



THE BETTERLEY REPORT

EPL VALUE-ADDED SERVICES 1999: VALUE-ADDED SERVICES BECOME MORE VALUABLE

RICHARD S. BETTERLEY, CMC
PRESIDENT
BETTERLEY RISK CONSULTANTS, INC.

Editor's Note: In this issue of The Betterley Report, we evaluate the loss prevention and control services offered by 30 leading Employment Practices Liability insurance companies. As noted in our last report (1999 EPLI Market Survey, published in October 1999), carriers continue to pour significant resources into developing services to attract and retain customers. These services have become the major source of product innovation, and offer employers potentially valuable tools to reduce their EPL exposure.

As the services component of EPL has become more developed, we have expanded our analysis. Our introduction this issue discusses additional types of services and gives more information about existing services. In this report, we surveyed the services of 30 leading carriers and reviewed samples, such as handbooks websites, and software. The carriers have reviewed the accompanying tables, but as always, our comments are based on our own interpretation and evaluation of the carriers' material.

Note that we listed both EXCEL and Starr Excess in this report, although they do not offer EPL services to their insureds. Both carriers focus on either large employers or the excess market, making EPL services less critical to their insureds. We included their contact information, to remain consistent with our EPLI Market Survey. And we note with regret ACE USA's withdrawal from the monoline EPL market.

Since this area is evolving rapidly, please see our website (betterley.com) for updates.

INTRODUCTION

We have been closely following the EPL industry since 1991, noting in particular the rapid and creative product innovation that characterizes this product. In particular, we have observed with interest the research and experimentation of the leading carriers as they try to find the right mix of product quality, marketing strategy and pricing to successfully compete in this specialized field.

The original competition revolved around three critical issues:

- How broad to make the coverage? Carriers learned over time that employers wanted broader coverage than they originally offered, and that it was prudent to offer such broader coverage.
- How to market this new coverage? The slow growth of this product surprised many of us; it took a while to learn how to get employers to buy such a compelling product.
- What price was appropriate for the risk assumed – and competitive? Carriers have been extremely aggressive in lowering their rates.

In the past three years, carriers have become quite competent in these three areas of competition, developing very broad coverages, effective marketing techniques (in conjunction with an active broker community), and attractive prices. At the same time, numerous new competitors have entered the market in search of business (and at the request of their agents and brokers).

NEXT ISSUE:

Managed Care Liability Comes of Age:
We Examine Four Leading Markets

LIST OF TABLES

Contact and Product Information	8
Services Offered - Employment Practices Audit or Other Loss Prevention Surveys	14
Market Information	15
Elements of Audit	16
Services Offered - Employee Reporting Line (800#) . . .	17
Services Offered - Consultation (800#)	19
Services Offered - Statistical Information and Analysis	21
Services Offered - Defense Counsel Qualifications . . .	22
Services Offered - Information and Sample Materials . .	24
Services Offered - Training	26

Which brings us to EPL value-added services. How can a carrier compete when it has maximized coverage innovation, marketing strategy and price? Well, one way is to add services to the product. Much like the innovation in Property and Boiler & Machinery Insurance—and, more recently, Workers Compensation—adding additional services can be an attractive way to make a carrier’s product more attractive.

Value-added services are appealing to insureds if the services appear valuable. Of course, services that nobody wants aren’t appealing, but services an insured needs, particularly services they may already be buying separately, are very attractive. Boiler inspection services, for example, not only have the appeal of reducing potential damage, but also are required by law; if an insured has to have inspections, they may as well be received “free” with insurance.

Adding quality services has several key benefits to the carrier, as well. The most obvious is the opportunity to improve the risk characteristics of its insureds, a lesson learned in Property Insurance (Highly-Protected Risk) more than a century ago. More recently, managed care services for Workers Compensation claims is another example.

A less obvious benefit for the carrier is the de-commodification of its products. Following the example of Property and Workers Compensation, we see many insureds who happily pay more for their coverage, knowing that the value-added services are worth more than any short-term premium savings.

EPL is no different; it is a line that offers substantial opportunity to improve risk characteristics and link customers more closely to the insurer.

Of course, improving the risk is also of enormous benefit to carriers, so EPL value-added services can be a real win-win for insureds and insurers, if they are effective. Are

the services that carriers offer effective? Do carriers offer the right mix of services, providers and underwriting credits? Will Human Resource and Risk Management professionals value these services?

If so, they will help reduce the problems of Employment Liability; if not, they will just drive up the cost of the policy. Quality services can be costly, both to purchase and to implement. Are these services really valuable to insureds, or are they just going to drive up the cost of EPL coverage? We offer our comments at the end of this article.

Several exciting new features have been added to some carriers’ products. Sophisticated statistical analysis, particularly valuable for larger employers, is a new feature offered by several carriers. Employee-reporting 800 #s are another service, which encourages employees to confidentially report possible EPL transgressions.

MARKET TRENDS

Carriers have continued to add services, and to add depth to existing services, during 1999. Smaller employer-oriented carriers in particular have added 800# consultation services, and additional sample materials.

Chubb Executive Risk has taken the best of both Chubb and Executive Risk’s products, to offer a nice combination of free and optional subsidized services.

AIG has added a lot to its services package, with Lexington preparing to roll out a website with an educational tracking component that is sure to be a hit. However, the website is not available to its program insureds unless specifically negotiated.

Finally, Zurich has added a nice feature by paying the professional society dues for member insureds of the Society of Human Resource Managers. (Paying RIMS dues should be next!)

As EPL services have matured, we have analyzed their features more deeply. For example, we present more information about the elements of EPL audits, having found that some audits are more complete than others. A service that is not new, but we think worth examining, is a carrier’s skill at selecting members of their defense panel, and their willingness to refer their insureds to competent counsel.

We hope this issue of EPL Value-added Services provides our readers with more information to help them evaluate the many high-quality products available to employers. We also hope it will help carriers build and deploy more effective services.

TYPES OF SERVICES

In this report, we surveyed the EPL services offered by 30 of the leading carriers, focusing on 7 key areas:

- Audits of employment practices, which are an independent review of an insured’s employment practices, such as handbooks, supervisor training, and dispute resolution.
- 800# consultation services, which allow an insured to speak with an employment practices expert, often an attorney, on employment matters.
- 800# employee-reporting services, which allow an employee who is aware of a possible EPL problem to report it confidentially to a third party.
- Statistical information and analysis services, which employers can use to identify possible hiring disparities, and/or to help defend in litigation.
- Defense counsel.
- Sample documents, such as employee handbooks, that have been specially developed to comply with EPL law and regulations.
- Training and information, such as newsletters and websites, which can help employers stay current on EPL matters.

Not all carriers provide all of these services, and, as might be expected, the depth and quality can vary significantly.

Note that we have not included an analysis of defense management capabilities of the carriers. While important to the insured, we view these as services provided by the carrier for its own benefit, although clearly benefiting the insured as well. Value-added services, conversely, are primarily offered as a benefit to the insured, although benefiting the insurer as well. Defense management would and should be done even if the insured doesn’t value it; services are primarily offered in the hope that the insured wants to make use of them. A small, but we think useful, distinction.

The range of services, who provides them and their value to employers are factors which vary significantly, challenging insureds and their advisors to evaluate them carefully. Poor quality services can be damaging to the insured, so careful evaluation and implementation is critical.

SOURCE OF SERVICES

Different carriers have taken different approaches to providing these services. Some provide these services largely through the use of their own staff; others retain outside firms.

We think both methods work. It is true that internal staff can be more responsive to an insured’s needs, but few carriers have enough EPL volume to justify internal staffing with sufficient expertise to do a really good job of supporting EPL services. For those that can, such as Lexington, there is a great opportunity to provide a high level of expertise and responsiveness to insureds.

In our accompanying tables, note the pervasiveness of several providers of EPL services:

- Jackson, Lewis, Schnitzler & Krupman is the most commonly used law firm.
- Labor Consultants of America and Laurdan & Associates are very active in the human resources consulting area.

Many services are generic to the EPL industry; the standard services of one company may be available to insureds of several different carriers. However, many of the services are customized, such as Traveler’s arrangement with Labor Consultants of America (LCA).

Since last year’s report, Chubb has acquired Executive Risk, and combined the two packages of services. From the Executive Risk Checkmate services list, they have continued the:

- 800# consultation line,
- newsletter,
- desk reference manual, and
- web site.

All of these are free to insureds.

At a subsidized cost, wherein Chubb pays 50 percent of the cost, up to 10 percent of the policy period premium, the following services can be arranged from any of the its providers:

- employment practices audit,

- 800# employee reporting line,
- statistical information and analysis,
- custom employee handbook, and/or
- training seminars.

Other EPL services that the insured may need can be considered as well.

We continue to like this type of service, mostly because it allows the insured to select the service they want, rather than use a preselected array of services. The market seems to agree, particularly HR professionals who want to customize the services they buy and control which firms provide them.

EPL AUDITS

EPL audits are intended to provide an independent, expert evaluation of the quality of employment practices of an insured (or, sometimes, an applicant). They are similar in purpose, but not in technique, to a loss prevention inspection for Property or Workers Compensation.

Our evaluation is based on true EPL audits, done for the benefit of the employer, and only incidentally for the benefit of the insurer. This is in contrast to an underwriting audit, which is largely for the benefit of the carrier, and helps determine the acceptability of the applicant and appropriate pricing posture. It does not include self-audits, which, although useful, we do not consider a truly independent evaluation.

The majority of carriers offer an EPL audit (as we defined above), and most will provide the audit annually (or at least beyond the coverage inception year). Several that do not offer outside audits do offer the well-respected ELLA self-audit.

Audits can be conducted by a law firm, such as Baker & McKenzie, an HR consulting firm, or LCA, or by the insured. When an insured conducts their own audit, it is referred to as a self-audit in our tables.

Of the carriers offering audit services:

- Most are provided by law firms.
- A handful are true independent audits performed by HR consulting firms.
- The remainder are self-audits.

Audits can be very dangerous, in that problems uncovered in an audit can be used by a plaintiff's counsel in an attack on the insured's HR practices ("But Mr. Jones, your audit told you three years ago that your appeals process was inadequate!" says the plaintiff's lawyer). Thus, it is critical that audits be protected by attorney-client privilege. Surprisingly, seven of the carriers receive a copy of the audit results.

Reliance has a very good response to this potential problem, requiring the insured to pay for the audit, then providing an underwriting credit in an equal amount.

Are audits valuable? We think so, but are concerned that some insureds may be misled into thinking that a cursory audit is good enough, and not realize that a thorough audit is needed for proper protection. Such an audit needs to be performed by an external provider, preferably a law firm to protect discoverability, and should include on-site interviews. One carrier mentioned to us that only 1 percent of its insureds request the self-audit materials; presumably, even fewer use it.

Nevertheless, all of the audits listed have value, as long as the insured knows what they're getting.

Audit details:

This report includes additional details about the elements included in an audit.

Most include a review of documents such as: employment applications, offer letters and contracts. In addition, the performance evaluation process will be reviewed.

Several audits include on-site interviews, which are very valuable to detect problems that may not be apparent in a review limited to documents.

800# CONSULTATION SERVICES

This service provides the insured with a resource to call on for external EPL expertise. Typically, they are used when the insured is confronted with some HR problem, such as the termination of a difficult employee, and needs guidance as to how to proceed.

Initially, such services seemed somewhat superficial; how valuable can advice be from someone who you don't know (and who doesn't know you)? But upon reflection, these services can be very helpful, as long as their limitations are recognized.

The amount of time available annually is occasionally limited, but most carriers allow their insureds a reasonable

amount of access. Others offer additional time at a discount. For example, Gulf, Kemper (smaller employers only), Legion, London Special Risks, Monitor, NAS, National Union and Reliance all limit the time (or number of calls), which is reasonable. Others don't limit, but rely on the insured to be moderate.

Many small and mid-sized insureds do not have established relationships with employment law firms and tend to handle HR problems without adequate expertise. Although calling your own employment law attorney is preferable, for those employers without such services, calling the 800# is better than proceeding without any advice.

A problem with such services is that the person providing the consultation is perhaps not familiar with the caller's situation, jurisdiction or industry practices. The advice may often be technically correct, but missing more practical solutions. In sum, however, it is much better for employers to have an imperfect source of advice than to have no advice at all.

800# EMPLOYEE REPORTING LINES

Several carriers offer services that allow an insured's employees to anonymously report possible wrongdoing. The anonymity offers the reporting employee the comfort that they will not suffer retribution for their report.

The service is provided by a third party under contract to the carrier.

This can be a very effective way for employers to learn about possible transgressions, and the existence of the reporting line can help in the defense of a claim. From a carrier's standpoint, the reporting line is not only an added benefit to the insured, but also an early-warning signal that can help reduce the cost of a potential claim. eight carriers currently offer this service.

We will set aside for now a discussion about the downside of such anonymous reporting.

STATISTICAL INFORMATION AND ANALYSIS

Recognizing that workplace statistics are a useful tool in avoiding or defending workplace litigation, several carriers offer statistical information and analysis to their insureds. Many of these services are simply sources of information, but a few offer advanced, sophisticated analysis customized to their insureds.

Chubb Executive Risk, for example, offers its insureds access to labor economists and statisticians who are members of their provider network.

Particularly useful for larger employers, this can be a valuable service.

DEFENSE COUNSEL QUALIFICATIONS

In past years, we have been uncertain as to whether or not to include information about defense counsel as a value-added service. This year, we became convinced that the quality of defense panel members is a product differentiator for carriers that require the use of panel counsel, or for insureds who need referrals to counsel. We include information about counsel qualifications, the firms that are members of the panel, and whether the carrier will refer insureds to counsel when requested.

SAMPLE HANDBOOKS AND POLICIES

Almost all carriers offer sample employment-related documents, such as employment handbooks, policy statements and guidelines. These can be helpful, particularly for the smaller employer that has not written and maintained such documents.

These sample materials vary in quality. Some are standard materials available from associations, seminars and publications, but at least they have the benefit of being written by employment experts.

Some are available on paper only, but the more useful materials are available on disk and can be customized easily for the employer's own employment situation. These customizable documents make it easier for users to adapt the material for their own needs. This adaptation offers an additional advantage: the user is more involved in the process, thereby gaining important EPL knowledge.

How frequently materials are updated is critical. EPL continues its rapid evolution, and last year's handbook may well be out of date.

TRAINING AND EDUCATIONAL RESOURCES

Most carriers provide information to help insureds avoid EPL problems. These are in the form of:

- newsletters,
- seminars,
- websites,
- EPL manuals, or
- videos.

Newsletters are often prepared by EPL law firms, but sometimes by the carrier itself. Even carrier-prepared newsletters include contributions by outside experts.

Training seminars are offered by some carriers, typically regionally. A few offer seminars at the employer's site, but these are unusual, due to cost. Most seminars are conducted with the assistance of law firms.

A few carriers have developed EPL websites that are useful for disseminating information and training. We expect more, as the Web becomes a more valuable and cost effective medium for training. Certainly, several carriers have used the Web as a powerful tool to increase the quality of their risks and to attract new insureds.

ARE THESE SERVICES VALUABLE?

We have reviewed many EPL value-added services, and are impressed with the amount of time and effort involved in developing and maintaining them. It is a time-consuming and expensive proposition for carriers to develop a worthwhile set of EPL loss prevention tools.

Professionally, we believe in Risk Management, and loss prevention tools are an important part of the Risk Management process. Loss prevention services provided by insurance companies are an important part of Risk Management, and have proven their value. It is hard to imagine an effective Property, Boiler, or Workers Compensation program that did not include an integral loss prevention component.

However, EPL Risk Management is somewhat different, particularly for small to mid-sized insureds. These are the employers that can most benefit from EPL services, since they may be hard pressed to establish, implement and monitor strong EPL avoidance programs. A strong EPLI partner is valuable to these employers. Larger organizations are more likely to benefit from access to strong resources, since they should have the ability to implement their own programs.

HR is usually the control point, not Risk Management, so insurance relationships are not so ingrained in EPL. HR professionals are not as likely, in our experience, to look to insurance companies for services (at least outside of group insurance programs). Instead, they have existing relationships with law firms and HR consulting firms.

We wonder whether there is enough money in the premium to support quality services over time. During this period of EPL development, it is reasonable to invest heavily in services to attract new customers, but whether this can

continue on an ongoing basis is another question. Particularly for the low-cost carriers, services could become an unsustainable investment.

EPL services can be quite expensive, more so than property loss prevention, for example, because of the complexity of the risk and human involvement. Educating and training people to avoid EPL problems is a time-consuming effort, one that must be repeated continually. Property loss prevention also involves human behavior, but we suspect the retraining cycle is much longer.

Some of the cost can be justified by the reduction in claims, and of course, this is the best way for carriers to justify the cost of services. If services can be paid for by a reduction in future claims, everybody benefits. But services will have to be effective for carriers to continue to justify giving them away in hope of an improvement in losses.

There are really two types of services: those that help an insured reduce their exposure, and those that reduce the exposure for the insured.

The best type of service is one that helps the insured reduce losses by becoming a better risk, but for small and mid-sized organizations, we think the services need to be proactively involved in avoiding claims. An 800# is an example of a proactive service, providing the user with contemporaneous assistance at a time when it is most needed.

Audits are another proactive services taking an active role in identifying potential problems and providing a path to fixing them.

Handbooks are useful, but passive. They don't help unless they are used (although if an employer doesn't call an 800#, it is useless as well).

We are not optimistic about loss reduction potential from these services, unless insureds use them. Carriers will need to encourage insureds to use them frequently, which will drive up the cost perhaps, but will have a better result in reducing claims. The more they use the services, the more effective the value-added services will be.

Therefore, we like the carriers that have services with a heavy emphasis on delivery action, not just information.

So, are EPL services valuable? Undoubtedly, the answer is yes for smaller and mid-sized employers. HR professionals need all the resources they can get, and if those are included in the premium for an EPLI policy, all the better.

The answer for larger insureds is also yes. They gain access to quality EPL services—sometimes for free or at a discount—that support their efforts to avoid employment liability.

Such services can be a valuable adjunct to existing EPL risk-mitigation efforts, or a good foundation for new efforts. For these employers, careful selection of carriers is critical, the services possibly being even more important a differentiator than the policy itself.

Beware of carriers that have offered services just because they are needed to compete. If the service is shallow, it may be more of a distraction than a valuable tool to reduce EPL exposures.

And, as we said last year, there is no substitute for good EPL counsel from employment law and HR specialists.

Back issues available!

Call us toll free at

1-877-422-3366

- or -

on line at betterley.com

1999 Issues Available:

- *The Impact of ERISA Preemption Doctrine On Rising Health Care Costs (February 1999)*
- *Software Errors & Omissions Market Survey (April 1999)*
- *Intellectual Property Insurance Market Survey—1999 (June 1999)*
- *Employment Practices Liability Insurance Market Survey: (August/October 1999)*



BETTERLEY—SERVICES

Betterley Risk Consultants, Inc., is one of the oldest and most experienced Risk Management firms in the nation. P. D. Betterley, who founded its predecessor firm in 1932, was instrumental in pioneering the development of the Risk Management profession. We continue that pioneering spirit by bringing unmatched innovation and dedication to our clients. Our services are provided to organizations both large and small. We pledge to our clients not only the highest technical skill, but also a dedication to quality and performance second to none. Your inquiry is welcomed.

INDEPENDENCE • We are an independent firm, providing clients with a source of objective expertise unavailable from insurance brokerage firms or insurance companies. This assures our clients of advice free from potential bias, and allows us to recommend noninsurance solutions where appropriate. It also allows us to work with the client's existing professional service providers, if desired.

SPECIALISTS • As specialists in Risk Management consulting, we bring a focus to our work that others cannot. Our team dedicates 100 percent of its efforts to the understanding of client requirements, the development of appropriate solutions customized to a client's particular needs, and the timely installation of our recommendations. We supplement our expertise with that of others, such as actuaries and tax and legal advisors, when needed.

INNOVATION • Innovation is a hallmark of our practice. We use managed care strategies, risk financing alternatives such as captive insurance companies, and sophisticated Management Information Systems to help our clients control their Cost of Risk. Our clients have attained levels of operational effectiveness and cost-effectiveness unmatched by their peers.

SERVICES • *Some of our recent engagements include:*

- A Big Six accounting firm asked us to review their insurable operational exposures, as well as the adequacy and cost of coverage.
- We benchmarked the Risk Management performance of a leading regional bank.
- A group of private colleges asked us to examine the feasibility, and subsequently guide the creation, of a Workers Compensation Self-Insurance Group.
- We helped a leading international insurer identify and select an offshore management company.
- A mid-sized hospital asked us to develop and oversee a competitive bidding project, which reduced insurance costs by 27 percent.
- A Fortune 1000 technology firm uses our Risk Management expertise on an ongoing basis to supplement its treasury function.

BETTERLEY RISK CONSULTANTS, INC.
THIRTEEN LORING WAY • STERLING, MASSACHUSETTS 01564-2465
PHONE (978) 422-3366 • FAX (978) 422-3365
TOLL FREE (877) 422-3366
EMAIL RBETTERLEY@BETTERLEY.COM

The editor has attempted to ensure that the information in each issue is accurate. Opinions on insurance, financial, legal and regulatory matters are those of the editor and others; professional counsel should be consulted before any action or decision based on this matter is taken. Note: All product names referred to herein are the trademarks of their respective owners.

The Betterley Report is published six times yearly by Betterley Risk Consultants, Inc. This material is copyrighted, with all rights reserved. Additional copies are available.

Annual subscription: \$150.00US.
ISSN 1089-0513

Online Version: \$99.00US For additional information go to: www.betterley.com