

MARSH INSIGHTS: PROPERTY

MARSH DELIVERS ASIAN INSURANCE MARKET CAPACITY

By [Julian Ball](#), Managing Director, Global Head of Business Development, Bowring Marsh

In collaboration with its specialist international placement broker, Bowring Marsh, Marsh is leading the way in cultivating and delivering new and emerging capacity from markets across Asia. This includes accessing an estimated US\$1.6 billion of total capacity from Chinese markets.

Bowring Marsh is ideally placed to source capacity in Singapore, Shanghai, Beijing, Seoul, Hong Kong, Tokyo, and Dubai. Bowring Marsh continues to develop and expand international markets for clients and prospects, including:

- In Japan, where Bowring Marsh is working with Aioi Nissay Dowa to strategically review the insurer’s appetite to increase its portfolio to underwrite US and international risks outside of Japan. Aioi Nissay Dowa has an A+ rating with Standard & Poor’s and an A rating with A.M. Best.
- In the Middle East, through development over recent months with markets in the DIFC (Dubai International Financial Centre), several insurers have authorized

high excess-of-loss capacity on a handful of North American accounts. Markets have generally shown the greatest interest in clients that have a global spread of risk, rather than purely North American exposures, especially those clients with some exposures in the Middle East. Markets are quoting on a “follow” basis and should be approached after lead terms are established for a given layer.

The following is a snapshot of the region’s market appetite:

- Abu Dhabi National Insurance Co. (ADNIC), the Mediterranean and Gulf Insurance Co. (MEDGULF), and Kuwait Re (K-Re) have offered small amounts of capacity on middle excess layers (including catastrophe, or CAT). All three insurers prefer to write layers that have not been affected by losses over the last five to 10 years.
- General Insurance Corporation of India (GIC) is participating on several global programs, with lines in the region of US\$10 million to US\$20 million.
- International General Insurance Co. (IGI) in Jordan is able to provide up to US\$35 million in capacity on North American accounts, on non-CAT risks only. The attachment point varies and depends on premium levels and the specifics of the account being quoted.
- Q Re, which is headquartered in Doha, Qatar, is currently accepting facultative property business from Asia, the Middle East, Eastern Europe, and Africa. Currently, Q Re is not able to underwrite business from North America and Western Europe, although this is expected to change later in 2013.

These capacity offerings are combined with recent successes in developing new capacity from markets across Asia, particularly in China, where Marsh just introduced



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new capacity into programs. This new capacity provides further diversification and competition, which reduces cost to clients, and increased catastrophe capacity, which improves coverage for clients.

Chinese markets have significant capital with which to underwrite their portfolios, ranging from approximately US\$450 million to US\$6 billion. While some markets look to clients with assets and exposures in their local regions, geographic footprint is becoming less important, and this new capacity is benefiting both US domestic clients and global clients domiciled in the United States.

Two leading insurance companies in China are supporting Marsh's efforts to introduce capacity from the region and are demonstrating a strong appetite for risks domiciled in the US:

- China Pacific Insurance Company (CPIC), with an estimated US\$1.2 billion in capital, an estimated US\$640 billion in assets, and a Moody's A1 rating.
- People's Insurance Company of China (PICC), with an estimated US\$1.8 billion in capital, an estimated 10% interest from AIG, and a Moody's A1 rating.

These markets are willing to consider quota share participation and, where needed, are issuing direct policies on a self-procured basis and providing significant natural catastrophe capacity. Alternatively, these markets are willing to reinsure a captive or the global fronting carrier. Other markets across Asia require fronting by either captives or other global carriers.

Other markets in China include:

- China Re, with an estimated US\$5.8 billion in capital and the potential to write up to US\$30 million capacity.
- Ping An Insurance, with an estimated US\$2.2 billion in capital and the potential to write up to US\$100 million capacity.
- Huatai Insurance Company, with an estimated US\$500 million in capital.
- Nine accessible markets in greater China.

Chinese markets understand the high quality of Marsh's clients and their focus on risk management and loss control and have thus been encouraged to participate on larger-profile clients. These markets have underwritten or quoted terms for a number of clients within various industries, including;

- Auto manufacturing.
- Steel.
- Mining.
- Special coating manufacturing.
- Chemical manufacturing.
- Logistics.
- Glass manufacturing.

- Hospitality (hotels).
- Retail.
- Real estate.
- Power.

Ratings may be more challenging for real estate clients, whose lenders require a minimum A.M. Best rating unless fronted. Terrorism insurance is available from CPIC on a direct basis as part of the property coverage but not as standalone coverage.

While these are established longstanding markets within their own regions, the time is proving very favorable for clients and prospects that seek further diversification as Marsh looks to align clients' risks within these regions to strategically develop new capacity.

An additional dozen other markets in Singapore, Korea, Taiwan, Hong Kong, and Japan can be approached, with capacity estimated from US\$5 million to US\$150 million.

Bowring Marsh has access to approximately 25 markets across Asia and the Middle East with appetites ranging from quota share to excess-of-loss capacity, including natural catastrophe. All markets meet Marsh's security guidelines, with most markets rated by S&P, A.M. Best, or Moody's.

As global clients continue to develop their own business strategy within these regions, Marsh's local servicing and placement capability make us ideally placed to bring new and innovative solutions to the benefit of clients and prospects.



PUBLIC ENTITIES: HOW INSURANCE AND FEMA WORK TOGETHER

By [Jeb McPherson](#), Senior Vice President, Marsh Risk Consulting

Superstorm Sandy caused major damage to many public entities' real and personal property and critical infrastructure. Just prior to the storm, some local governments and public structures had responded to budget deficits by purchasing less commercial insurance – either lowering their policy limits or reducing critical coverage sublimits. Consequently, in the aftermath of Sandy, many of these entities are facing far greater uninsured property losses than insured losses and are relying on assistance from the Federal Emergency Management Agency (FEMA) to pay for most of their storm-related damage. It is critical for public entities to understand the interplay between insurance and FEMA and to establish claim accounting protocols that satisfy the requirements of both.

As a condition for receiving FEMA public assistance, an applicant must obtain and maintain insurance to cover the facility (i.e., buildings, equipment, contents, and vehicles) for the specific hazard that caused the damage. Under Title 44 of the Code of Federal Regulations, if the damage was caused by any peril other than flood, the coverage commitment must be, at a minimum, equal to the eligible project costs indicated by FEMA's "permanent work" project worksheets. If damages were caused by flood, the coverage required is based on FEMA recoveries, not on total eligible damages. A significant difference exists between the two, so understanding that coverage commitment levels are variable depending on the cause of loss is a critical first step in satisfying FEMA's insurance purchase requirements.

FEMA regulations state that if a facility does not meet these insurance purchase requirements, the agency will not provide assistance for that facility in future disasters of the same type. Thus, it is vitally important that public entities verify that their property risk programs comply with FEMA's insurance purchase requirements.

FEMA'S "SUCCESSIVE DISASTERS OF THE SAME TYPE" REGULATIONS

FEMA's approach to public entities that suffer property damage in successive disasters of the same type could result in drastic reductions of federal aid available to these entities. Public institutions located in high-risk areas prone to flooding, windstorms, or earthquakes may be most affected by FEMA's position, as insurance coverage for these catastrophic perils may be costly and difficult to secure.

FEMA has stated that this policy is an effort to apply the Robert T. Stafford Disaster Relief and Emergency Response Act of 2000 uniformly and as Congress intended.

INSURANCE REQUIREMENTS, DAMAGES, AND FEMA CLAIM RECOVERY

The significance of insurance protection, which forms the basis for calculating any recovery from FEMA, becomes apparent from the onset of a regional disaster. Anticipated or actual insurance proceeds are subtracted from FEMA's total eligible damages to arrive at the starting point for FEMA recovery. FEMA considers itself only a means of last resort and requires entities sustaining damages in a disaster to pursue all available insurance recoveries as a condition for receiving its assistance.

For example, if a university sustained \$10 million of property damage after a declared named windstorm loss but had only \$6 million of insurance, FEMA's recovery starting point would be \$4 million, assuming that all damages are eligible for reimbursement. Although the applicant may receive less than \$4 million from FEMA, the total eligible damages were calculated at \$10 million, which is an important principle for insurance commitment purposes.

FEMA also enforces insurance purchase requirements to help prevent public entities from being underinsured for losses sustained in subsequent disaster events. Before FEMA funding is approved, an applicant must demonstrate that adequate insurance coverage will be obtained and maintained going forward. Thus, \$10 million of insurance coverage specifically for the peril that caused the damages must be in place in order to initiate the recovery process. The insurance commitment is based on total eligible damages — not on actual FEMA recoveries.

Self-insurance may be used to satisfy FEMA's "obtain and maintain" insurance requirements for state governments, but not for local governments and private nonprofit organizations. Those entities (except nonprofit organization whose buildings are located in flood zones) are not required to purchase insurance prior to a disaster if they have not previously received disaster assistance from FEMA. The insurance requirements apply only to applicants that have received public assistance related to previous disasters, are based on eligible permanent work, and are calculated on a building-by-building basis.

Emergency work does not factor into FEMA's insurance requirements, and the requirements do not apply to buildings that have eligible damages of less than \$5,000.

SUCCESSIVE DISASTERS

Under FEMA's insurance commitment regulations, what would happen if the same university suffered damages from another declared named windstorm event two years later? In such instances, FEMA may arrive on-site and request all pertinent insurance information and a detailed description of the damage sustained at each facility. Accuracy is critical in advising FEMA of past assistance and related insurance requirements so that the FEMA recovery process can be expedited and credibility can be established. FEMA deployed its National Emergency Management Information System (NEMIS) in 1998 to record such information.

In the example described in the previous section, in order to receive FEMA assistance for a subsequent loss of the same type, an entity's total loss must exceed \$10 million (the limit of insurance obtained after the first disaster). If a second declared named windstorm disaster caused \$13 million in damages, FEMA's starting point in calculating the recovery amount will be \$3 million (the amount in excess of available insurance). Under this scenario, \$13 million of flood insurance coverage would need to be obtained and maintained going forward.

If the university failed to carry the \$10 million of insurance coverage, no FEMA assistance would be available for the second, same peril disaster. Inadequate insurance for the same peril damages will be considered ineligible for public assistance unless certification is granted by the state insurance commissioner and agreed to by FEMA waiving the insurance purchase requirements.

The insurance requirement may be waived only if the state insurance commissioner certifies that the type and extent of insurance required by FEMA is not reasonably available. For practical purposes, the premium costs for adequate insurance coverage requirements would have to represent a significant portion of the public entity's global operating budget in order to justify this waiver ruling. FEMA then must approve the insurance commissioner's findings before waiver authorization is granted.

During an entity's first disaster, insurance deductibles are considered uninsured and eligible for public assistance. However, most deductibles are not recoverable after a second disaster of the same type.

For example, a university's health and science building has stated values of \$40 million; a deductible of 3% of stated values, or \$1.2 million; and a blanket named windstorm policy for \$50 million. If a hurricane caused \$4 million of damages to the building and the disaster was declared, FEMA assistance would be available to cover the uninsured loss — the \$1.2 million deductible. FEMA's insurance purchase requirements would be met since the blanket windstorm coverage exceeds the total eligible damages (\$50 million versus \$4 million). No additional insurance coverage would be required.

However, the university decides for the next policy period to reduce premium costs and increase its deductible from 3% to 5% of stated values. If a hurricane caused \$5 million of damages to the health and science building one year later, only \$1 million of FEMA assistance would be available (\$5 million of eligible damages less \$4 million of prior eligible damages from prior FEMA assistance). In this instance, the university may recover \$3 million from insurance (\$5 million less the new 5% stated value deductible of \$2 million). Although the university's uninsured losses would technically be \$2 million (the deductible or 5% of \$4 million), only \$1 million of assistance would be considered by FEMA.

Because FEMA provided prior disaster assistance at this location, only damages in excess of the total eligible damages from the first disaster are available for recoveries during a second, same peril disaster. The health and science building loss of \$5 million would be funded using \$3 million from insurance, \$1 million from FEMA, and \$1 million of self-funding sources (unrecoverable losses).

The bottom line is that FEMA will provide financial aid to reduce uninsured losses following a declared disaster. However, FEMA expects public entities to be accountable for subsequent disasters caused by the same peril. If a public entity has received FEMA assistance in the past, it should not rely on FEMA to cover the same types of damages in the future. Identifying FEMA's insurance purchase requirements and verifying that those requirements are satisfied will allow public entities favorable FEMA recovery opportunities in subsequent disasters.

CATASTROPHE MODELING RELIES ON HIGH QUALITY DATA

By [Bob Smith](#), Global Practice Leader, Marsh Property Risk Consulting

Presenting a large and complex property portfolio to insurers is a challenge on many fronts. Loss experience, stability of operations, and a good understanding of the operational hazards and external exposures to the portfolio all come into play.

Exposure to catastrophic natural hazard (CAT) events such as earthquake, hurricanes, and flood is now evaluated and quantified by insurers using catastrophe models developed using high quality, up-to-date science and engineering data and methods. These models, which are mainstays for insurers, rely on descriptive data inputs to calculate damage projections.

Marsh Risk Consulting's (MRC) CatDQ service brings a powerful solution to our clients to help drive the best results for their natural catastrophe insurance placements.

Every structure has unique attributes, including location, time of construction, materials used, and building codes in place at construction. Each structure will behave differently when subjected to a CAT event and, consequently, damage projections will vary.

CAT models assign vulnerabilities to properties in developing a composite portfolio view that, when combined with the hazard level, results in estimates of projected losses at various return periods and an average annual loss for the portfolio. Most insurers derive the appropriate premium based primarily on the average annual losses.

These loss estimates are shrouded in uncertainty. First, there is uncertainty around the frequency and severity of an event impacting the portfolio. There is the uncertainty around the models' assigned vulnerability for each structure within the portfolio and how it relates to the actual vulnerability of the structure. If the input data is of poor quality and does not account for all relevant construction and location factors, there will be greater uncertainty and less-than-optimum modeling results. When the input data are poor, underwriters typically will increase the pricing to account for their own uncertainty about what they are underwriting.

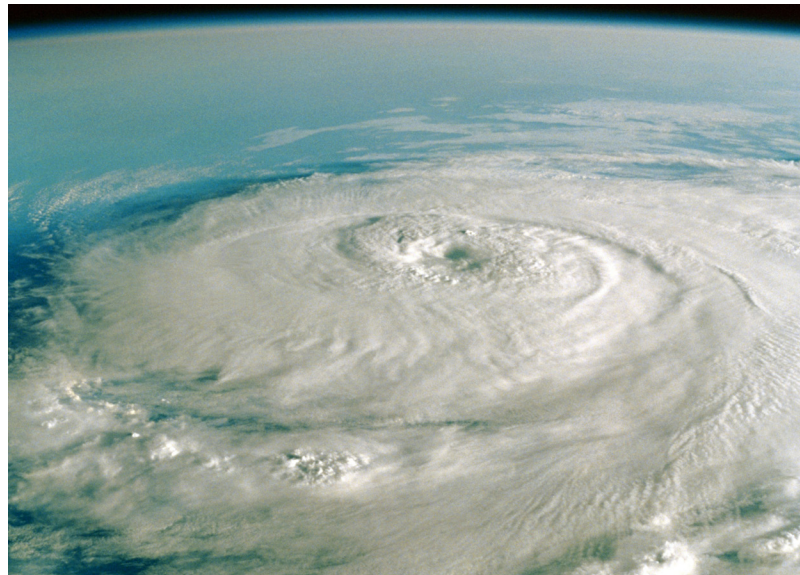
The fact is: Poor information equals greater uncertainty, which in turn equals larger premiums.

The CatDQ service is completed by an MRC natural hazards and analytics team experienced with multiple catastrophe models. The team understands structures, catastrophic events, and the benefits of presenting property portfolios accurately to the markets. By identifying a portfolio's loss drivers, our team can determine the structural characteristics for a location and accurately define each structure by using a wide range of fully validated and documented primary and secondary building characteristics. This provides for a refined building description that eliminates much of the uncertainty around a building's performance during an event and thus the premium associated with this uncertainty.

MRC delivers a detailed report confirming and documenting the construction components and exactly how they should be coded for modeling using models from both RMS and AIR. This MRC assessment report can give insurers a high degree of confidence in a structure's construction and its proper coding. Insurers typically accept the coding presented in the report, which we have shown to improve the quality of the results. The result helps client achieve the best placement results.

The service involves an additional fee, but the return on the investment in annual premium savings is typically higher than the fee. Depending on how a client's program is currently positioned, annual premium savings in excess of 15% are not uncommon. More importantly, all savings realized now will continue annually, barring a significant change to the property portfolio. Once high-challenge locations are assessed, properly described, and coded for modeling purposes, they will not have to be revisited year after year.

For more information about MRC's CatDQ services, contact your Marsh representative.



NEW RMS CATASTROPHE MODEL SLATED FOR RELEASE IN 2013

By [Duncan Ellis](#), Marsh's US Property Practice Leader

Two years after the release of v11 of its CAT modeling program, RMS is targeting the end of July to release v13. (Contrary to popular belief, the various versions of RMS' CAT modeling are not tied to upgrade numbers, but to the years in which they are released.) RMS v13 will pay special attention to hurricane assumptions that were changed in v11, resulting in large increases in annual average loss (AALs) and aggregate exceedance probabilities (AEPs). So, what's changing?

In 2012, RMS presented supplemental information about the assumptions and uncertainties in v11. And in March 2011, RMS undertook a comprehensive review of its medium-term rate (MTR) forecasts, which give a prospective view of hurricane frequency incorporating past hurricane activity; underlying drivers of activity, such as surface water temperatures; other weather patterns; and points of landfall. The MTR hurricane forecast is being updated to incorporate new research on hurricane activity rates and data from the past two hurricane seasons. The assumptions related to medium-term hurricane frequencies are likely to decline, particularly in Florida and other states in the Southeast. Conversely, small changes are expected to long-term rate (LTR) forecasts.

RMS has also been reevaluating storm surge "leakage" of flood claims into wind claims. This resulted from feedback from some insurers that the model was overly conservative in its modeling of wind and the introduction of surge that may or may not have been insured. RMS has thus looked at past claims activity and will make adjustments to these assumptions.

Continuing with that theme, v11 brought to the forefront discussions around storm surge, which was the driving force behind most claims from Superstorm Sandy, which happened well after v11 was introduced. Along with the changes mentioned above, v13 will be enhanced to take into account:

- Updated FEMA flood zoning.
- Updated base flood zone elevations.
- Cross references with RMS' enhanced flood zone data.

- Updated, built-in National Flood Insurance Program (NFIP) insurance assumptions.
- Enhanced methodology for determining default building elevations.
- Updates specific to Texas City, Texas and southern Louisiana.

Other changes specific to Puerto Rico vulnerability curves, the Caribbean in general, and Central America and Canada will be included. News of the upcoming v13 is welcome as the 2011 version introduced significant changes to the view of risk, particularly for peak risk levels, which led to some significant increases in AALs in certain areas.

These changes are likely to bring down RMS' view of hurricane risk from the v11 software release. The changes, in conjunction with better data and information — perhaps gleaned from a detailed data quality review — could potentially bring down the AEP and AAL estimates, which in turn will have a direct effect on premium.



TERRORISM RISK MODELS AID IN RISK FINANCING DECISIONS

By [Edward J. Haas, Jr.](#), Managing Consultant, Marsh Risk Consulting

Terrorism presents a dynamic risk landscape for organizations to understand and prepare for, one in which the potential risks and management strategies are ever-changing.

The three firms that produce catastrophe modeling for natural hazards — AIR Worldwide, EQECAT, and Risk Management Solutions (RMS) — added terrorism modeling to their capabilities following the attacks of September 11, 2001.

FINANCIAL QUANTIFICATION

Models help organizations understand the relationship between vulnerable sites and the potential likelihood of impact from terrorist acts — or other risks — on their operations and profitability. These models seek to quantify the potential economic losses from a terrorist attack and thus aid in risk quantification, insurance program design, and risk financing. Financial quantification can help companies to:

- Achieve greater understanding of their financial exposure.
- Assess the appropriateness of insurance deductibles and limits.
- Optimize risk finance strategies.
- Rate the terrorism risk to negotiate adequate insurance premiums.
- Understand the risk's potential impact on capital.
- Help prioritize risk mitigation strategies.
- Enable efficient business continuity planning.
- Understand the correlation and potential benefits of diversification among sites, locations, and regions.

TYPES OF MODELS AND ANALYSES

The three main methodologies used to model terrorism risk are:

- **Probabilistic modeling**, which estimates losses based on a large number of events, and is most suited to portfolio risk.
- **Exposure concentration analysis**, which identifies and quantifies concentrations of exposures around potential terrorist targets.
- **Deterministic modeling**, which represents a compromise between the lack of accuracy in accumulation analysis and the uncertainty of a probabilistic model. It imposes an actual event's damage "footprint" at a specified target, producing a specific, yet hypothetical, scenario that can be analyzed with some certainty.

TERRORISM MODELING PROCESS

Probabilistic modeling of terrorism follows a technique that is similar to earthquake or windstorm modeling.

Exposure at risk: What are the likely targets in the vicinity of the property being modeled? In some instances (for example, trophy hotels) the property itself will be a target. Others include government buildings, iconic sites, transportation centers, skyscrapers, tourist attractions, industrial plants, and nuclear energy sites. The likelihood of an attack on a target is developed considering its likely "desirability" and the capabilities of groups that may be motivated to attack. The potential for thwarting an attack is also calculated.

Quantify hazard: This step involves applying each attack scenario to each target and then quantifying the impact on the property of concern.

Assess vulnerability: For each attack mode on each target, the model determines a local impact on the property, including a financial damage range.

Financial impact: Each of the previous factors has a variance probability associated with it. The models combine all targets, all attacks, and all probabilities of damage into a factor that is applied to the values exposed. The model further optimizes the selection of values, targets, attacks, and damages to produce the loss level estimates. The potential for swarm attacks (multiple, simultaneous attacks at different sites) is included. The result is the exceedance probability table, or curve of probabilities of exceeding different levels of loss, in dollars. Additionally, annual aggregate loss levels, and average annual loss levels are determined.

CONCLUSION

To help manage and underwrite terrorism risks, insurers, reinsurers, brokers, and individual companies are increasingly using data management and modeling tools. The dynamic nature of terrorism and the uncertainty involved requires a specialized approach to manage the risk.

MARSH'S 2013 TERRORISM RISK INSURANCE REPORT

In 2002, in response to the September 11, 2001, terrorist attacks, Congress passed the Terrorism Risk Insurance Act (TRIA) to help alleviate a severe market shortage for terrorism insurance. TRIA provided a federal "backstop" for insurance claims related to terrorism events in the US as defined by TRIA. It has since been extended and modified twice, most recently in December 2007, when it was renamed the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA). If not renewed, the Act is scheduled to expire on December 31, 2014.

For a detailed look at TRIA, terrorism insurance benchmarking, and related issues, we invite you to read *Marsh's 2013 Terrorism Risk Insurance Report*. To access a copy, reach out to your Marsh representative, visit us at [marsh.com](#), or send a request to questions@marsh.com.

TOTAL VALUE IS KEY TO CHOOSING INSURERS

RISK PROFESSIONALS LOOK BEYOND PRICE

Overall value, not simply price, is a main consideration for organizations as they seek bids from carriers for their insurance programs. And a key component of value is claims handling capacity, according to a panel of risk managers speaking at a recent industry forum in New York City.

Another key consideration in selecting insurers is the carrier's commitment to communicating year-round, not just during the renewal period. Other factors weighing on the decision include stability related to price, ratings, and capacity. Loyalty, too, is important as organizations generally want an insurer that will stay with the insured even after a large loss, and that will commit to do business on a given risk in a specific geography for the long term. Finally, panelists said, it would be helpful to see more collaboration between a carrier's claims and underwriting departments.

Other observations from the panel included:

Risk differentiation: Companies spend significant time educating insurers about differentiated risk profiles, which are based largely upon such items as best-in-class engineering, analytics, business continuity plans, and valuations. Insurers could potentially improve the process through on-site visits and meetings with company engineers. Panel members noted

that best-in-class risk measures are not taken simply to reduce insurance premiums, but to control risk and improve the business. Increased transparency from insurers on underwriting methods would help to keep policyholders' senior management apprised of the business case for investing in best-in-class measures.

Broker relations: Brokers generally are adept at bringing technical expertise to the process, but there sometimes can be an overreliance on email and not enough face-to-face contact. Brokers could also provide better intelligence regarding product development and product solutions, and focus more on assessing specific risk needs rather than relying too heavily on benchmarking. Finally, panelists urged brokers to devote more resources to consulting, developing creative solutions to problems, and building national and international capability.

Alternative risk transfer: The cost of alternative risk transfer products — including insurance derivatives; insurance options; multiyear, single limit solutions around aggregated covers; CAT bonds; and parametrics — is high relative to traditional insurance. Still, such products may present the best solutions for companies with esoteric or unusual risks. They may also work well for companies that have heavy rate on line(s) (ROL) for their primary layers, which are being driven by CAT perils that may be better addressed with an aggregated CAT limit with a reload provision. These products may become more widely used as their price points become more in line with traditional insurance. Just such a trend is developing with some heavily CAT-exposed risks and with insured's that are looking to "finance their risk" over the long term as opposed to "buying insurance" annually.

The panel, hosted by Advisen, was moderated by Duncan Ellis, leader of Marsh's US Property Practice. The other panelists were Jim Curtin, vice president, Risk Management at Vornado Realty Trust; Judy McInerny, director, Risk Management at Corning; and Shari Natovitz, senior vice president, Risk Management at Silverstein Properties.

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