-person firm writing $2 million in premiums—these are the best of times, not the worst. "I'm so enthused about being in the insurance business," he says over a late afternoon iced tea at the Ironstone restaurant. "I've never written more new business than I have in the last three months, and I'm having a great time."

But times weren't always so great for the agency. "For the past three years I'd been running scared." He worried about markets, about attracting new business, and about retaining what he had. Then, last year, he was approached by Erie Insurance Exchange, in Erie, Pennsylvania. Would he like to become their first agent in New York?

Although Erie is the thirteenth-largest auto insurer in the country, it isn't a household name, probably because it doesn't advertise. Its operations are concentrated in Pennsylvania, Maryland, and Virginia, and, not surprisingly, Johansen wasn't familiar with the company. To learn more, he began calling Erie's agents. "Every single one said that Erie was the best thing that had happened to them."

Although Erie had approached Johansen, an agency appointment was not immediately forthcoming. First there was a six month interview process during which both Erie and Johansen made sure that their business philosophies were compatible. Although Erie writes $1.6 billion in premium, it has less than a thousand agents, most of whom place the majority of their business with Erie.

Although the company didn't require any minimum production from Johansen, he finds that he is placing the bulk of his business there, anyway. "Their pricing allows me to sell a lot more—for the first time I'm beating State Farm—and they provide great service to me and the policyholder. They do it the old-fashioned way—they really underwrite and engineer a risk.

"Erie has given me a new confidence and a great sense of optimism. Without Erie I'd be full of gloom and doom."

Being the first Erie agent in New York, says Johansen, "is almost like having the first McDonald's franchise."

Erie Insurance Exchange is neither a stock company nor a mutual—it's a reciprocal (similar to a mutual) managed by an attorney-in-fact, Erie Indemnity Company. Although some consider mutuals and reciprocals anachronistic, Erie, like State Farm and Northwestern Mutual, exemplifies the best of the breed. Its principles and approach to business have remained basically the same for seventy years. Erie sells through agents. It writes automobile insurance, personal lines, and Main Street risks. About two-thirds of its business is still in Pennsylvania.

One thing that sets Erie apart is its extreme dedication to its policyholders and agents. Its pricing is among the most competitive in the industry—a recent survey by the Pennsylvania Insurance Department showed that Erie has the lowest rates in sixty-four out of sixty-seven counties—and *Consumer Reports* rates its service near the top. (Only Amica Mutual, USAA, and Cincinnati Insurance are rated higher.) Jeffrey Ludrof, a senior vice president, says that the company only has a single approach, "to treat people well." Ninety-one percent of policyholders renew their policies each year, an indication that the company is doing something right.

Erie's financial strength is truly exceptional. In addition to an A++ rating from Best, it is one of only eight property/casualty companies to receive Weiss's highest rating, an A+. Policyholders' surplus, which has grown at an astounding 22% compounded annual rate since 1970, was $1.4 billion at year-end 1994, compared to premiums of $1.6 billion. Considering that Erie doesn't write long-tail business and has negligible coastal or earthquake exposure, these figures are all the more impressive.

As a result of its conservative balance sheet, Erie is able to invest heavily in common stocks, which comprised 37% of invested assets at year end. The stock portfolio, managed by John Petersen, the company's chief executive officer, is concentrated in a relatively small number of issues. Five companies—Microsoft, Compaq, Intel, Fannie Mae, and Wells Fargo—accounted for 34% of the $1.1 billion portfolio. Although this is a bit unusual, the payoff has been handsome.

Erie's corporate culture is also special. The company is relatively unstructured and there's a general feeling of trust and respect among employees. For example, the door to the chairman's office has a door knocker on the *inside*, since the door,

Erie Insurance Exchange and Affiliates

	Earned Premium	Policyholders' Surplus
1925	$31,900	$34,411
1930	201,046	121,924
1940	523,470	215,409
1950	3,306,127	1,371,283
1960	14,427,430	4,016,130
1970	57,678,652	12,085,562
1980	303,813,093	114,819,608
1990	1,127,953,634	740,823,920
1994	1,639,884,809	1,449,280,799

which swings out, is open to everyone. Notes Dan Johansen, "I can call the CEO, John Petersen, any time. I don't even *know* the name of the CEO at other insurance companies."

Erie is listed in *The 100 Best Companies to Work for in America* ("Stimulating jobs in a boring industry"), and, in a recent survey, 97% of the employees said they were "proud" to work there. "For a lot of us, it's more than a just a job," says John Brinling, Jr., a senior vice president who's been with the company twenty-eight years.

The Erie Insurance Exchange was formed in 1925 by thirty-eight year old H.O. Hirt, whose previous jobs included teaching history, collecting overdue accounts receivable, managing a grocery, and selling auto insurance for three years. Hirt, who lived to be ninety-five and served as Erie's president until he was eighty-seven, was a man of strong convictions: he was a pacifist who opposed World War I and a socialist who voted for Norman Thomas. A paternalistic manager who preached hard work, fair dealing, and thriftiness, Hirt watched every penny and oversaw even the most minute corporate details. Once, when a branch manager requested permission to buy new casters for his desk chair, the Old Man, as Hirt was known, wrote a lengthy memo suggesting that the manager save money by fixing the chair with "a great big wad of chewing gum." Hirt was equally tight with himself: he didn't own a new car until he was past fifty, and, rather than buy new pants, taped the holes in his pockets to prevent coins from falling out.


H.O. Hirt

When, in 1968, Hirt addressed a U.S. Senate subcommittee on underwriting selectivity and cancellations, he began by saying, "I am not a farmer, but those who know me give me credit for producing more corn than any farmer in the United States." Hirt, whose philosophy is summed up in Erie's mission statement—"to provide its policyholders with as near perfect protection, as near perfect service, as is humanely possible, and to do so at the lowest possible cost"—never tired of preaching the golden rule. "Success in business," he wrote in a weekly bulletin he put out for forty years, "is a matter of simple common sense mixed with just plain decency." Hirt worked tirelessly to make sure that employees and agents lived up to the company's hokey motto, "The Erie is above all in SERVICE®."

How is it that an old-fashioned company like Erie has achieved such wonderful results when many of the grand old names of the industry, who embraced "modern" corporate strategies and management techniques, have run into trouble? To find the answer, we paid a visit to this old smokestack town of 117,000 and spent some time hanging around the company.

Erie Insurance Exchange occupies an attractive complex located in a formerly run-down section of downtown Erie not far from the waterfront. The main building, which is tasteful yet understated, includes a four-story atrium, spacious offices, plants, lounges, and gardens. Photos and plaques of H.O. Hirt adorn the walls, as do reminders about providing SERVICE®.

The old headquarters, now known as the H.O. Hirt building, adjoins the main building. Modeled after Philadelphia's Independence Hall, it was built in 1956 and now houses the executive suite. We sat down in H.O. Hirt's wood-paneled office, which, except for the addition of a stock-quote terminal, has changed little over forty years, and chatted with its current occupant, John Petersen, the chief executive officer. Why has Erie been so successful?" we asked.

"We don't keep our method a secret," said Petersen, a financial man who spent a dozen years at General Electric before joining Erie back in 1962. "It's service. We count on service. As we grow bigger and bring new people in, they've got to believe in our commitment or they don't belong here. If an adjuster can't take a call at 10 o'clock at night, he doesn't belong in that business.

"As our founder used to say, 'We are the competitors. We beat the competition on service, we beat them on price, we beat them on fairness.' This is the way to do business.

"We have a wonderful relationship with our agents. They're our front-line underwriters. We believe in the agent and always keep the market open. The other companies are in and out. Agents are salesmen; you've got to provide them with product. We continue to do that, even in very tough times.

"I've been here longer than most of the agency force, so for thirty years I've been going out into the field. I know many of the agents on a first-name basis. It's a family relationship. That doesn't mean we don't run the shop in a businesslike manner, but it's the personal contact with these people. If I take a vacation, it's probably going to be with an agent, or several agents. It's that kind of a relationship.

"On New Year's Day I call the top twenty-five producers personally to thank them for what they did in the past. One year I could only reach about eighteen of them and I thought, 'Maybe this is passé,' so I didn't do it the next year. But as I traveled around, agents said 'I missed your call.'

"It's a way of doing business. We're very automated. Ninety percent of the endorsements on our automobile contracts are never touched by a human being. They come in electronically, they're edited electronically, they're rated electronically. We carry it right through the printing. It is all delivered electronically to a mailroom.

"We don't have a business plan. People look at us and say, 'How can you run a business the size of yours without a budget or a forecast?' We're hands-on managers. If we need to buy new software or build a new building, we look at that and justify it at that time. We don't go a year-and-a-half ahead and say, "Now here's what you allocated to do next year."

Although Petersen doesn't scrutinize the expenses the way H.O. Hirt did, either he or the chief financial officer approves every project above $1,000 that isn't ongoing.

Stephen Milne, Erie's executive vice president in charge of insurance operations, knows what it's like to be an Erie insurance agent because, from 1991 to 1994, he was one. "I had a $4.5 million book of business, and 98% of it was with Erie. It's an economical way to do it, but you have to trust the company. By and large, the majority of our agents have faith that we're going do the right thing."

Erie agents tend to agree with Milne. Like Dan Johansen, they usually speak of the company in superlatives. They count on the Erie to be consistent and competitive year in and year out. Erie serves its agents well and looks for certain things in return. Says Milne, "We expect the agent to have conversations with prospects, to evaluate them as insurance risks. Once they determine that they're appropriate insurance risks, they have to write them properly. Attention to detail, completion of applications—we not only ask for it, we insist on it. We make it a religion."

Erie is equally careful in choosing its agents. In New York, which it recently entered, 200 have been interviewed, but only fourteen appointed. Says Milne, "What we're looking for—if we appoint an existing agency [as opposed to a start-up]—is somebody who's looking to reduce his number of companies. Our expectations are very simple: honesty and good underwriting."

Gene Connell, Erie's senior vice president and chief actuary, elaborates in his concise, to-the-point way: "If the expense ratio is 27%, that leaves 73% for underwriting." Careful risk selection, he says, is what makes all the difference. "My staff and I spend a lot of time talking to agents. We're trying to deal with the soft market by establishing the credibility of our pricing process and considering the agents' needs."

Jeffrey Ludrof, the senior vice president who oversees Erie's claims division, is eager to talk about Erie's SERVICE®. "Claims are opportunities to give people a taste of what they purchased from us," he says with enthusiasm. Erie's claims staff of 1,500 handled 491,000 claims last year. "Word of mouth comes from good claims service," Ludrof insists, noting that Erie has never advertised.

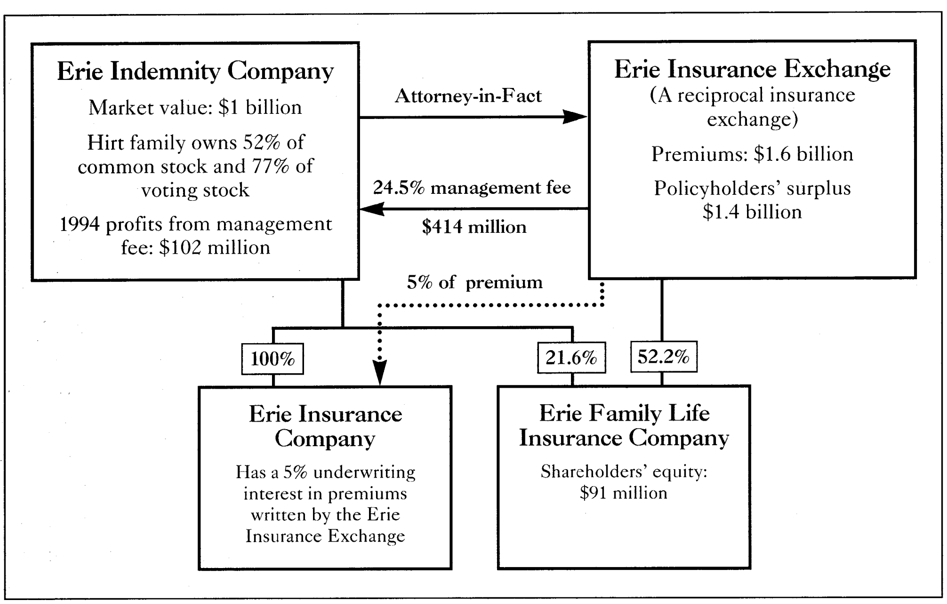
Erie has always been a family-run operation. In 1976, H.O. Hirt was succeeded as chairman and CEO by his son, F.W. Hirt, who in turn was succeeded by Thomas Hagen, H.O.'s son-in-law, in 1990. Although other large insurance companies (State Farm, for example) have been family affairs, in Erie's case the family connections are especially important because of the way the company is structured. Although Erie Insurance Exchange is a reciprocal (and, as such, is "owned" by its policyholders) it is managed by Erie Indemnity Company—for a 24.5% fee. For that fee, Erie Indemnity pays all of the Exchange's expenses other than losses and loss-adjustment expenses, taxes, licenses, and investment expenses. H.O. Hirt's children, F. W. Hirt and Susan Hirt Hagen, own 52% of Erie Indemnity's common stock and 77% of its voting stock. (Other officers and directors control 18% of the common stock.) Based on a recent price of $41 per share, the Hirts' stock is worth $550 million. In 1994 they received about $8 million in dividends from the company.

Until 1987 or so, there was almost no market for Erie Indemnity's stock. In fact, to some, the stock *appeared* to have little tangible value. Several major changes have taken place since then, and these have increased the value of Erie Indemnity exponentially. First, Erie Indemnity began raising the management fee that it charged the Exchange. The fee went to 20% in 1989, 23% in 1990, and 25% in 1991. These higher fees have enriched the company significantly since most of the incremental income went directly to the bottom line. Second, the company underwent a financial restructuring that included, over a period of several years, an 8,000-for-1 stock split. This increased the liquidity and marketability of the shares. Then, in 1992, a wholly-owned subsidiary of Erie Indemnity entered into a reinsurance pooling agreement with Erie Insurance Exchange, giving it a 5% underwriting participation in the Exchange's business. As a result, Erie Indemnity had $78 million of earned premium last year. Finally, in 1993, Erie Indemnity was required to register with the Securities and Exchange Commission and file an annual report and 10-K for the first time. The company now has 1,500 shareholders—according to John Petersen, it had about 100 in 1987—and its stock is traded, albeit very thinly, in the unlisted over-the-counter market.

The effect these transactions have had on the value of Erie Indemnity's stock can be appreciated by some of the facts and allegations spelled out in a lawsuit brought by the estate of James Arnold against two Erie agents, Frank and Gary Strock, and Erie's executive vice president and chief financial officer, Thomas Sider. The *Erie Daily Times* reported that in 1987 the Strocks offered to buy fifty Erie Indemnity shares held by the Arnold estate. Mellon Bank, the estate's trustee, contacted Thomas Sider and mentioned the Strocks' offer of $500 per share. (This was before any stock splits.) Sider allegedly said that there were no other buyers for the stock and that $500 per share sounded like a fair price.

In May of 1987 the Strocks bought the fifty shares from the Arnold estate for $25,000. Later, ten of the shares were sold to Sider for $5,000. Not too long after that, Erie instituted some of the previously mentioned changes. Today, those fifty shares, adjusted for stock splits, have become 400,000 shares worth $16 million.

The Arnold lawsuit alleges that the Strocks and Sider had inside information—that they knew about the upcoming corporate changes and made a "secret deal" to buy the stock at a low price. The Strocks and Sider denied any wrongdo-



ing, and the lawsuit was recently settled. The settlement was sealed by the court, and all sides have agreed not to discuss the matter.

Whatever the merits of the case were, several points are worth pondering. The Arnold estate's fifty shares represented 1.4% of Erie Indemnity's outstanding shares. A price of $500 per share implied a total value for Erie Indemnity of just $1.8 million, a ridiculously low figure. Why didn't Erie Indemnity offer to buy these bargain-basement shares? Did Sider apprise Erie Indemnity's CEO or board of directors that these cheap shares were available? Why did Erie foster an environment in which minority shareholders were unable to sell their shares at a reasonable price?

Despite all the gushing about Erie—by its agents, employees, policyholders, *and us*—there is another dark episode in its recent past that it will not discuss. In 1993, fifty-seven-year-old Thomas Hagen, the company's chairman and CEO (and husband of Susan Hirt Hagen who, with her brother, controls the company) either was forced out or resigned for "personal reasons." Hagen, who is still on the board, received a $677,123 severance payment the following year and served as "special consultant to the chairman of the board" until January 1995, when he was appointed Pennsylvania's secretary of commerce.

That the abrupt departure of a man who'd spent his entire career at the company wasn't even mentioned in the company's annual report is unusual. Two other senior officers also left the company at the same time, and John Petersen, the CEO, will be retiring this year. Noting these departures, one knowledgeable insider asserts that "the company is changing, and not for the better. The old line is leaving."

Is something going on at Erie Indemnity, and if so, will there be any shock waves for Erie Insurance Exchange and its agents? The compensation of the top officers increased dramatically last year (it still remains relatively modest, however) and, in April 1995, the four senior executives (other than Petersen) signed employment contracts guaranteeing them three times their annual salaries in the event that they're fired "without cause." (The company is looking both inside and outside for its new CEO.) It is always possible that, at some point, H.O. Hirt's children, or perhaps their heirs, may want to sell their shares. Whether the controlling shareholders' paternalistic attitude and the company's wonderful corporate esprit can survive another generation unscathed remains to be seen.

On the other hand, only a handful of companies in America can show a twenty-five year track record as great as Erie's. Its surplus has grown at a 22% compounded annual rate without the addition of any capital. (Even Warren Buffet hasn't done much better than that.) And, like Buffet's Berkshire Hathaway, this has been achieved without debt.

Although that kind of growth will be impossible to replicate going forward, as long as Erie remains above all in SERVICE®, it should do fine. ■

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Auto Insurance Report

The Authority on Insuring Personal and Commercial Vehicles

Vol. 1 #15 **Feb. 7, 1994**

Inside

Financial Disclosure Statements have been filed on both sides of the California pay-at-the-pump battle, revealing the scope of spending and where the money came from. **Page 3**

Best Commercial Markets Over Time: Ranking of states by average profit margins since 1985. **Page 7**

Commercial Auto Profits 1992-1985. Page 6

The Grapevine

An opportunity for non-standard writers may be developing in **Mississippi**. The **House of Representatives** has passed legislation strengthening the enforcement of the state's motor vehicle responsibility laws. **H.1095**, sponsored by **Rep. Ann Stevens** and others, hits drivers with a $1,000 fine, in addition to license suspension, if they are involved in an accident and fail to show financial responsibility either through a bond, a certificate of deposit, or insurance. The fine can be lowered to just $100 if the driver purchases insurance. A spokesperson for Rep. Stevens said it is expected the **Senate** will not go along with the bill as currently drafted, and the legislation will wind up in a conference committee. AIR

Auto Insurance Continues To Stay Outside Clinton Health Care Plan

When the Clinton health plan was just a rumor last fall, it seemed the health insurance portion of auto insurance would escape merger into a universal health system. Now, after months of battling and enough studies to fill the Library of Congress, it appears that original position will stand, and auto insurers will get to keep their slice of the business. (AIR, 10/25/93, P1)

Further, there are side benefits to the implementation of the Clinton plan that could save auto insurers billions of dollars.

Now all insurers have do to is to make this scenario comes true, and that will require continued battling.

Auto insurers are advancing many arguments for keeping auto insurance separate. Some worry about insolvencies, others about escalating law suits, others about

Please see CLINTON on Page 2

Illinois: Favorite Example For Light Regs, Heavy Competition

Ask auto insurers what they like best about the **Illinois** market, and you almost always hear "open, competitive environment." Ask the insurance department the same question, and you hear the same answer: "open, competitive environment." When regulator and regulated are singing from the same page, you usually get good news. In this case, an almost total lack of regulatory intervention in rate setting (and a population that sues less than many other large states) has created a fiercely competitive environment.

Here's the good news:

• Premium rates are low for consumers, ranking 22nd in the nation despite the presence of a giant urban center, Chicago. Those rates look especially good to a state with average income ranking around 9th in the country. Of the top 10 states in total premiums, only Ohio has lower

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Across the Great Divide

Imprisoned by the Freedom of the Road

We like traveling by car. Seeing the USA in a Chevrolet beats flying the friendly skies of United. Every time we set out down the lonesome highway we have visions of a simpler America, one of vast prairies, endless deserts, hokey roadfood joints, motels shaped like wigwams and hot-dog stands shaped liked pigs. We preferred the roadside before it turned into an expanse of golden arches and Whoppers.

Until the 1920s there was no real cross-country route; roads ended somewhere in Nebraska. Although the Lincoln Highway, completed in 1923, was the first paved route across America, it was Route 66, which follows an old Osage Indian trail and was immortalized in song and a TV show, that achieved mythic status as America's Main Street.

There's a restlessness to the American spirit that keeps us moving—especially to the open west—searching for space and freedom. The frontier has been pronounced dead many times: with the advent of the transcontinental railroad, when the Oklahoma territory was put up for grabs, and with the coming of the interstates. By 1969, the frontier, which in this century has been more conceptual than geographical, had so shrunk that the poster for the film *Easy Rider* read: "A man went looking for America...and couldn't find it."

Five years ago we went looking for America on Route 66. We began our journey in Oklahoma City, because that conjured up images of the Joad family of *The Grapes of Wrath* setting out for pastures of plenty in their Model T. Somewhere west of El Reno, Oklahoma, there's a sign that's the gateway to the west: "Last McDonald's for 150 miles."

Until the early 19th century hardly anyone went out west. By 1850, however, travelers on the Sante Fe Trail reported abandoned covered wagons and other detritus scattered along the route.

In the 1950s, an eccentric Texas millionaire named Stanley Marsh 3 (that's how he writes it) commissioned a work of art called *Cadillac Ranch*, which consisted of ten Cadillacs buried halfway in the ground, nose first, along the road outside Amarillo. Perhaps more than he realized, this was a fitting and bittersweet tribute to what the west had become and the force that wrought this change, the automobile. The shells of vintage Chryslers, Chevys, Fords and Plymouths, broken down and stripped but looking surprisingly fit, litter the west, in fields, backyards, dumps, roadsides, deserted gas stations, defunct burger joints and closed motels,

Route 66 was decommissioned some years back and replaced by Interstate 40. As a result, the towns that were bypassed are contemporary Angkor Wats. Texola, for example, located at a desolate sun-baked crossroads near the Texas-Oklahoma border, barely exists. Its wide streets are devoid of life and the shut-down stores are frozen in the late 1940s; the gas station and diner are abandoned. Contrast this with a 1946 guidebook describing Texola as a small town with "an old section of stores that truly savors of pioneer days...Old-timers still lounge on the corners."

The roadsides are filled with billboards. Hundreds of miles before Amarillo we see signs for The Big Texan, home of the free 72-ounce steak. Free, only if you can eat the 4½-pound steak, with a potato, in less than an hour.

The terrain is dry and barren in the Texas panhandle. Deep washes cut into the ground. We get out of our car and sit in the middle of the road for several minutes, our eyes following the broken white line until it disappears into the wide horizon.

We cross into New Mexico and head north into the solitude of the snow-capped Sangre de Cristo mountains, the high plains and the final leg of the Santa Fe Trail. We drive past fertile valleys along the Rio Grande and visit the impoverished Taos Pueblo, the oldest occupied pueblo in the United States, where Indians live in traditional adobe houses. Emblazoned on an adobe wall is a poignant reminder of the 20th century: "fuck you" spray-painted in large neon-blue letters.

New Mexican food is so hot that it brings tears to your eyes. At the M&J Sanitary Tortilla Factory in Albuquerque we have a bowl of menudo, a staggering concoction of chiles and cows' stomachs. We finish up with sopapillas, a soft fried pastry covered with honey.

Along an open stretch of western New Mexico a sign says "Continental Divide, 1 mile." A mile ahead, in terrain indistinguishable from anything else, was the Continental Divide Gift Shop and Trading Post.

The towns become farther apart in Arizona. The sun seems hotter. We ride the endless blacktop past the badlands and the Petrified Forest.

We leave Route 66, veering 50 miles north to the Grand Canyon. Four million visitors go there each year, and even though it's 300 miles long, they all go to the same spot. So it's back to the mother road and the western-Arizona desert where a billboard invites us to "eat upstairs at the 60-foot high teepee."

In Kingman, near the California border, we make a detour to the gambling town of Laughlin, Nevada, a nightmare land of blue-haired, beer-bellied, *True Detective*-reading tourists traveling in RVs. Inside one of the bright-light slot-machine low-roller casinos in this wretched torn-up strip of desert we see an unforgettable sight: a man at a blackjack table, hooked up to a portable oxygen tank, chain-smoking Marlboros.

Back on the open road: 20 miles outside Needles, California, we bid farewell to Route 66 and head into the loneliest stretch of the Mojave. After an hour we come to desolate Amboy, with its out-of-business two-pump gas station and diner. There are no people. A sign says "Town For Sale. You can be the mayor."

After eight days on the road in some of the most sparsely populated parts of America, we end our trip in Los Angeles. The congestion and the traffic are overwhelming.

Why, you may ask, did we drive 2,100 miles during our vacation? Perhaps the answer can be found in a country-and-western lyric we heard on the radio while passing through Texas:

> I'm a prisoner of the highway,
> Imprisoned by the freedom of the road.

Perhaps we still believe that you must lose yourself in America to find yourself. ■

The Insurance Beat

Misplaced Trust

ACCORDING TO *Lloyd's List Insurance Day*, the practice known as "intermingling"—using trust funds belonging to some Names to temporarily meet the debts of other Names—"is common through Lloyd's because managing agents are finding it increasingly difficult to fund individual Names' shortfalls by calling on the dwindling Central Fund."

Black Hole

MBL LIFE, which assumed the insurance obligations of defunct Mutual Benefit Life, recently reported to policyholders that its General Account statement showed a net worth of approximately $186 million. However, 41% of the company's $13.47 billion in assets was invested in mortgages and real estate.

In its publication *Customer Focus*, MBL reminded its policyholders that "there remains a 'hole'—a shortfall between the market value of the company's assets and its liabilities....Consequently, restraints on withdrawals of account values continue to be necessary at this time."

Jack the Ripper?

FOR A LONG TIME, A.M. BEST was the Will Rogers of insurance rating agencies—it never met an insurance company it didn't like. As a result, it received considerable criticism, much of it in the pages of this publication.

In our October 1994 issue, in the article "The Harder They Fall," we explained why Best would soon begin downgrading major insurance companies. Six weeks later Best's new, improved stance was unveiled, as The Home was demoted from A– to B+. Among other notable downgrades since then are some of Cigna's companies from A– to B++, Farmers from A– to B++, and State Farm Fire & Casualty from A++ to A+.

Although Best still has improvements to make—it should clarify its ratings definitions, adopt designations similar to those of the other raters, and align its ratings with long-term default ratios—its tougher stance has prompted V.J. Dowling, the ubiquitous and intrepid insurance analyst at Paulsen, Dowling Securities in Hartford, to come up with a nickname for the A.M. Best scion and vice president in charge property/casualty ratings: Jack "the Ripper" Snyder.

Bull Market

IN 1970 MARSH & MCLENNAN decided that Putnam Investments was a good business being offered at a reasonable price, and bought it for $30 million.

In 1994 Putnam earned a whopping $208 million—31% of Marsh & McLennan Companies' total profits. Putnam is so profitable that its earnings exceed even those of Marsh's U.S. insurance brokerage operations. Perhaps that's why Marsh's highest-paid employee is Lawrence J. Lasser, the president of Putnam. In 1994 he took home $11,320,000, almost six times as much as A.J.C. Smith, Marsh's chairman and CEO.

Easy Money

IF YOU'RE UNDER THE IMPRESSION that Conseco's deal to acquire Kemper fell apart because the financing was shaky—well, that's just not so, says Stephen Hilbert, Conseco's cocksure chairman, president, and CEO.

"Our lenders were steadfast in their willingness to provide financing, and they said so in writing," he declares in his company's recent annual report. "Our problem was not that we couldn't borrow the money, but rather that we'd concluded we couldn't pay it back."

That, of course, is a serious problem, and Hilbert doesn't say whether he informed his lenders of this minor glitch. Such an admission might have changed the banks' "steadfast willingness," although, given the current lax lending environment, it might not have.

"Bank financing is readily available for life insurance industry deals," notes Hilbert. For proof, one need look no further than Conseco's $1.1 billion plan to acquire the outstanding shares of its affiliates, CCP and Bankers Life: Chase Manhattan and First Union Nation Bank agreed to provide 100% financing for the transactions. (The Bankers' Life acquisition has since been scuttled.)

Although Conseco's increase in cash flow as a result of these deals wouldn't have covered the interest payments on its increased debt, we're certain of one thing: Hilbert assured the banks he'd pay them back.

Catastrophe Futures

IN THE OCTAGONAL PITS on the floor of the Chicago Board of Trade, frenzied traders communicate via shouts and hand signals as they buy and sell billions of dollars worth of futures contracts on corn, soybeans, oats, wheat, interest rates, and other things.

Not all commodities generate a lot of activity, however. Off in a corner of the floor is a desk—not a trading pit—where the action (or lack thereof) in catastrophe insurance futures takes place.

To say that catastrophe insurance futures haven't yet caught on is an understatement. Despite their potential, trading has been limited and only two states—Illinois and California—allow insurance companies to deal in futures. In one recent week, just twenty-six contracts traded.

To put that in some sort of context, even the *cheddar cheese* contract on the New York Coffee, Sugar and Cocoa Exchange is more active. It trades about fifty contracts a week.

The Great Insurance Opera

FROM THE *Portland Oregonian*:

> Opera is about extraordinary people: scoundrels and fanatics, courtesans and greedy gods. But how about two insurance agents?
>
> David Schiff's new opera, called *American Life and Casualty*, is about an imaginary meeting between two New England figures, composer Charles Ives and poet Wallace Stevens. Both were extremely successful insurance agents....
>
> No premiere has been set but the Portland Opera is an interested party.

David Schiff, the composer of *American Life and Casualty*, teaches music at Reed College. He is not related to David Schiff, the editor and writer of *Emerson, Reid's Insurance Observer*.

David Schiff, the editor and writer of *Emerson, Reid's Insurance Observer*, circa 1973.

Even as a misanthropic young man meandering through the streets of New York in a psychedelic haze, David Schiff knew that he wanted to write about the insurance business. Of course, his options were somewhat limited. With his abysmal grades, poor attitude, and aversion to work, most careers were simply out of the question.

Insurance, however—where intellect, judgment, and competence are not prerequisites—not only welcomed a pensive curmudgeon like Schiff, but gave him the greatest job in the world as well: observing the rampant dementia, deceit, and sophistry in the industry and chronicling it in a fearless newsletter beholden to no one.

So Schiff lucked out. He spends his days waist-deep in insurance-company filings, financial statements, trade publications, and actuarial reports. His nights are spent penning cutting-edge exposés, groundbreaking analyses, and hard-hitting commentary in his trademarked tone of acerbic irreverence.

Yes, Schiff's job is so much fun that he ought to be willing to do it for free, but he dreams of the fabulous wealth and international renown that come from owning a successful newsletter about the insurance business, so...

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