National Association of Chemical Distributors Annual Meeting

Paradise Island, Nassau, Bahamas
Wednesday, May 6, 2009

Agenda and Presenters

➢ *Welcome from the Moderator*	Larry J. Knight, ARM Aaxia Chemical Ins. Services
➢ *Crime*	Brian O'Neill AIU Holdings
➢ *Employment Practices Liability*	Johnny Prewitt J.R. Prewitt & Associates
➢ *Directors & Officers Liability*	Dave Mathews, CPCU, ARM Pritchard & Jerden, Inc.

Fraud

Presenter:

Brian O'Neill
AIU Holdings

Fraud in the Workplace

What is Fraud?

- Fraud is the use of one's occupation or position within the company to:
  - Steal company money, property, or assets for personal use
  - Improperly receive kickbacks or bribes from suppliers, vendors or customers

Surprising Statistics

- Did you know?
  - Fraud and abuse costs American companies up to 7% of company revenues
  - Translates to approximately $900 billion in fraud losses when applied to the US Gross Domestic Product (GDP)
  - In 2007, FBI investigation resulted in 183 indictments and 173 convictions of corporate criminals
  - Corporate fraud cases increased by 47% from 2003 to 2007

Motivators for Fraud

- Motivators:
  - Financial Incentive, Rationalization, Entitlement, Addiction
- Contributing Factors
  - Insufficient controls (34%)
  - Low level of commitment to the firm (34%)
  - Relative anonymity (17%)
  - Lack of clarity about the company's ethics (14%)
- Commingling of Responsibilities:
  - **C** (Custody)
  - **A** (Authority)
  - **R** (Recording)
  - **R** (Reconciliation)

Crime Does Pay

- Crime Trends
  - As the economy worsens, crime increases
  - Increase in fraud schemes over the last year
  - Claims are rising

Emerging Business Threats

- Majority of major losses arise from:

1. Vendor related fraud
2. Senior executive fraud
3. Fraud in foreign locations
4. Robbery
5. Theft of precious metals

Emerging Business Threats: #1 – Vendor Fraud

- **Former Executive Embezzles Approximately $66 Million Over a Three-Year Timeframe**
  - Executive conducted sale transactions
  - Eliminated sales people
  - Engaged with vendors directly

Emerging Business Threats: #2 – Senior Executive Fraud

- **CFO Embezzles $10.86 Million for Lavish Lifestyle**
  - Extravagant home purchase
  - First class air travel around the world
  - Jewelry purchases
  - $300,000 monthly transfers
  - His mother turned him into the authorities
  - Sentenced to 14 years in prison

Emerging Business Threats: #2 – Senior Executive Fraud

- **Accountant Steals $6.9 Million Over 6 Years**
  - Theft discovered by bookkeeper
  - Sentenced to 4 years, 7 months in prison

Emerging Business Threats: #3 – Fraud in Foreign Locations

- **Former Executive Embezzles Approximately $66 Million Over a Three-Year Timeframe**
  - Involved with theft scheme with 30 customers
  - Goods were purchased for export
  - Received kickbacks for involvement
  - Made claim for sales tax that was not paid
  - Loss claimed was approximately $34 million

Emerging Business Threats: #4 – Robbery

- **Armed Robber Forces Staff to Surrender Diamonds Worth $108 Million**
  - Robbers entered shortly before closing
  - Absconded with jewels on display

Emerging Business Threats: #5 – Theft of Precious Metals

- **Alloy Theft Amounts to Approximately $2 Million in South Africa**
  - 12-month time period
  - #2 Senior executive at manufacturing facility
  - Suspected of murdering his boss
  - Faked his own kidnapping

Disclosures

- The data contained in this presentation is for general informational purposes only. The advice of a professional insurance broker and counsel should always be obtained before purchasing any insurance product or service. The information contained herein has been compiled from sources believed to be reliable. No warranty, guarantee, or representation, either expressed or implied, is made as to the correctness or sufficiency of any representation contained herein.
- The claim scenarios summarized herein are offered only as examples. Coverage depends on the actual facts of each case and the terms, conditions and exclusions of each individual policy. Anyone interested in the above product(s) should request a copy of the policy itself for a description of the scope and limitations of coverage. Policy terms may vary based on individual state requirements and may not be available in all jurisdictions.

Exposures for EPL
- Who Needs It!

Presenter:

Johnny Prewitt

J.R. Prewitt & Associates

Job Bias Charges Rise 9% in 2007, EEOC Reports

Basis of Charge Filing	FY 2007	FY 2006	Percentage Increase/Historical Comparison
RACE	30,510	27,238	Up 12% to highest level since FY 1994
RETALIATION	26,663	22,555	Up 18% to record high level, double since FY 1992
SEX/GENDER	24,826	23,247	Up 7% to highest level since FY 2002
AGE	19,103	16,548	Up 15%, largest annual increase since FY 2002
DISABILITY	17,734	15,575	Up 14% to highest level since FY 1998
NATIONAL ORIGIN	9,369	8,327	Up 12%, above 9,000 for second time ever
RELIGION	2,880	2,541	Up 13% to record high level, double since FY 1992
TOTAL CHARGES	**82,792**	**75,768**	**Up 9%, largest annual increase since FY 1993**

EPL: More laws than ever before

A few of the Federal Employment Discrimination Statutes enacted recently:

- Title VII of the Civil Rights Act of 1964
- Civil Rights Act of 1991 (amends Title VII above)
- Americans with Disabilities Act (ADA)

Title VII of the Civil Rights Act of 1964

- The statute makes it unlawful for an employer to "fail or refuse to hire or discharge any individual, or otherwise to discriminate against any individual with respect to his/her compensation, terms, conditions or privileges of employment" because of race, color, religion, sex, including sexual harassment, national origin, and pregnancy childbirth, or related medical conditions.
- Applies to employers with 15 or more employees (state laws may differ)

Civil Rights Act of 1991 (amends Title VII)

- Provides compensatory and punitive damages from private employers
- Provides the right to a jury trial

Americans with Disabilities Act (ADA)

- The ADA prohibits discrimination on the basis of disability against a qualified employee, defined as an individual who, with or without reasonable accommodation, can perform the essential functions of the employment position for which the individual holds or desires.
- Litigation continues to define “disability”. Even successful organizations can incur significant defense costs over a long period of time litigating if “high blood pressure” is a covered disability.
- The ADA covers employers with 15 or more employees.

Employment Practice Liability

- Factors that will fuel continued increases in litigation:
  - High profile, high pay out awards
  - Ambiguously worded employment laws (i.e. disputes over what constitutes a “disability” or a “reasonable accommodation”)
  - The number of employees that may qualify for a legally protected class
  - The backlog of EEOC complaints

Employment Practice Liability

- Factors that will fuel continued increases in litigation - *continued*:
  - State and city governments have enacted their own employment-related laws
  - Various state laws can circumvent federal punitive damages caps
  - Lucrative class action settlements

Why a client should consider EPL coverage:

- Economic recession climate results in corporate decisions to:
  - Reduce costs via reduced number of employees
  - Close plants / divest operations
  - Sell entity or merge with other firm
- Weakened financial position from economic recession climate cannot withstand the impact from frivolous or non-frivolous EPL litigation and/or indemnification

EPL Exclusions to “watch out” for

- Intentional (vs. “purposeful”) acts
- Merger or downsizing
- Retroactive date (prior acts exclusion)
- Breach of express contracts
- No retaliation carve out to Workers’ Compensation
- No severability of exclusions or applications
- Prior and pending litigation (including dismissed EEOC charges with right to sue)

Directors & Officers Liability Insurance

Presenter:

Dave Mathews, CPCU, ARM
Senior Vice President – Pritchard & Jerden, Inc.

Directors & Officers Insurance

Why are directors and officers at risk?

- Directors and officers (including their spouses and estates) can be personally liable for alleged breach of duties while acting in their capacity.

Directors & Officers Policy Insuring Agreement

- Generally, protects Directors & Officers for their **personal liability** arising out of business decisions or "Wrongful Acts"…
- ***"Wrongful Acts"*** defined as "any error, misstatement, misleading statement, act, omission, neglect, or breach of duty committed, attempted, or allegedly committed by an insured person…"

Typical Gaps in Traditional Coverage

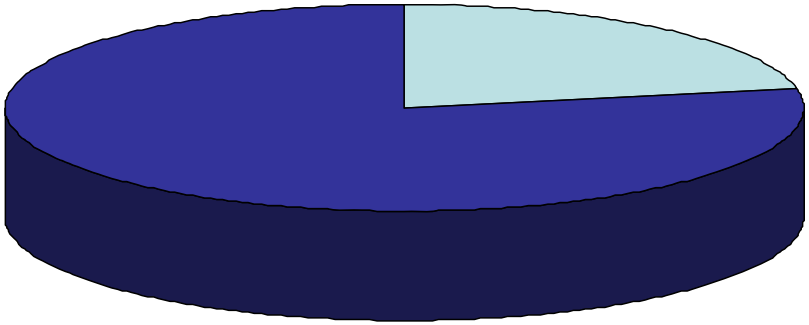
- D&O Liability insurance can fill coverage gaps such as:
  - A General Liability (GL) policy may:
    - Insure directors & officers against liability for bodily injury, property damage, personal injury and advertising injury
    - Exclude coverage for the financial consequences for alleged wrongdoings typically
  - Umbrella policy contains the same coverage as the underlying GL policy

The D&O policy may address the following claims:

- Mismanagement of the business and operations
- Competitor suits involving unfair trade, anti-trust, or intellectual property infringement
- Misrepresentation in connection with private placements of stock or debt or in the sale of part or all of the business
- Regulatory actions brought by the government such as FTC, FDA or the IRS
- Wrongful interference with a contract
- Failure to deliver services
- Self-dealing and conflicts of interest

Are private company executives underestimating their D&O liability risk?

- Not unlike public companies, private companies and their directors and officers are vulnerable to lawsuits.

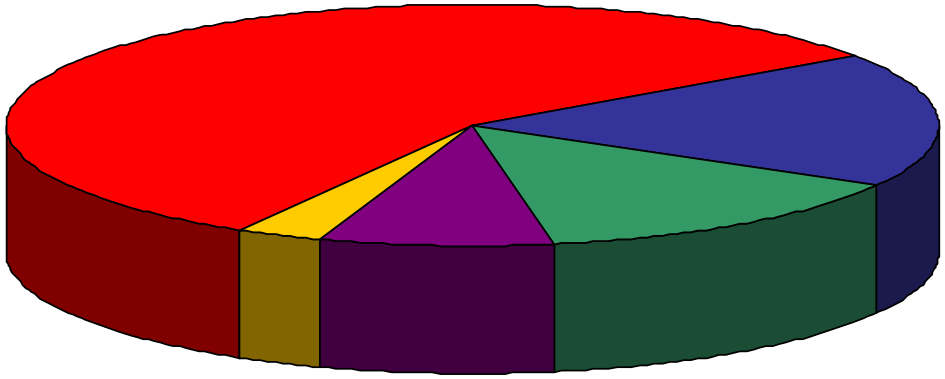


1 in 5 companies (22%) experienced a D&O liability lawsuit in the past 5 years*

**** Based on Chubb 2007 Private Company Survey.***

Who is suing?

- Customers are more likely to sue private companies and their directors and officers than are all other groups combined*



57% Customer

18% Gov't/regulatory agency

14% Vendor

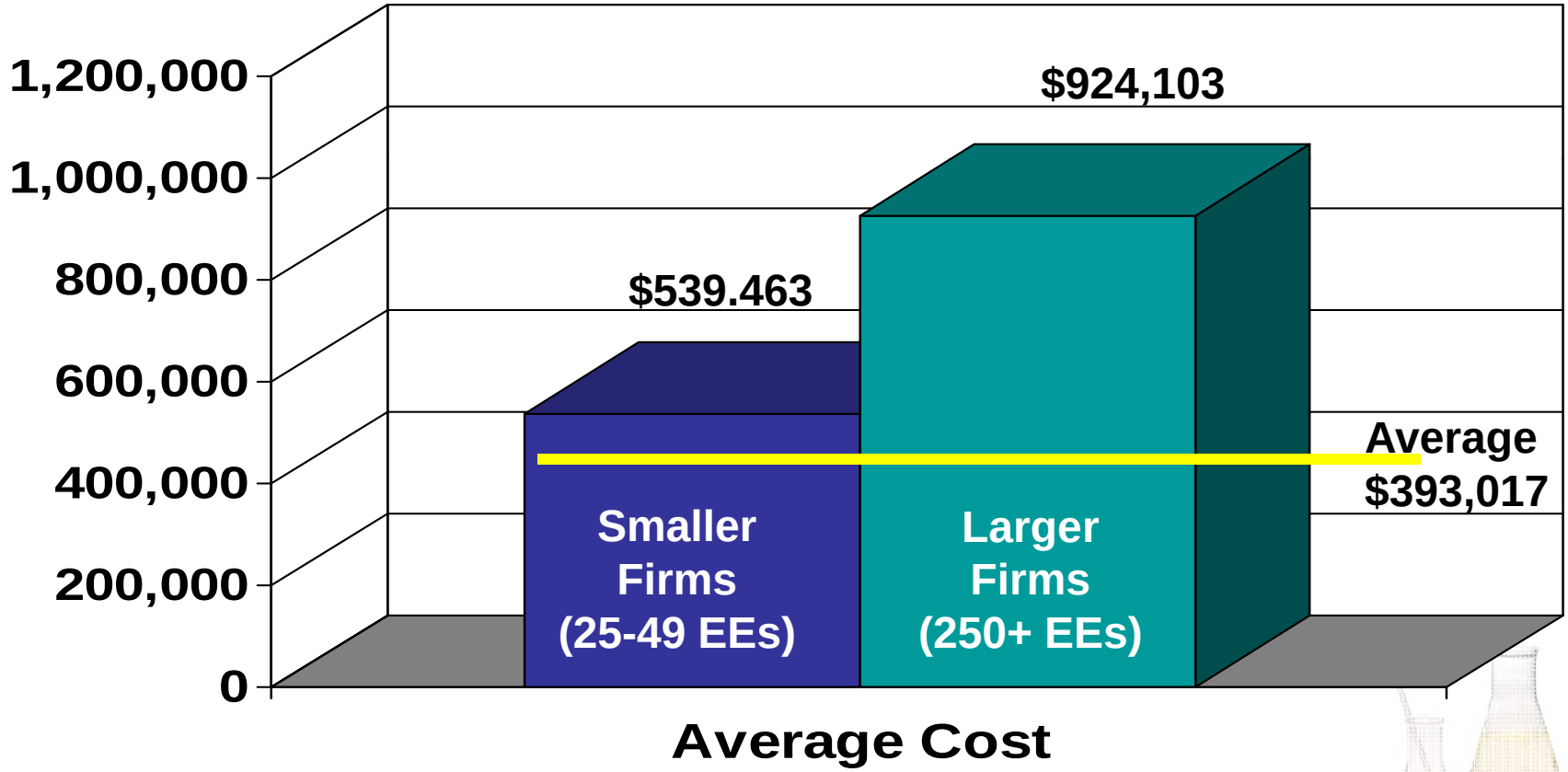
8% Competitor

3% Partner/ shareholder

**** Based on Chubb 2007 Private Company Survey.***

How costly can a D&O lawsuit be?

- The average loss (settlement, judgment, and legal costs) was: **$393,017***



** Based on Chubb 2007 Private Company Survey.*

Reasons for D&O insurance

- Quality directors will not serve without D&O coverage
- The personal assets of directors and officers are at risk
- The cost of defending a corporate lawsuit can be high
- Judgments can be financially crippling
- Corporate indemnification may not be available for certain types of claims (i.e. shareholder derivative actions)
- Directors & Officers insurance is not expensive and protects the corporate assets that may be required to indemnify the directors and officers

Purchasing Directors & Officers Insurance

- D&O insurance can be purchased
  - as a “stand-alone” policy with a specific limit, or
  - In conjunction with other policies including Employment Practices Liability, Fiduciary Liability, Kidnap & Ransom, Crime coverage. The limits of insurance can be shared by multiple coverage parts or separate limits.

Conclusion

- Thank you for your time.
- Questions???