How to navigate a complex market

A U.S. insurance buyer's guide
for Canadian companies

TRAVELERS

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A U.S. insurance buyer's guide for Canadian companies

Making sure that your U.S. operations are covered requires in-depth knowledge of the U.S. market and its idiosyncrasies. In this white paper, we look at the top four risks that Canadian companies face when buying insurance in the U.S. – and how to overcome them.

Global opportunities, global risks

A large number of Canadian companies export products to or set up operations in the U.S. Gaining a cross-border footprint brings complexity. Whether companies have operated in the U.S. for decades or are making their first foray into the U.S. market, they must ensure that they comply with evolving insurance and tax regulations, while protecting their balance sheets from potential U.S. exposures.

Many companies assume that the practices and procedures they are familiar with in Canada are the same worldwide. However, that is not the case, so companies need to understand the nuances of the U.S. market and how to cover their operations effectively.

Without the right coverage, an event such as an earthquake or a class-action lawsuit could have a catastrophic impact on profits and shareholder value – or even put you out of business.

Reputation is also a crucial consideration. We find that midsized to large Canadian companies are increasingly concerned with protecting their reputations abroad. A top priority for many of our clients is being able to tell their boards that they have effectively managed their U.S. risks, while being viewed as good corporate citizens.

We hope that you find this report useful and would be interested in your feedback.

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A litigious society

"A Florida jury awarded US$23.6 billion in punitive damages from R.J. Reynolds Tobacco to the widow of a smoker who died of lung cancer."

The U.S. has a reputation for being a litigious society and we are used to reading about big settlements for sometimes frivolous-sounding lawsuits, such as the McDonald's case in which a jury awarded US$2.86 million to a customer after she spilled scalding coffee on herself (later reduced to US$640,000).[1]

Individuals in the U.S. have greater access to courts, mainly because claimants virtually never have to pay a defending company's costs or fees if the claimant sues the company and loses, which leads to more cases being brought.

The fact that so many cases in the U.S. are held before juries also tends to lead to high awards. In one recent example, a Missouri jury awarded US$72 million to the family of a woman who died of cancer, found by the court to have been caused by Johnson & Johnson talcum powder.[2]

In some states, juries tend to be sympathetic to claimants, particularly when they are up against huge corporations in David vs. Goliath-type scenarios.

Several costly factors

Several factors push up the already high costs of lawsuits in the U.S. For example, for any claims involving injuries, the lack of free healthcare leads to significantly higher settlements or judgments, which typically reflect both past and future medical costs. This is a big issue in the U.S. In the 2015 Travelers Business Risk Index, we found that medical cost inflation ranked as the biggest concern (60%) for U.S. businesses.

However, punitive damages are the most daunting issue for businesses and are more common in the U.S. Punitive damages are frequently available in cases where the defendant has knowingly caused harm and are often much higher than the original award. In the Johnson & Johnson case mentioned previously, US$10 million of the award was actual damages, while the remaining US$62 million was punitive.[3]

Potential punitive damages are normally a multiple of the compensatory damages; however, exceptions exist and can total up to an extremely high number. In 2014, a Florida jury awarded US$23.6 billion in punitive damages from R.J. Reynolds Tobacco[4] to the widow of a smoker who died of lung cancer.

Risk one

Companies operating in the U.S. need to be mindful of the litigious environment when assessing their exposures there.

Large payouts are not uncommon and companies' duties to their customers can be unclear, presenting significant challenges.

60%

of U.S. companies found that medical cost inflation was their biggest concern.

50

U.S. states – each is a separate legal jurisdiction with its own courts and its own laws.

The geographic influence

Canadian companies should understand that the U.S. is made up of 50 states – each is a separate legal jurisdiction with its own courts and its own laws, in addition to federal laws and courts. Companies also need to know the effects this has on litigation. Each state's demographics and political leanings can influence the level of payouts to claimants. New York and California, for instance, are known for awarding high levels of compensation.

Claimants often capitalize on the differences between states by "forum shopping" – i.e., trying to have their case heard in the state most likely to give them a favorable judgment. The claimant may be eligible to bring a case in one of several jurisdictions – for example, an injury happened in one state, but the company is headquartered in another – and choose a state where juries in the past have been sympathetic to claimants. Defending companies, in turn, often spend significant sums trying to remove certain cases from state courts to federal courts, or seeking to transfer the case to another state.

Unclear duties to customers

Canadian manufacturers and retailers selling products in the U.S. are vulnerable to a wide range of risks because of ambiguities around what companies need to do to protect their customers. "Failure to warn" is a common accusation and businesses are in the unenviable position of balancing the need to warn consumers against every conceivable danger with producing reasonable and practical communications related to their products.

"Canadian manufacturers and retailers selling products in the U.S. are vulnerable to a wide range of risks because of ambiguities around what companies need to do to protect their customers."

An unfamiliar insurance market

Companies may assume that a Canadian policy with worldwide territorial scope can simply be extended to cover the U.S., combining the familiarity of a domestic policy with appropriate U.S. coverage. However, a policy issued in Canada will be tailored to Canadian law, which raises the important question of whether the policy will actually pay out if you have a claim in the U.S.

Risk two

Insurance regulation and practices are not the same worldwide. It is tempting to assume that other insurance markets directly mirror our own in Canada, but that is not the case. Companies need to make sure that they understand the different aspects of the U.S. market.

Structuring your coverage

Clients with on-the-ground operations in the U.S. are required to buy a local policy in local jurisdictions.

Local policies are partly useful because insurance terminology sometimes differs between countries.

When companies buy local policies, those policies, as a rule, must comply with the laws of the state in which the company's U.S. operations are located. Many of the states have differing requirements. In some states, for example, a policy has to contain specific language in order to be valid and enforceable in one state; similar but not identical language may be necessary in another state; and a third state may not even prescribe particular wording on that particular topic.

Differing coverages available

Workers compensation

U.S. workers compensation coverage indemnifies the insured for injuries to employees and addresses loss of earnings and medical expenses.

Due to the scope of the coverage, workers compensation insurance is expensive. However, it also brings a range of added benefits, acting in some ways as a healthcare policy for the workforce, although only in relation to on-the-job injuries. As a result, there are benefits to having a workers compensation insurer who is active in claim management, often partnering with their clients to help ensure that the workforce does not get sick or injured in the first place – rather than just paying out if they do.

U.S. auto liability

U.S. policies tend to offer low standard limits that need to be increased to make sure coverage is adequate. This is partly because U.S. claims are often very expensive, possibly due to high damages awarded by a jury. In a 2014 example, a Walmart truck hit a limousine carrying comedians Tracy Morgan and James McNair. The accident injured Morgan and killed McNair.[5] James McNair's family members were awarded US$10 million[6] and Tracy Morgan's settlement was rumoured to be substantially higher.

Gross profit vs. gross earnings business interruption

There are key differences between Canadian and U.S. versions of business interruption insurance.

Canadian gross profit business interruption coverage is designed to put the customer back in the same financial position they were in before the event that disrupted their business. The insurance covers the loss of profits and lasts for a pre-agreed period, such as a year, which allows companies time to get back on their feet.

U.S. business interruption coverage, on the other hand, only covers loss of income until the repairs should reasonably have been completed. However, it is possible to buy an "extended period of indemnity," making the coverage more similar to the Canadian version.

Risk three

Just as the insurance market differs in the U.S., so does the availability of certain types of insurance. We explore the differences between certain key Canadian coverages and their U.S. equivalents.

"As a result, there are benefits to having a workers compensation insurer who is active in claim management, often partnering with their clients to help ensure that the workforce does not get sick or injured in the first place – rather than just paying out if they do."

Significant natural catastrophe exposures

Risk four

Dealing with natural catastrophe exposures can be a challenge for Canadian companies not used to such risks. The U.S. experiences nearly every type of extreme weather on a regular basis, and its climate varies widely across the country.

"In 2015 alone, insured losses from natural disasters in the U.S. came to approximately US$15 billion."

The U.S. is second only to China in the number of natural disasters that it experiences.[7] Of the top 10 insured loss events in 2015, seven took place in the U.S.,[8] and the costliest natural catastrophe worldwide was the winter storms in the U.S. and Canada, which caused US$2.1 billion of insured losses.[9]

Unsurprisingly, the costs arising from such catastrophes can be massive. In the past 35 years, there have been 188 U.S. natural disasters that have cost US$1 billion or more.[10] In 2015 alone, insured losses from natural disasters in the U.S. came to approximately US$15 billion.[11]

In addition to experiencing almost every type of natural disaster, weather varies considerably across the country, so a company with operations across the U.S. needs to understand its unique natural disaster exposures in every location.

Be prepared

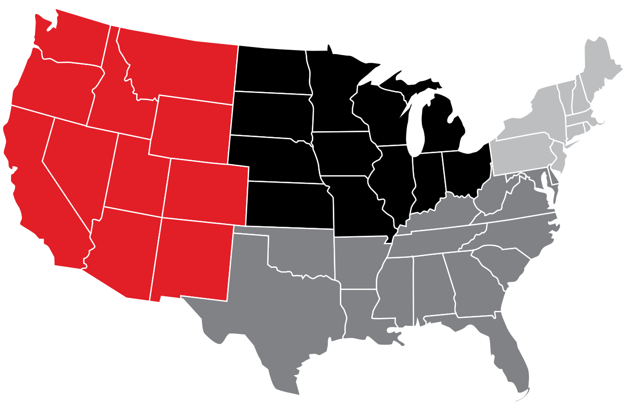
Natural disasters can result in substantial property damage and loss of life, and companies need to ensure that they are prepared and insured appropriately.

A local U.S. policy should cater to all of the extreme weather and natural catastrophe events that can occur, and companies need to understand the true scale of their natural catastrophe exposures, so that they can purchase the right limits.

For those companies establishing new operations in the U.S., it is important to bear these risks in mind when deciding where to base shops, offices or factories. For example, avoid locating operations in an earthquake zone just to be close to customers – or if required to be based there, ensure that buildings are designed to withstand earthquake activity.

52% on average believe severe, damaging weather events have grown more frequent.

51% 49% 47% 59%



How to avoid the risks

Insurance coverage should enable you to fulfill your ambitions and make the most of opportunities, not prevent you from doing so. While there are challenges to purchasing U.S. coverage, they are certainly not insurmountable if you understand the risks involved.

Top 10 tips

We've put together our top 10 tips below for purchasing coverage for your U.S. operations:

1

Make sure you understand your U.S. exposures.

2

Remember that the U.S. is made up of 50 states with 51 insurance jurisdictions, each with different rules, regulations and exposures.

3

Be aware of all local insurance and tax rules and comply with them. Buying the right coverage at the right price and paying the applicable taxes is good for your reputation with a board of directors and customers alike.

4

Be mindful of the litigious environment and high payouts in the U.S., and make sure that you have the right insurance coverage in place in case of possible lawsuits.

5

Do not assume that a Canadian policy can be extended to cover the U.S. Consider having local policies that cater to local laws and regulations.

6

Make sure that your limits are high enough. As an example, think of the substantial amount of damages that might be awarded against you in something like a product liability case.

7

Remember that your duties to customers are often more onerous than in Canada; try to prevent any possible accusations of "failure to warn" relating to your products.

8

Be aware of the differences in the types of coverage available in the U.S. – such as workers compensation.

9

Keep natural catastrophe exposures in mind when you are choosing or building new premises. Ideally, locate your premises away from a natural disaster zone – or ensure that it is built to withstand the risks.

10

Finally, ensure that you partner with brokers and insurers who understand the U.S. market inside out and have claim experts on the ground – preferably in every state where you operate – so that any claims will be dealt with by knowledgeable people who understand the environment.

Ask the experts

While there are challenges around buying insurance coverage for activities in the U.S., we are here to help. Travelers was founded in the U.S. more than 160 years ago and has multiple insurers licensed in all 51 jurisdictions. Today, we are one of the country's leading insurance companies. That means we understand the U.S. market inside out and are experts at helping our clients navigate its complexities.

For more information, visit us at travelerscanada.ca

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About Travelers

The Travelers Companies, Inc. (NYSE: TRV) is a leading provider of property casualty insurance for auto, home and business. The company's diverse business lines offer its global customers a wide range of coverage sold primarily through independent agents and brokers. A component of the Dow Jones Industrial Average, Travelers has approximately 30,000 employees and operations in the United States and selected international markets. The company generated revenues of approximately $29 billion in 2017.

By arrangement with other Travelers companies, strategic partnerships and insurer networks, we are able to provide insurance and risk management services in almost 100 countries worldwide.

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