

# The Gordon Gazette

Insurance news you can use... for the customers of

**Andrew G. Gordon, Inc.**

**Insurance**



Fall, 2006

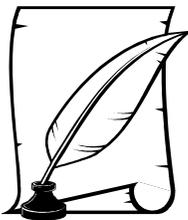
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## From the owners desk...

Most people who have property on Cape Cod, or live within a mile of the shore, are buying insurance through the State's "FAIR Plan". The enclosed article from Banker & Tradesman explains why this state agency is the fastest growing "company" in the state, and what is driving the price of coastal insurance. Further increases in FAIR Plan rates will relieve some of the pressure on private companies, and rising prices may bring new options back to the coast. With the continued high cost of reinsurance, however, coastal insurance will stay expensive, and wind deductibles will remain common throughout the South Shore. Our chart on page 3 helps define "coastal" and shows where companies' capacity and appetites fall today.

There's better news on auto insurance. Several factors are contributing to lower costs going forward. The primary trends: safer cars, less tolerance for drinking and driving, and more recently, high gas prices.

Accident frequency has trended down faster than upward push driven by more expensive cars and increasing medical costs. The net effect has been and will continue to be lower auto insurance premiums. We expect auto insurance costs to drop another 8% - 10% next April when rates change (no longer on January 1 as in the past).

One wild card in the auto insurance arena is regulatory. Last year Insurance Commissioner Julianne Bowler proposed an "Assigned Risk Plan" (ARP), to replace the existing system of loss cost sharing. Her proposal was in court for nearly a year, but recently the Massachusetts Supreme Judicial Court affirmed her authority to install an ARP. So we expect a new plan shortly. An assigned risk program is the first step to national style auto insurance. Thus, companies that shun Massachusetts today may come here when they can earn a better return than under today's system. We will update you as details emerge.

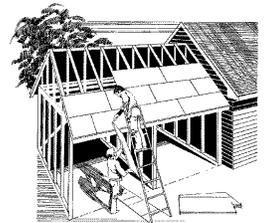
If you're happy with our service, tell a friend; if not, please tell me.

*Geoffrey Gordon, CFP®, CIC, CRM*

## The Cost to Rebuild 2nd of our 4-part series

One of the most important first steps to assessing your insurance needs is estimating the cost to rebuild your property when the unexpected disaster happens. We always think in terms of deductibles, as the measure of how much we monetary value we retain personally. Less attention is given to the amount we retain after the insurance runs out! That's a mistake.

Liability limits are always hard to determine; a really bad car accident can result in multi-million dollar damages, where even a \$1,000,000 umbrella might not be enough. Property insurance is easier. Homes, vehicles and



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## Commercial Corner: Controlling the Cost of Risk

Many insurance decisions are driven by the cost of insurance, when in fact they should be driven by the cost of risk.

The process for determining and controlling risk is actually pretty straightforward. The devil is in the details.

The first step is to identifying the kinds of things that can go wrong, prioritizing by critical business functions first. The next logical step is to see how to reduce the cost of these potential “uh-ohs”.



Once identified, consider risk control. Using safety glasses when operating machinery, placing signs clearly marking wet or slippery

floors, and installing sprinkler systems are all good examples of risk control.

The next step is deciding which risks we transfer. Risk transfer can often be accomplished with contracts, such as a lease in which a landlord requires the tenant to name the landlord as an additional insured on the tenant’s insurance. Or when a general contractor requires subcontractors to have insurance limits equal to his. Another is when you require a shipper of your product to provide insurance while it is on its way to the customer.

Many risks we don’t want to retain can’t be transferred to others for free. They’re our responsibility that arise strictly from what we do or what we sell. Here’s where insurance comes in to play.

When buying insurance, insure only what you can’t afford to lose. High deductibles usually make sense. On the other hand, “Don’t risk a lot for a little”. Flood insurance is a good example here. If you’re not in a flood zone, flood insurance is inexpensive. If you are, it’s more expensive, but federal subsidies in the pricing still make it a bargain. And finally coming full circle, don’t let insurance be a substitute for sound risk control. Insurance doesn’t make an unsafe work site safe.

## Rebuild cost—for your home

*(Continued from page 1)*

belongings have a definable limit to that value, which we use to arrive at coverage amounts.

Our office uses specialized software which can map your home (distance to the ocean), draw replacement cost estimates using public records (assessors office and tax records), and then lets us add miscellaneous information that you provide.

Because few insurance companies still offer “guaranteed” replacement value (where they would pay an unlimited amount, even over your insurance limit, to replace your house), the burden has shifted to all of us to get this right.



Pressure on building supplies from last year’s hurricanes in Florida and the Gulf has kept rebuilding costs up, in spite of softening market values. So, we systematically review your home’s replacement cost adequacy, and advise you whenever we think you should make adjustments. However, we still rely on you to assist us by providing up to date information, particularly additions or upgrades.

Remember, if you decide to add on, call us before construction begins. If you’re not sure your home insurance amount could leave you with a big enough check to rebuild your house, we can recalculate the cost for you in minutes.

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## “Rebuild” Cost for Autos

New autos can pose a problem with rebuilding (or replacing altogether) under some circumstances, but there are solutions.

Typically this isn’t a problem with a brand new car: most companies estimate value based on the price you paid minus mileage, rather than by the depreciated or resell value, a poor approach for consumers.



But if you roll a loan from one used car to another, it’s possible to owe more than the car is actually worth. For that there’s “gap insurance”, and we offer that here. We can offer you this protection for about half what auto dealers charge, so if you are thinking you may buy this coverage from a dealer, check with us first.

## Overheard in Hamilton Bermuda, ...and Why does that affect me?

Reinsurance is the insurance that insurance companies buy when they need deeper pockets to pay all claims when “the big one” hits. Many international reinsurance companies operate in Bermuda because of its attractive tax structure for these financial goliaths.

Many homeowners engage in various levels of deniability when assessing insurance needs:

1. it won't happen to me,
2. if it does, it won't be that bad
3. if it is, the government will bail me out.

The first denial has the most basis in reality. Forget two and three, because it's only when it's that bad do you really need insurance; and government bail-outs are not hand-outs; they're usually just loans. You're still out, and still owe, the money.

Insurance companies can't use the “it won't happen to me” myth at all, because when a big storm hits, probability and the principle that makes insurance companies viable, “spread of risk”, comes home to roost. Spread of risk refers to the ability to collect premiums over broad geographical regions to pay big claims in a particular region.

Companies monitor their spread of risk carefully as it is the basis for their cost structure.

As weather models become more sophisticated however, the spread of risk for weather related claims (unlike fires, and other randomly placed disasters) has become much more concentrated on the coast. Reinsurers in particular, with a spread of risk from Galveston, Texas to Portland, Maine know they'll take plenty of hits within five to ten miles from the coast. It is this reality that is driving the cost and availability of coastal homeowners insurance. It is also driving the growth of wind deductibles (see our spring article about these).



Even this year's mild hurricane season, the cost of reinsurance is not going down. Jamie Veghte, head of reinsurance for Bermuda insurer XL Capital, remarked at a Fox-Pitt Kelton insurance conference in September, "There is absolutely no room for softening cat (*catastrophe*) prices ... even if we don't have a puff of wind." "Rates need to rise 10 to 15 percent." If pricing on business prospects is inadequate to cover possible claims, Veghte says XL will walk away.

### For a snapshot of the coastal market today, here's what our companies are doing...

| <u>Company:</u>            | <u>Insurance value sweet spot - most competitive</u> | <u>less than 1/2 mile</u>  | <u>1/2 mile - 1 mile</u> | <u>1-3 miles</u>                             | <u>3-5 miles</u>        | <u>&gt;5 miles</u> |
|----------------------------|--|--|--------------------------|--|-------------------------|--------------------|
| <b>AIG</b>                 | 1,000,000 +  | will entertain including no wind deductibles                       |                          |  |                         |                    |
| <b>Bunker Hill</b>         | 250K - 700K  | no   | 2% named storm           |  | 1% named storm          | regular            |
| <b>Cambridge Mutual</b>    | 350K - 900K  | no   | no                       | no new                                       | 1% named storm          | regular            |
| <b>Chubb</b>               | 900,000+   | will entertain including no wind deductibles                       |                          |  |                         |                    |
| <b>Commerce</b>            | 200K - 500K  | no   | no                       | will entertain including no wind deductibles |                         |                    |
| <b>Encompas</b>            | 750K - 1.5mm   | no   | no                       | 1% named storm                               |                         | regular            |
| <b>Hingham Mutual</b>      | 150K - 500K  | no   | no                       | 1-3% named storm                             |                         | regular            |
| <b>Merrimack Mutual</b>    | 350K - 900K  | no   | no                       | no new                                       | 1% named storm          | regular            |
| <b>One Beacon</b>          | 250K - 1mm   | >2000' OK  | no wind deductibles      |  |                         |                    |
| <b>Travelers / Premier</b> | 500K - 2mm   | no   | no                       | no   | 1% - 5% wind deductible |                    |
| <b>FAIR Plan</b>           | 50K - 1,000,000                                      | state's market of last resort: 1% - 5% wind deductibles, depending |                          |  |                         |                    |



# LIFE & FINANCIAL NEWS

## Life insurance rates continue to fall...

On average, premiums will drop by four percent in 2007, according to the Insurance Information Institute (I.I.I.).

“This continues a generally downward trend in life insurance premiums, which began several decades ago,” according to I.I.I. economist and life insurance spokesperson Dr. Steven Weisbart. “The four percent drop projected for 2007 is in line with the average five percent per year drop beginning in 2000,” added Dr. Weisbart. “The result is that, in 2006, premiums are less than half of what they were over a decade ago.”

“Life insurance rates are dropping because

death rates for the 25-44 age group — the primary age range for purchasing life insurance—have decreased significantly over the past 10 years,” Dr. Weisbart added.

In 1996 the death rate per 100,000 for the 25-44 age group was 177.8; by 2004 it had dropped to 161.8 (preliminary data, National Vital Statistics Reports). That is nearly a 10 percent drop in the death rate in less than a decade for the prime insurance-buying ages.

If you haven't reviewed your life insurance costs lately, call us or get a quote on-line at [www.agordon.com](http://www.agordon.com).

## While health insurance costs continue to rise...

Advances in drug treatment and new medical procedures continues to drive health insurance costs higher, much faster than general inflation rates.

Group insurance renewals are running mid to high teens (that is, renewals are 15% - 19% higher than last year's rates). Companies are coping by increasing in-office co-pays, higher hospital deductibles, and higher employee contributions.

Health Savings Accounts (HSAs) are another approach. These plans combine high



deductible health plans with a tax-free savings feature to fund items that fall under the “deductible”. These plans got a big boost last year with legislation that simplified them and enhanced the tax benefits.

Because they bring the consumer (patients) closer to their providers, renewals for these plans are running lower as well.

There are many options in medical insurance for Massachusetts small businesses. Contact us to explore your options.

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