



Independent Insurance Agents



Brokers of America, Inc.



Memorandum

TO: IIABA State National Directors
State Association Chairmen/Presidents
IIABA State Association Executives
IIABA Government Affairs Committee
IIABA Agents & Brokers Roundtable
IIABA Executive Committee

FROM: Debra Perkins

RE: Executive Summary of Zurich American Insurance Company's Regulatory Settlement Agreement and Attorneys General Settlement Agreement on Producer Compensation

DATE: March 22, 2006

Zurich American Insurance Company and its subsidiaries (Steadfast Insurance Company, Fidelity & Deposit Company of Maryland, Empire Fire & Marine Insurance Company, American Guarantee & Liability Insurance Company, Empire Indemnity Insurance Company, and Assurance Company of America) (collectively "Zurich") has entered into two agreements with certain state attorneys general and insurance commissioners relating to their investigations involving producer compensation and insurance placement practices. One agreement is between Zurich and the principal insurance regulator of each state that adopts it ("Regulatory Settlement") and the other agreement is with state attorneys general from California, Florida, Hawaii, Maryland, Massachusetts, Oregon, Pennsylvania, Texas, Virginia, and West Virginia ("AG Settlement"), which calls for the entry of an Order and Stipulated Injunction ("Order") in state court in the states agreeing to the AG Settlement. Many terms in the Regulatory Settlement and AG Settlement and Order (collectively "Settlement Documents") are identical and this memorandum includes an executive summary of the Settlement Documents as well as information on their impact on agents and brokers conducting business with Zurich.

BACKGROUND

Following and arising out of the investigations initiated by New York Attorney General Eliot Spitzer in 2004, other state attorneys general, and state insurance regulators, numerous civil investigations were instituted into certain practices of insurance carriers, including Zurich, concerning, among other things: i) the quotes and placements of new and renewed insurance policies; and ii) compensation provided to agents and brokers placing such policies. These investigations led to a number of federal and state court private party lawsuits brought on behalf

of insureds. The cases filed in federal courts were consolidated into a multi-district class action lawsuit ("Class Action") pending in New Jersey.

On October 14, 2005, Zurich and the plaintiffs in the Class Action agreed to a Memorandum of Understanding with respect to a potential settlement of the Class Action, subject to various contingencies. The settlement agreement based on the Memorandum of Understanding is being negotiated, and is conditioned on Zurich resolving the investigations that led to the Class Action, a number of which Zurich advised IIABA have now been resolved.

It should be noted that the AG Settlement and Regulatory Settlement, including the monetary payments, may be independent of any settlements Zurich may choose to enter into with any other state insurance regulators and/or state attorneys general that are not parties to those agreements. Zurich does not admit liability for any violations in the Settlement Documents.

The Settlement Documents are complex and include many terms and details that are not covered in this summary. All three documents are posted on www.independentagent.com on the Legal Advocacy page under IIABA/Industry Information & News in the section called Litigation (and Related Materials): Involving Zurich.

BUSINESS TERMS OF THE SETTLEMENT DOCUMENTS

1. **Implementation of Disclosures**

- a. Disclosure Statement - Starting 180 days from execution of the AG Settlement, Zurich must require agents and brokers it compensates for placing or renewing commercial insurance to provide each commercial insured with a Disclosure Statement (described below) **before** a commercial policy is bound.

The Disclosure Statement must be written and on the form in the Settlement Documents, (inserted at the end of this memo) advising the insured of the compensation that may be paid to the agent or broker for the placement or renewal of a commercial insurance policy, and must include:

- a. base compensation - the maximum percent of premium that will be paid as base compensation on each covered commercial insurance policy placed;
- b. contingent compensation - the maximum percentage of contingent compensation that could be paid to the agent or broker, the average percentage of contingent compensation paid by Zurich in the prior calendar year, and the factors Zurich will consider in determining the percentage of contingent compensation;
- c. other compensation – if any other compensation will be paid to the agent or broker, and if so, how it is determined (including anything of material value received by an agent of broker directly from Zurich, such as money; base compensation; contingent compensation; brokerage fee; service fee; incentive; rebate; money; credit; loan; forgiveness of debt; principal or interest; vacation, prize, gift or the payment of employee salaries or expenses, **but not including** de minimis fees or amounts

- collected by or paid to the agent or broker in amounts established by the state department of insurance for such fees or amounts);
- d. a Zurich website address where a disclosure will be posted; and
- e. other contact information, including a toll-free telephone number for an insured to get additional information.

The Settlement Documents include a mechanism for Zurich to petition for modification of the Disclosure Statement in the event that Zurich suffers a market reduction resulting from compliance with the disclosure requirements.

The Disclosure Statement will not be required of Zurich captive agents (defined as representatives obligated to submit specified business only to Zurich or to give Zurich a right of first refusal on the placement of commercial policies) if they disclose to the insured that the producer will receive compensation (including base, contingent, and any other form of compensation) for the placement of the policy or services rendered. The Settlement Documents do not specify any requirements for the form of such a disclosure.

- b. Website Disclosure – Zurich must post on its website a disclosure covering:
 - i) the range of and average amount of base compensation it paid in the prior calendar year for the types of commercial policies covered by the Disclosure Statement and the factors determining the base compensation;
 - ii) the range of and average amount of contingent compensation it paid in the prior calendar year for the types of commercial policies covered by the Disclosure Statement and the factors determining the contingent compensation, including if it is calculated by policies (number of policies or dollar value of premium), growth (number of policies or dollar value of premium), rate of retention or renewal of in-force policies, amount of business achieving specific loss ratios or other measures of profitability, or anything of material value it provided to an agent or broker.

2. **Implementation of Business Reforms**

Zurich is required to implement business reforms, in addition to the Disclosure Statement, as follows:

- a. Compliance Program - Within 30 days after entry of the Order in the applicable state court, Zurich must have in place a United States Compliance Office, which will have responsibility for all compliance and regulatory matters relating to the Settlement Documents. The duties of the Compliance Office will include maintaining a training program focused on compliance with laws and regulations (such as antitrust laws, state insurance laws and regulations, unfair insurance practices, fiduciary duties of agents and brokers, and the duty not to engage in deceptive/fraudulent conduct), timely internal reporting of findings and recommendations relating to compliance, investigation of alleged misconduct and appropriate disciplinary action when warranted, adhering to a records retention policy for commercial lines quotes that are

provided but not bound, obtaining certification from officers and directors of their agreement to comply with the Order, and various reporting requirements to the appropriate state attorney general and insurance regulator, including for violations of the Order and to demonstrate compliance with the Settlement Documents.

- b. Prohibited Conduct - Zurich cannot:
 - i) knowingly provide any false bids, quotes or indications to agents or brokers, or any other quote that is not based on “bona fide business, actuarial or underwriting considerations;”
 - ii) allocate customers or markets, rig bids or quotes, or fix or stabilize prices; or
 - iii) compensate any agent or broker to include Zurich on a list of companies to quote or enter into any “pay-to-play” arrangements.

3. **Restitution**

Under the Settlement Documents, Zurich must pay:

- a. \$100,000,000 to the Settlement Class Members, plus \$51,700,000, to be distributed according to a Plan of Allocation (which is to be drafted by plaintiffs’ counsel in the Class Action, in consultation with regulators);
- b. \$100,000 to cover the costs of notice to the Settlement Class Members; and
- c. \$20,000,000 to the state attorneys general that are parties to the Settlement Documents.

There are a variety of conditions and terms associated with these payments, including settlement credits for certain payments made under separate settlement agreements to states that are not parties to the Settlement Documents.

4. **Cooperation with Attorneys General and Insurance Regulators**

Zurich must continue its cooperation with investigations and actions regarding any person or entity (including former employees), including voluntarily producing or providing access to documents and information.

5. **Releases for Zurich**

Upon execution of the Settlement Documents, the existing investigations, claims and proceedings relative to quotes and placements of new and renewed insurance policies, compensation provided to agents and brokers placing such policies, and the allegations in the Class Action by participating insurance regulators and state attorneys general as to Zurich and its current and former officers, directors, and employees will be terminated (except for former officers or employees of Zurich’s business unit known as Marsh & McLennan Global Broking Unit who are no longer officers or employees of Zurich), and no investigations, claims or proceedings will be made or reinstated as to these same matters.

IMPLICATIONS FOR AGENTS & BROKERS

The Settlement Documents between Zurich and the state attorneys general and Zurich and the insurance regulators for the participating states do not just affect Zurich --- they also impact agents and brokers doing business with Zurich. Although an agreement, including a settlement agreement, typically obligates only the parties to the agreement to comply with its terms, the Settlement Documents are structured to create new disclosure requirements on agents and brokers that are distinct from the requirements of applicable statutes or regulations, if any. That is accomplished by the provisions that call for Zurich to require agents and brokers placing or renewing covered commercial insurance policies to provide the insured with a Disclosure Statement before the policy is bound.

Zurich has 180 days from execution of the AG Settlement to implement the use of the Disclosure Statement. IIABA has been advised by Zurich that it will require all agents and brokers in all states placing or renewing covered commercial insurance policies with the company to use the Disclosure Statement, including in the states where the attorney general and/or insurance regulator has not executed the Settlement Documents.

Agents and brokers doing business with Zurich should have received some communications already from the company regarding changes in its business practices and the Settlement Documents, and the company has indicated it will keep agents and brokers informed as the implementation process moves forward.

As to the Regulatory Settlement, it should be noted that state insurance regulators played an integral role in developing the business reforms and disclosure obligations included in the Regulatory Settlement. The NAIC Broker Activities Task Force Chairman, Michael T. McRaith, (Director of the Illinois Division of Insurance), stated that the Regulatory Agreement “prioritizes consumer protection with sensible business reforms.” The NAIC press release on the Regulatory Settlement also notes that, “While the decision of whether to join the settlement is subject to the individual review and analysis of each state regulator, the NAIC Task Force supports the settlement as a sound regulatory framework with unprecedented consumer protection benefits.”

IIABA will update you as we learn of any significant developments regarding this matter.

Note: The **Zurich Agent/Broker Compensation Policy** is on the next page.

Zurich Agent/Broker Compensation Policy

Most insurance companies providing commercial coverage in the United States distribute their insurance products through the independent agency and brokerage system. Your agent or broker is an independent businessperson or team of people not employed by Zurich or any other insurance company.

Most agents and brokers choose to be compensated for their services through the insurance companies with whom they place the insurance that they sell to their customers.

Base Commission

Zurich will pay your agent or broker a commission. Zurich establishes its base commission on several factors including the type of insurance policy, the size of the insurance policy, and individual policy underwriting considerations. Each insurance policy has a standard commission which is the most that Zurich will pay. The standard commission for the types of policies Zurich is quoting is:

Policy 1 _____%	Policy 3 _____%
Policy 2 _____%	Policy 4 _____%

If you have chosen to compensate your agent or broker directly or you have not consented to your agent or broker taking a commission, you should speak directly to your agent or broker.

Contingent Compensation

[May be deleted if no agreement with broker to pay contingent commissions]

Zurich may also pay contingent compensation to your agent or broker. Zurich does not pay contingent compensation to all of its agents and brokers, and some agents and brokers choose not to accept contingent compensation from insurance companies. Contingent compensation is paid in addition to the base commission. Contingent compensation is not calculated until the end of the year. The amount will be a percentage of premiums based on several factors that determine how profitable your agent's or broker's insurance is for Zurich including [to be modified if factors changed]:

1. The total premium written for all eligible business in a year
 - Zurich pays a percentage of the eligible premiums in addition to the "Base Commission."
2. Achievement of targeted premium levels
 - Zurich sets reasonable targets of premiums that will be placed with Zurich by your agent or broker each year. If that target is reached, then your agent or broker is paid an additional amount on the eligible premiums.

3. The profitability of the business

- For each agent and broker, Zurich calculates the ratio of the total value of the claims over the premiums. The resulting ratio generates a payment. Lower ratios generate higher payments because lower ratios mean that the result is more profitable to Zurich. We do not disclose the actual ratio and payment percentages.

4. Preferred business considerations

- We have unique agreements with some agents and brokers to place particular types of business with us. These agreements may result in the payment of additional commission for such policies.

The maximum percentage for contingent compensation is 6.75%. The average paid in 2005 was ____%.

Visit Zurich's Web Site

For a more complete explanation of the nature of compensation Zurich pays to agents/brokers—including specific information on the maximum, average and actual ranges of commission paid by Zurich on the specific types of policies we are currently quoting for your company, please go to www.zurichna.com/yourcompany. This web site includes a full explanation of the formula for developing contingent compensation if your agent or broker is eligible for contingent compensation from Zurich. Alternatively, you may call 1-800-xxx-xxxx to obtain the information.