



Beyond the Balance Sheet

Once again we enter this renewals season facing the impact of a major event in our industry. This year, we must come to terms with hurricane Katrina - both the extent of the human and financial loss to the states of Louisiana and Mississippi, and the losses to insurers and reinsurers. Depending on how much the industry as a whole is impacted, I expect there will be continued discussion about the industry's ability to absorb such events and continue to assume new risks. And you, the cedant will continue to question the quality of the coverage you are buying and the stability of the reinsurers you buy from.

The truth is, events such as hurricane Katrina are exactly the reason why insurance and reinsurance exists. How a reinsurer responds to such 1-in-100-year events is a good indication of their financial strength and long-term viability. But what else can you do as a buyer to be sure you are accessing the best coverage and working with the most secure partners? There are other areas - beyond the balance sheet - that every reinsurer should be willing to expose should they be asked, and you should feel free to ask them. We suggest you should challenge your reinsurers, and ask questions that will give you the most holistic view of their product and service.

The issues of concern in placing your risk could fall into a few key categories: Security, Underwriting Process and Service, and External Factors. Another area of concern for you may be price. I venture to say that price should be the last part of the analysis, and that the answers you seek lie somewhere between the balance sheet and price.

First, Security. We continue to hear about companies going into run-off or running into problems that lead to downgrades and questions about security. A reinsurer should be comfortable explaining to you how they think about risk. What risks they accept that can damage their ability to pay your claim, and how those risks are managed. They should be able to show you how well prepared they are to cope with large or "shock" losses, and how their own strategy may impact the security of their product.

Underwriting Excellence and Service are always part of the evaluation process, with an emphasis on such favorite terms as underwriting discipline and expertise. But what do those mean? I challenge you to look further at how a company arrives at its underwriting decisions, how their decision-making process is structured and what tools they use. Beyond that, what sort of partnership can you

expect from your reinsurer. If you are looking for additional service, what can they provide?

Finally, External Factors can impact how you are treated as a cedant. Every company must manage various audiences, and must make sure that their diverse constituencies are kept in balance. A reinsurer should be willing to articulate how their commitments to brokers or shareholders impact their business with you.

As an insurer, you stand on the front line of risk. At PartnerRe, we are in the business of assuming risk to help you manage yours. We have built our organization on the basis that we must be the best at understanding, assessing and managing risk in order to live up to the commitment we make to you. We invite you to test our approach and the added value we bring to the table.

Patrick Thiele
President & CEO

Inside:

Protecting Life Portfolios with Cat XL Reinsurance	2
When the Tables Turn	3
PartnerRe U.S. Looking Ahead To 2006	5
New Appointments	7

Protecting Life Portfolios with Cat XL Reinsurance

Disasters such as Piper Alpha, the September 11 attacks and the 2004 Asian tsunami frequently lead not only to property damage, but also, sadly, to large loss of life. Insurance markets are expanding in a world faced with a forecast for increasingly frequent and/or severe weather events, and with growth in global air travel and risk concentration. The potential accumulated loss from such events is a major concern for both Non-Life and Life insurers. Catastrophe excess of loss reinsurance (Cat XL) is an established risk management solution in Non-Life markets. In comparison, the impact of these events on Life portfolios is often overlooked. Life Cat XL is, however, available, offering Life insurers protection against the potentially severe impact of accumulated event losses. In this issue, we look at how it works, and how the risk environment, particularly with respect to global travel, is changing the way we analyze risk.

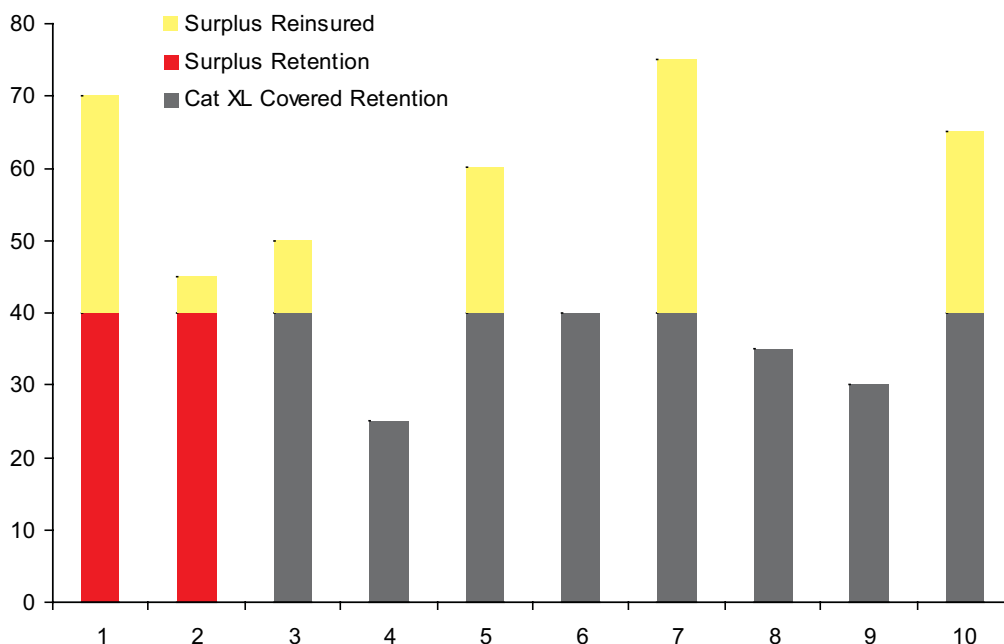
Insurance companies traditionally control exposure on an insured or individual basis by introducing limits and by reinsuring exposures above a certain level, the retention. Life portfolios, for example, include a maximum net retention (to the insurer) per life. A single event, however, may have the potential to simultaneously impact more than one insured or individual, and/or more than one line of business. The accumulated losses from these events can be severe. From a Life perspective, the September 11 attacks, for example, claimed approximately 3,000 lives with total sums assured estimated at up to USD 40 billion. More than 300,000 lives are believed to have been lost in the 2004 Asian tsunami, and although insurance penetration in this instance was low, the numbers really speak for themselves. Just as Cat XL protects Non-Life portfolios, Life Cat XL is available to protect the retention

of Life portfolios against the highly volatile and severe nature of such events.

Life Cat XL coverages work in much the same way as their Non-Life equivalents in that capacity is provided per event, limited by an hours clause. Typically excluded are nuclear, biological and chemical risk, war, civil commotion, epidemic and nuclear, biological or chemical terrorism. Standard to Life Cat XL is a double trigger, requiring not only that the specified event retention be exceeded, but also that a certain minimum number of insured accidental death claims be caused by the event (the 'life warranty'). Coverage is usually limited to accidental death originating from and occurring within twelve months of the event, but may also be adapted to other Life benefits, such as Total and Permanent Disability.

Risk assessment and pricing for Life Cat XL requires estimation of the probability of an insured event involving more than a certain number of lives (the specified life warranty), combined with estimation of the average claim per life and the distribution of losses around this average. Assumptions by Strickler (1960) are the basis of both these components of the risk calculation. Strickler utilized the annual, accidental death rate per million of the (global) population. Given sufficient loss data, modelers now refine risk assessment by creating geographical sub-populations of death rate linked to different economical and environmental factors. At PartnerRe, our models currently evaluate risk using separate parameters for eleven, distinct geographical areas. These parameters are based on the latest data from the World Health Organization and U.S. Disaster Center.

Further adjustments then need to be made to reflect the fact that a Life portfolio will not necessarily have the same risk profile as the global population. The first reason



Example of event loss distribution: The cedent has a surplus reinsurance and Life Cat XL to protect its surplus retention. The triggers for the Life Cat XL are in this case (1) a cedent event retention of less than 80 and (2) a 3 life warranty.



Disasters such as the Asian tsunami frequently lead to both property damage and loss of life.

for this is that groups may exist within a portfolio for which an enhanced accumulation risk (compared to the insured portfolio) could appear, such as in the case of a touring orchestra or football team. This is known as 'contamination risk'. The reinsurer will examine each case individually, accordingly adjusting the related terms and pricing. The other reason for adjustment is that not all victims of an event will be insured. Of those that are, not all will be insured by the same insurance company. Risk assessment and pricing calculations for a particular portfolio measure and adjust for this 'dilution risk' by utilizing knowledge of the portfolio's concentration in the population.

Of course, no risk is static, which is why using the latest statistics is critical to accurate risk assessment. However, concentrating on the latest statistics from the portfolio, country or specific geographical area ignores one increasingly important factor: global travel. The 2004 Asian tsunami highlighted how this factor influences portfolio exposure by introducing a potentially higher risk of death, and an additional accumulation risk, anywhere in the world. Rather than looking solely at a portfolio's area-specific death rate statistics and accumulation risk, accurate risk assessment therefore also requires an adjustment to reflect this factor. Flexible, sophisticated modeling and pricing systems are required. At PartnerRe, our Life actuaries are carrying out research into adjustment parameters for travel that will enable us to offer our clients a more accurate and up-to-date assessment of their catastrophe exposure.

Life Cat XL provides Life insurers with a means of protecting their balance sheets against the potentially large and volatile accumulated losses resulting from accidents and natural catastrophes. At PartnerRe, we have developed a pricing tool for Life Cat XL that offers our Life clients an efficient means of evaluating and transferring this risk. Our team of experienced Life actuaries and underwriters are continually refining and updating this tool to incorporate the most up-to-date information and modeling techniques, and with regard to the ever-evolving risk environment.

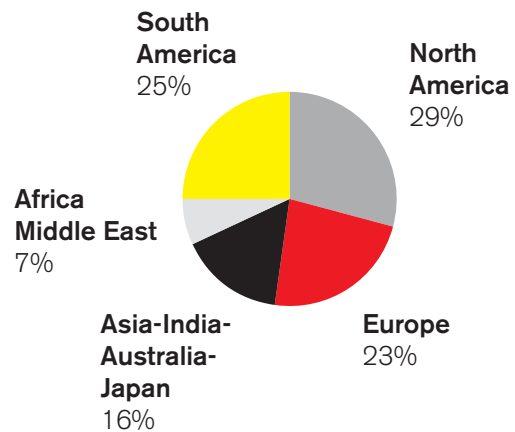
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When the Tables Turn

Lawyers are an established, well-regulated and organized profession, advising and legally representing their clients in an environment of growing litigation and claims awareness. However, the tables can turn. As professionals with a corresponding duty towards their clients, lawyers can also find themselves the subject of litigation. In this article we look at how their business model and Professional Indemnity (Global)/Lawyers Errors and Omissions (U.S.) insurance serve to mitigate risk in this disciplined sector.

There are currently approximately three million lawyers around the world. The chart below shows how this total is split by geographical area, with North America and Europe contributing a significant 52 percent. The grouping of lawyers into large law firms is mainly characteristic of Anglo-Saxon countries, the majority (84%) of the top 100 firms (in terms of number of members) being in the U.S.

Distribution of the Worldwide Lawyer Population



When agreeing to represent a client, a lawyer assumes the duty to perform professional services with the requisite standard of care. This is generally taken to mean that he or she agrees to represent the client with the skill and knowledge commonly possessed and exercised by a reasonable, careful and prudent lawyer in the same jurisdiction. The lawyer also generally owes his client the following: fiduciary duty, a general duty of trust encompassing undivided loyalty, confidentiality and a commitment to represent. Litigation may follow from failure to carry out these duties (negligence) if the claimant has experienced a loss. Insurance is available to protect against this eventuality.

It is estimated that approximately 80% of legal malpractice claims are settled within 24 months of first notification. The remainder are long tail, often taking in excess of five years to settle from first notification. The long tail nature of some legal malpractice claims leaves much room for loss inflation and introduces considerable uncertainty into loss estimation analysis. As a result, re/insurance pricing is exposed to potentially substantial adjustment should it later become apparent that loss inflation was underestimated.

Claims can arise from any area of the law. However, the principle sources of legal malpractice claims in terms of

frequency are currently: Personal Injury (plaintiff & defense), Real Estate, and Family Law. In terms of alleged error, claims can be classified as follows: Failure to know or properly apply the law, planning error, inadequate discovery / investigation, failure to know or ascertain deadline, conflict of interest, failure to understand tax, error in public record search, and error in mathematical calculation.

The law profession is generally well structured, regulated and organized, often through associations, at the city, region, state or national level. In most countries, professional indemnity / E&O insurance for lawyers is mandatory either by state law or by relevant law society or bar association regulations. Each association usually negotiates and either buys, or recommends where to buy, insurance on the behalf of its members. In conjunction with their mutual or insurance arms, these associations also collect and analyze detailed regional claims data in order to develop the most ideal risk management training, procedures and tools. This reduces claim incidence and severity, serving to improve the ethics and professionalism of the profession, and to optimize the cost of insurance premiums. All these elements combine to make lawyers a powerful and disciplined group of insurance buyers.

We estimate that the worldwide gross written premium for this market is approximately USD 2.5 billion. Although there are general insurance companies active in the market, the worldwide market for the primary layer is in fact dominated by specialized mutual insurance companies. The establishment of mutuals was predominantly a result of difficulties experienced in attaining much needed, affordable insurance for lawyers in the late 70's and early 80's. This concentration into specialized companies has enabled the development of reliable, accurate claims data.

Actuaries determine risk price by analyzing the relevant regional claims data, which is generally of a high quality. This is then combined with specific market knowledge and regionally defined legal and social economic risk control factors, which not only affect the risk now, but which could influence its future development. These considerations are particularly important in this sector due to the potential long tail nature of the risk.

At PartnerRe, we have separate Global and U.S. operations that deal specifically with Specialty Casualty risk. The underwriters and actuaries within these operations have experience in all forms of Specialty Casualty risk, including full awareness of the emerging legal and market trends and developments at both a national and international level. We provide our clients with intelligent and focused risk enabling and mitigating solutions based on a combination of this know-how, together with the utilization of advanced, flexible capital allocation and pricing systems.

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An extended version of this article is available at www.partnerre.com.

Policy terms and conditions are generally as follows:

Policy Trigger

Policies are commonly issued on a claims-made basis, typically with unlimited retroactive cover and extended reporting periods (predominantly to accommodate claims relating to retired lawyers).

Limits

Policies specify a limit for each and every loss, the majority of markets capping exposure with an annual aggregate limit. A minimum limit may be required, which is either fixed by law or by the relevant association. Limits of course vary depending on the market and size of the particular concern: In the U.S., Canada and Western Europe, for example, small firms usually purchase USD 1M/1M, medium firms (10-50 lawyers) between USD 10M/10M and USD 15M/15M, and large firms anything from USD 25M to USD 100M, with an aggregate set at a multiple of the each and every loss limit. Deductibles can be flat or a set, capped percentage of the loss limit. A single-lawyer practice would commonly have a deductible ranging between USD 500 and USD 5,000.

Cover

Policies indemnify legal liability resulting from 1) the delivery of professional services, and 2) personal injury arising out of professional services. Professional services normally means services that the insured performs for his or her client in their capacity as a lawyer, mediator or arbitrator, notary public, administrator, conservator, executor, guardian, trustee, receiver, or in any fiduciary capacity.

Personal injury normally means false arrest, detention, imprisonment, wrongful entry, eviction or invasion of right of occupancy, defamation, libel or slander, publication or utterance in violation of an individual's right of privacy; malicious prosecution, or abuse of process.

Exclusions

The majority of markets exclude: fraud, dishonesty or criminal acts, any fiduciary duty related to employee pension funds, claims made by a present or former or prospective partner, director, stockholder, employee, or employee of the insured unless such claim arises out of the professional services of the insured in a lawyer/client relationship, claims arising out of investment advice, claims for damages or expenses in connection with any claim made against an insured as the beneficiary of any trust or estate, claims arising out of bodily injury or property damage, and claims first asserted prior to the effective date of the policy.

PartnerRe U.S. Looking Ahead To 2006

Reinsurers have typically underwritten 80 to 90% of their business for a particular underwriting year by the time July 1 renewals are concluded. The 2005 underwriting year, for a reinsurer, is essentially complete. We know what's happened to our book of business, and we believe we have a good understanding of our projected profitability for the year. Now it's time to start turning our attention to 2006. We thought this issue of PartnerReviews would be a good opportunity to open the lines of communication with our broker and cedant business partners about how PartnerRe U.S., at this point in time, views the 2006 reinsurance market. We'll be meeting with many of you individually throughout the fall, at both conventions and individual renewal meetings, where we hope to continue – and expand upon – this dialogue. PartnerRe U.S., located in Greenwich, writes all lines of business for U.S. clients, except for catastrophe and other worldwide lines, which are written by our Bermuda, Zurich and Paris offices.

2006 – A Transitional Market

Prices – How much is enough?

2002 through 2004 were hard market underwriting years in the U.S., most visibly characterized by strong price increases that industry observers agree brought insurance and reinsurance lines to a profitable level after the very poorly performing years of 1997-2001. In 2005, price increases halted for most lines, with prices flat or declining, in some cases significantly for many lines of business. At the same time, economic forces were at work and loss cost trends continued their inexorable climb. There is no question that, catastrophe experience aside, policy year 2005 will be a less profitable year than 2004 for almost every line of business.

Some underwriters in both the insurance and reinsurance markets argue that prices overshot in 2002-2004, and that the price reductions we now frequently see are a reasonable adjustment to more appropriate, yet still profitable levels. Particularly for an individual policyholder with good, claim-free, experience, it can be hard to disagree that a flat or slightly reduced premium could be appropriate, most especially given the large increases that many policyholders saw in the hard market underwriting years.

Reinsurers, however, tend to think on a portfolio basis, not surprising considering that with treaty reinsurance we transfer portfolios of insurance policies. Some of the U.S. casualty lines where reinsurance tends to be bought performed at the 200-300% loss ratio level in 1997-2001; many national account property per risk treaties in 1999 and 2000 performed at a 100% loss ratio level. Even regional treaty business performed, in many cases, at a 100% loss ratio level. To bring a loss ratio of 100% down to 65%, prices have to increase by 55%. To bring a loss ratio of 300% down to 65%, prices have to increase by almost 400%. In the context of the 1997-2001 starting point, the hard market price increases, while large, may not have been too large for these portfolios.



We expect these differences between the individual policyholder versus portfolio viewpoint to be a major theme during 2006 reinsurance renewals. While policyholders may feel they deserve a price decrease, insurance companies will attempt to maintain the price adequacy of their portfolios. Similarly, reinsurers underwriting from the portfolio perspective, may be reluctant to accept decreasing prices, even those that appear moderate. A reinsurer, underwriting from a portfolio perspective, may be reluctant to accept decreasing prices, even those that appear moderate. A 10% price decrease, coupled with the 6-8% annual loss cost trend typical of a U.S. casualty portfolio, can lead to an approximate 20% loss ratio increase in one year, suddenly moving a profitable portfolio to an unprofitable position. Of course these are statistics, and the loss cost trend may not, in reality, move up smoothly by 6-8% every year. The history lesson of 1997-2001 in the U.S., though, is that over a multiple year period, loss costs will increase by approximately that annual amount for a casualty line, and similar economics, though less extreme, hold for short-tailed lines. Thus, any year in which prices lose ground compared to the loss cost trend will depress profitability for both insurers and reinsurers for years to come. Open, honest and transparent communication between a reinsurer and a cedant will be key to working through these issues in 2006.

Communication

The reinsurance marketplace is emerging from several years of transition, which saw several well established reinsurers discontinue operations in the United States. As a market, we are probably only beginning to assimilate the impact of this change:

- Cedants have felt a significant disruption in their reinsurance partners, which are only now stabilizing into new relationships.
- Cedants have been concerned, coming out of the hard market years, that reinsurers aren't communicating with them as much as they would like, and that new reinsurers aren't sufficiently familiar with the unique characteristics of their book of business.
- Cedants are looking for value-added feedback in the form of face-to-face meetings and audit feedback,

both as outside confirmation of their business strategies and as evidence that reinsurers are paying attention and are sincerely interested in the specifics of their business.

- The run-off activities of the discontinued operations, have, in some instances, appeared disruptive to cedants. This is causing some cedants, for some situations, to question the value of reinsurance. PartnerRe U.S. has always placed a premium on good communications with both brokers and cedants, and we plan to step up our efforts to make sure communications are frequent, transparent and useful to our business partners in 2006. What should you expect to see from us?
- Face-to-face meetings, both visits and audits. Written underwriting audit feedback is always available on request.
- PartnerRe U.S. attends every major insurance conference – and many smaller conferences. We are always interested in meeting with brokers and cedants at these conferences. Please let us know if you are attending a conference where there might be an opportunity to meet.
- Individual meetings with our underwriters and senior management. We encourage our brokers and cedants to meet with us, to find out more about PartnerRe and our business philosophy, and/or to discuss issues related to a particular reinsurance program. We encourage cedants to visit our offices in Greenwich, and we are always happy to come to you. Let us know if you would like to find an opportunity for an individual meeting at your site or at our Greenwich office.

PartnerRe U.S. – 2006 Risk Appetite

PartnerRe has a conscious strategy of diversification. With but a few exceptions, we are prepared to evaluate most risks presented on the reinsurance market. Every account is accepted on its own merits. There will be no change to this philosophy in 2006. In the U.S., we are prepared to underwrite the full range of reinsurance submissions available in the market, subject to the few exceptions enumerated below.

There are two key decision points in our underwriting process:

- The quality of the primary insurance operation. We like to get very close to the cedant, in order to develop a deep understanding of the quality of the insurance operation we will reinsure. This evaluation is one of the most fundamental factors in our decision to participate.
- Price adequacy. We are committed to our cedants, but in the context of a fair and reasonable economic relationship.

We encourage cedants and brokers to resubmit reinsurance submissions to us, even if we have been unable to participate in the past. If the reason was a disagreement on the appropriate reinsurance price, every year is a new opportunity to come to a meeting of the minds, and consummate a successful deal.

By line of business, our underwriting appetite is wide. In our U.S. office, we will underwrite broadly across all lines of business and customer types. The few exceptions are:

- Credit, aviation, engineering and political risk are considered world-wide lines by PartnerRe, and are written by our Zurich and Paris underwriting units, even for U.S. clients.
- Similarly property catastrophe is written out of Bermuda for U.S. clients.
- PartnerRe is not currently a market for accident & health, including medical stop loss, in the United States.

In addition to the standard property and casualty lines, we will be active in the professional liability, medical malpractice and D&O lines in 2006. We also write crop insurance, surety and terrorism covers, and we hope to increase our participations in these sectors in 2006.

Looking ahead

We look forward to meeting with you during the remainder of 2005 and into 2006, and welcome the opportunity to discuss these issues, as well as any others of interest to you, during the upcoming conference and reinsurance renewal season. We are committed to working with our brokers and cedants to fully explore the challenges facing us all, as our market continues to transition. We look to stay in close touch, so that we can best understand how we can assist you in the period ahead.

Contributor: Robin Williams, EVP, Chief Underwriting Officer, PartnerRe U.S.

New Appointments



As of July 1, **Ian Houston** joined PartnerRe as Head of Marine Underwriting, bringing with him 18 years of industry experience. Ian joins the company from Converium, Bermuda, where he most recently held the position of Head of Global Risk Pooling, responsible for the management of the gross to net account for all

lines of business. Ian also has a strong background in Marine Global management and underwriting at Converium, Liberty Re, Union Re, and M&G Re. His global market knowledge and depth of Marine risk know-how, perfectly positions him to lead the further positive development of our Marine operation.



Effective January 1, 2006, **Emmanuel Clarke**, currently Deputy Head of Business Unit Specialty, will be promoted to Head of PartnerRe's Global (non-U.S.) Property and Casualty business unit, replacing Jean-Marie Nessi, who will pursue a new business venture. Emmanuel will be responsible for all of the Group's

general property and casualty business outside the U.S., reporting to Bruno Meyenhofer, CEO of PartnerRe Global. He will begin to work closely with Jean-Marie and the P&C team immediately, in order to ensure a smooth transition during the upcoming renewal period. As of January 1, 2006 Emmanuel will also become a member of the Global Executive Management, as well as a member of the Group Senior Operating Management.

Since his appointment to Deputy Head of Specialty in April 2004, Emmanuel has taken an important leadership role in the Specialty team. With more than 10 years' experience in the reinsurance industry, Emmanuel joined PartnerRe in 1995 and was appointed Head of the Credit and Surety unit in 2001. He holds a Masters Degree in Finance from Paris Dauphine and an MBA from City University of New York.



Effective January 1, 2006, and following a transition period with Emmanuel, **Marcus Pollak** will be appointed Head of the Credit and Surety unit, reporting to the Head of Worldwide Specialty, Kurt Angst. Marcus joined PartnerRe in 2001 and has served as Senior Underwriter and Deputy Head of Credit & Surety, in charge of an underwriting team

covering USA, Canada, Northern and Eastern Europe. Prior to joining PartnerRe, Marcus held positions in Marine underwriting at Swiss Re, and finance at ABB. Marcus holds an Executive MBA from the State University of New York.

Photos

Corbis Images

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