

## Marketplace Conditions—Sanity Restored or Madness?

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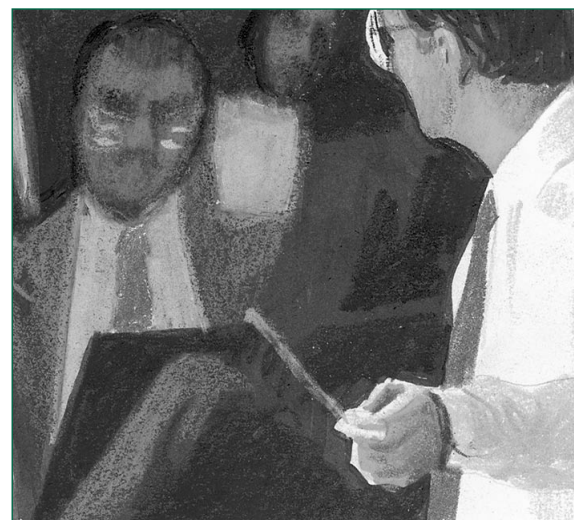
Mr. Arthur W. Powers  
Director of Marketing

By Michael J. Bemis, President and CEO

One year ago I wrote an article for this publication entitled “Marketplace Malaise—Sources and Solutions.” In that article I attempted to delineate and briefly explain the various elements/phenomena that produced or contributed to insurance market conditions at any point in time. The elements that I identified were:

1. your own account loss experience;
2. your insurer’s asbestos and environmental losses (so-called A&E losses);
3. emerging and developing tort loss experience (such loss phenomena as toxic mold, lead hazards, employment practices liability actions, pharmaceutical products liability, cell phone radiation, and others, now including many allegations of inappropriate/inadequate security);
4. natural and man-made catastrophe loss experience;
5. contingency loadings for losses expected as the result of legislation or regulatory actions (such as the increasing frequency of claims after the passage of the Private Securities Litigation Reform Act, or the quickly mounting D&O claims in this post-Enron, WorldCom, Arthur Anderson, etc. era, or anticipated litigation and resultant losses relating to Patient’s Rights legislation);
6. insurer expenses and the effect that wage, medical/hospital care, home repair, auto repair, and labor costs price inflation (as a function of claim costs presented to the insurer or the insurer’s own workforce) has on insurance carriers;
7. investment results and the manner in which, and degree to which, the investment markets are “propelling” or “propping” or “dragging” insurer operating results; and
8. competitive pressure—from standard market carriers, alternative market carriers, or financial services convergence following establishment of new financial service providers enabled by passage of the Gramm-Leach-Bliley Financial Services Modernization Act.

Two elements that I did not discuss, but which are becoming more and more relevant, are the effect of



consumer fraud on insurance company results, and the effect of reinsurance costs on primary insurer results.

Having completed this review, what can be said about the present state of the market? I would assert that three things can definitively describe this insurance market:

1. it is irrefutably a “hard” market (i.e., very high premiums, with restricted capacity and much tightened coverage terms/conditions);
2. it is considered by almost all primary insurers and reinsurers, many agents and brokers, and most industry pundits as a market that is experiencing a much needed “correction” that has restored “sanity” to the insurance transaction; and
3. by most insureds it is considered to be a difficult market, and by many insureds, a “price-gouging” market.

#### So who is correct?

As is the case with so many things in life, I believe that a thorough, unemotional and objective analysis of circumstances would lead one to conclude that there is validity to both the “sanity” and “madness” perspectives. Why would I contend that this is so?

Clearly, insurers are dealing with some historically unprecedented circumstances that make it ever more difficult for them to profitably perform their function in society. For example, consider:

(See *Marketplace Conditions* on page 6)



## From the Office of the President

By Michael J. Bemis, President and CEO

Enclosed is our mid-year unaudited financial report reflecting TNCRRG results through June 30, 2002, and comparatively year-over-year. I am indeed grateful that I am able to immediately highlight for you the significant improvement in TNCRRG results from 2001

to 2002. More specifically, you will note that we produced a \$217,508 operating profit through six months of our fiscal year, compared to a \$576,152 operating loss for this same period last year. So what has changed? Let me analyze that for you now.

To begin, the most significant development benefiting our company was the reduction in losses and loss adjustment expenses year-over-year. This may be surprising in light of the present crisis in the Church. However, while the actual number of sexual misconduct incident and claim reports to TNCRRG has substantially accelerated in 2002, it is a fact that the majority of these reports will never generate a loss to TNCRRG. The reason is that they relate to activities/victimization that pre-dates the existence of TNCRRG, and therefore occurred prior to the applicable retroactive dates of our claims-made coverage for sexual misconduct. In any event, we experienced a \$1,126,659 improvement in loss results for the period, year-over-year.

Another positively contributing factor to the improvement in our results was our ability to “hold the line” on overall non-loss expenses, even in light of consistent, and in some cases sizable, increases in the costs of goods, services, and supplies that we require to undertake our

operations. Our general and administrative expenses through six months declined by \$16,246 (1.1%).

On a somewhat negative note, our net investment income was dramatically reduced year-over-year, resulting in \$369,077 less investment income generated by TNCRRG through 6/30/2002 than through 6/30/2001. This was not the result of any alteration in our investment philosophy, our investment strategies, or our investment managers/adviser. The outcome simply reflects the very tough market conditions for both fixed income and equity securities so far this year.

Nevertheless, our ability to keep underwriting revenue essentially flat year-over-year, while reducing G & A expenses, combined with the major “lift” provided by reduced loss experience, all contributed to our operating profit of \$217,508, which represents a \$793,660 improvement in results year-over-year.

In closing, while I am very happy to report these results, I also need to remind you that by far the single most important element “driving” TNCRRG results is loss experience. Certainly we can significantly and positively affect that experience through our risk control efforts with our VIRTUS® programs, but much of these results is simply random and beyond our control. That is why we are always thankful when we experience improvement in our loss results. Looking “down the road,” if we continue to have favorable loss results in 2002, TNCRRG should be able to generate a sizable operating profit, even in light of the present dismal investment markets.

*Michael J. Bemis*

## Income Statement

|   | Year Ended<br>June 30, 2002<br>(Unaudited) | Year Ended<br>June 30, 2001<br>(Unaudited) |
|---|--|--|
| <b>REVENUES</b>                                     |  |  |
| Underwriting income                                 | \$ 2,176,215                               | \$ 2,185,847                               |
| Net investment income                               | 775,919                                    | 1,144,996                                  |
| Net realized gains (losses) on sales of investments | 13,654                                     | 26,212                                     |
| Ceding commission income                            | <u>180,619</u>                             | <u>118,920</u>                             |
| <b>TOTAL REVENUES</b>                               | <b>\$ 3,146,407</b>                        | <b>\$3,475,975</b>                         |
| <b>EXPENSES</b>                                     |  |  |
| Losses and loss adjustment expenses                 | \$ 1,279,741                               | \$ 2,406,400                               |
| Premium taxes                                       | 130,504                                    | 101,021                                    |
| VIRTUS® expenses                                    | 487,633                                    | 517,347                                    |
| Management fees                                     | 41,910                                     | 51,519                                     |
| Professional fees                                   | 114,875                                    | 166,744                                    |
| Salary and fringe benefits expense                  | 407,415                                    | 372,152                                    |
| Travel expenses                                     | 130,569                                    | 157,314                                    |
| Other expenses                                      | <u>336,252</u>                             | <u>279,630</u>                             |
| <b>TOTAL EXPENSES</b>                               | <b>\$ 2,928,899</b>                        | <b>\$ 4,052,127</b>                        |
| <b>NET INCOME</b>                                   | <b>\$ 217,508</b>                          | <b>\$ (576,152)</b>                        |

# Balance Sheet

|   | Year Ended<br>June 30, 2002<br>(Unaudited) | Year Ended<br>June 30, 2001<br>(Unaudited) |
|---|--|--|
| <b>ASSETS</b>   |  |  |
| Cash and investments                                      | \$ 39,178,432                              | \$ 41,756,572                              |
| Accrued interest/Investment income                        | 424,698                                    | 500,162                                    |
| Premiums receivable                                       | 328,742                                    | 132,771                                    |
| Reinsurance recoverable on paid losses                    | 2,934,407                                  | 1,857,459                                  |
| Reinsurance recoverable on unpaid losses                  | 9,772,799                                  | 10,357,789                                 |
| Prepaid reinsurance premiums                              | 705,007                                    | 368,325                                    |
| Other assets  | 148,290                                    | 156,515                                    |
|   | <u>                    </u>                | <u>                    </u>                |
| <b>TOTAL ASSETS</b>                                       | <b><u>\$ 53,492,375</u></b>                | <b><u>\$ 55,129,593</u></b>                |
| <br><b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>           |  |  |
| Loss and loss adjustment reserves                         | \$ 21,996,825                              | \$ 22,665,506                              |
| Unearned premiums   | 1,823,170                                  | 1,219,315                                  |
| Reinsurance balances payable                              | 1,068,898                                  | 405,022                                    |
| Premium taxes payable                                     | 15,989                                     | 18,136                                     |
| Unearned ceding commissions                               | 70,040                                     | 119,925                                    |
| Other liabilities   | 263,344                                    | 101,109                                    |
|   | <u>                    </u>                | <u>                    </u>                |
| <b>TOTAL LIABILITIES</b>                                  | <b><u>\$ 25,238,266</u></b>                | <b><u>\$ 24,529,013</u></b>                |
| <br><b>SHAREHOLDERS' EQUITY</b>                           |  |  |
| Capital stock:  |  |  |
| Class A   | \$ 1,160                                   | \$ 1,140                                   |
| Class B   | 297,997                                    | 297,562                                    |
| Additional paid-in capital – cash                         | 392,987                                    | 347,530                                    |
| Additional paid-in capital – policyholder dividend        | 8,879,436                                  | 8,879,436                                  |
| Unrealized gain (loss) on investment                      | (2,938,197)                                | (283,671)                                  |
| Retained earnings   | 21,620,726                                 | 21,358,583                                 |
|   | <u>                    </u>                | <u>                    </u>                |
| <b>TOTAL SHAREHOLDERS' EQUITY</b>                         | <b><u>\$ 28,254,109</u></b>                | <b><u>\$ 30,600,580</u></b>                |
| <br><b>TOTAL LIABILITIES AND<br/>SHAREHOLDERS' EQUITY</b> |  |  |
|   | <b><u>\$ 53,492,375</u></b>                | <b><u>\$ 55,129,593</u></b>                |

# Expediting cost efficient resolution of claims

By *The Honorable Anthony J. Mercorella, Retired Justice Supreme Court of the State of New York*

In the increasingly cost-conscious arena of legal services, companies are constantly seeking alternatives to the expense, delay and uncertainty of the American civil justice system. Realizing that more than 97 percent of all civil actions eventually settle prior to trial, it is readily apparent there is a need to re-evaluate your approach to resolving disputes before and after litigation commences.

Alternative dispute resolution (ADR) encompasses various techniques aimed at resolving disputes without full-blown litigation. The procedures involved with ADR generally resolve disputes quicker and more efficiently because the parties, depending on the technique used, have more involvement and control over the process and outcome. ADR generally involves negotiation, mediation or arbitration. Negotiation allows the parties involved to reach a mutually acceptable agreement whereas arbitration involves a third-party decision maker who can render a binding decision. Mediation falls somewhere in the middle of negotiation and arbitration by allowing a third party to try to facilitate a settlement between the parties involved.

Defense counsel must be committed to providing quality legal services to our shareholders/insureds without sacrificing cost-efficiency. Defense Counsel should explore new ways to better serve their needs. The use of ADR as an effective and efficient method of resolving disputes should be initially considered as a practical alternative to more traditional litigation.

## Why should you choose ADR?

There are several good reasons for choosing ADR to resolve disputes. The two major advantages of ADR over the litigation process are efficiency and economy. The methods provide convenient and expeditious proceedings, speedy results, quick solutions, and substantial time savings. The methods are also economically sound, as the procedures save significant costs, including unneces-

sary attorneys' fees and trial expenses.

The confidentiality of the ADR procedures and the privacy of the results allow for a resolution of the dispute without public exposure. These procedures also benefit from the expertise of the individuals involved. The people who assist the parties or who decide the disputes are impartial, neutral, independent, knowledgeable and trained experts. The procedures are less formal and structured than litigation and avoid the application of strict rules, legal technicalities and complex procedures.

The flexibility of the ADR procedures is another reason for their appeal. The parties involved can select a dispute resolution method, which meets with their interests and needs. This control over the process makes for greater satisfaction for all parties involved.

Another advantage of the ADR procedures is the parties' ability to explore alternative settlement arrangements such as structured settlements yielding creative and innovative results, which are of mutual benefit to the parties. Further, ADR will eliminate unpredictable judicial decisions and excessive jury verdicts.

## When should you choose ADR?

When deciding to incorporate ADR procedures as a method of handling disputes, it is important to design a comprehensive strategy for their implementation. This strategy must provide a method for answering the following questions:

1. What type of dispute is this?
2. What are the strengths and weaknesses of the dispute from our perspective? From the claimant's perspective?
3. What exposure potential does this case present?
4. What are the estimated defense costs of this dispute should it develop into litigation?
5. Does this case present the opportunity for setting a legal precedent that will be beneficial or harmful in subsequent disputes?
6. What method of resolving this dispute will result in the most favorable outcome both from a legal and an economic viewpoint?
7. Is there an ADR procedure that will best serve us in resolving this dispute?

Your experience with both traditional litigation and ADR methods should enable you to determine the dispute resolution strategy that is best suited for each case. Do not forge blindly down the path of litigation.

Once you have made a determination that a dispute may be amenable to resolution through an ADR method, you should consider these checklists as to the suitability of a particular ADR method:

## Factors that support ADR:

1. The business relationship.

(Continued on page 5)

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To learn more about National Catholic, visit our company website:

[www.nationalcatholic.org](http://www.nationalcatholic.org)

To learn more about our child sex abuse prevention programs and other risk control programs, go to:

[www.virtus.org](http://www.virtus.org)

(Continued from page 4)

2. It is desirable to be able to determine the outcome of the dispute.
3. The position of each side has merit, and a trial could well result in either side's prevailing.
4. Trial preparations would be costly and protracted.
5. A speedy resolution is important.
6. The dispute raises highly technical or other complex factual or legal issues.
7. An adverse jury trial result and/or precedent.
8. The law on the determinative legal issues is well settled.
9. Publicity about the case or its outcome should be avoided.
10. The case lends itself to settlement before a trial court decision.

11. A strong presentation will give one side or the other a more realistic attitude about the case.
12. A mediator could help diffuse the emotion or hostility which may bar a settlement of the dispute.
13. The evaluation of a neutral adviser could help break the stalemate.

**Factors that don't support ADR:**

1. The amount in controversy is not extremely large.
2. A vital shareholder's interest is involved.
3. The case can most probably be disposed of on a motion for summary judgment.
4. There is no bona fide dispute. The other side's case is without merit.

*Justice Mercorella is a partner with the firm of Wilson, Moskowitz, Edelman & Dicker, New York, NY. Article reprinted with permission.*

## Plan now to attend National Catholic's 2003 Winter Meeting February 2 to 4, 2003, San Diego, California

Our 2003 Winter Meeting will be February 2-4 at the Hyatt Regency Islandia in San Diego, California. We hope to be able to present another VIRTUS® programs workshop at the meeting, along with workshops on other timely and relevant issues. Information about the 2003 Winter Meeting was mailed to shareholders and friends this summer. Detailed information about the meeting will also be available on our company website in the next few weeks. Keep an eye on our online calendar of events at:

**www.nationalcatholic.org**

We can guarantee rooms at our special group rates only for those who register before December 20, 2002. To expedite the registration process, most of your registration can now be managed through our website. The process is simple and takes approximately 10 minutes to complete. To register, go to:

**www.nationalcatholic.org/calendarofevents.htm**

- 1) Read the letter from Michael Bemi, regarding the Winter Meeting.
- 2) Read the Letter from Christian Brothers Travel Services, regarding the hotel reservation process.
- 3) Next, click the link to print the Christian Brothers Travel Services hotel registration form. You'll need to fill out this form and return it according to the mail or fax instructions included on the form.
- 4) Finally, click the link to Register Online with National Catholic. This online registration DOES NOT book your hotel room. You must make your hotel reservation according to the instructions provided by Christian Brothers Travel Services. This online reservation does, however, hold your place at all the Winter Meeting events.

**Note:** Remember to make your airline reservations at your earliest convenience.

If you have questions about the reservation process, please call our toll-free number at 1-877-486-2774. For details about the hotel and the San Diego area, visit the Hyatt Regency Islandia website:

**www.islandia.hyatt.com/property/index.jhtml**

The screenshot shows the website for The National Catholic Risk Retention Group, Inc. The main heading is "Calendar of Events" with a sub-heading "Click on a calendar item, below, to go directly to that item:" and a bullet point for "2003 Winter Meeting, February 2-4, 2003, San Diego, California". Below this is a section titled "Plan now to attend National Catholic's 2003 Winter Meeting" with a sub-heading "(Updated on Thursday, August 08, 2002)". The text describes the 2003 Winter Meeting at the Hyatt Regency Islandia in San Diego, California, and provides instructions on how to register. A "Here's how to register:" section lists four steps: 1. Read the letter from Michael Bemi, 2. Read the letter from Christian Brothers Travel Services, 3. Print the registration form, and 4. Register online. A "Note" section reminds users to make airline reservations early. A "More about the hotel:" section describes the Hyatt Regency Islandia. At the bottom, there is a "Have questions? Want to place an order? Need technical support?" section with a link to contact the company.

# Marketplace Conditions—Sanity Restored or Madness?

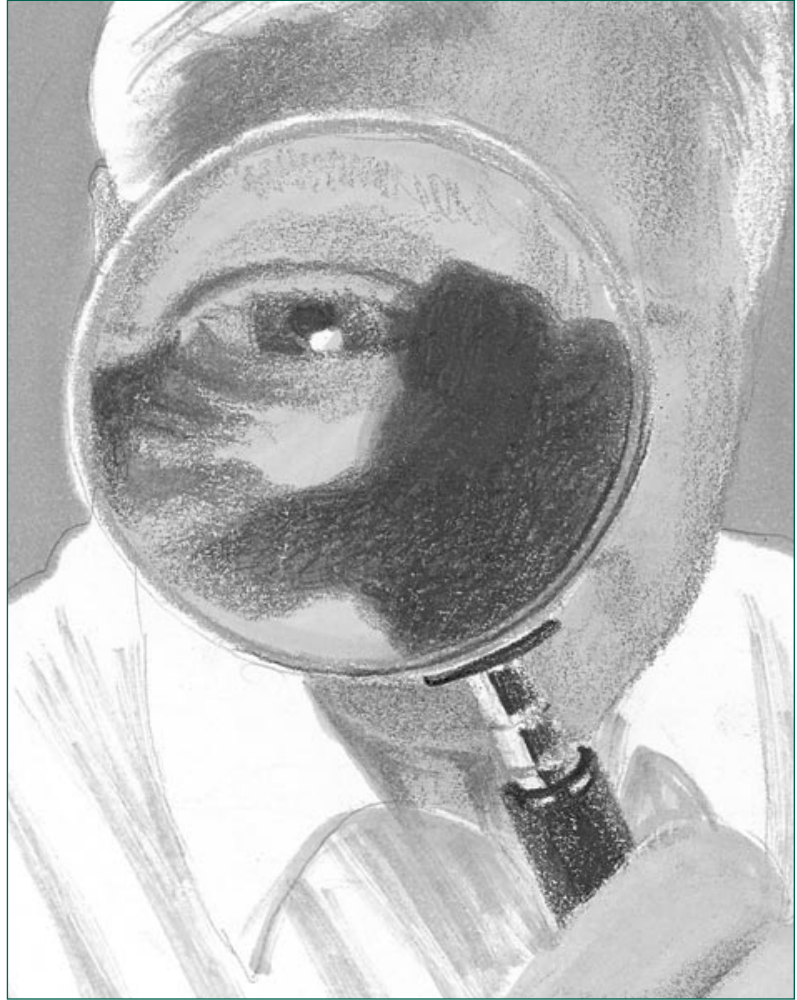
(Continued from page 1)

1. the 9/11 WTC tragedy was the single largest insured event in history, and other insured terrorism losses are a virtual certainty (note that many carriers still provide terrorism coverage for many of their lines of business/insured accounts);
2. insurance fraud is both escalating and at an all-time high magnitude—costing the industry billions in loss payments and for fraud prevention activities;
3. the investment markets, which have been quite “friendly” to the insurance industry for many years, now are hurting the industry’s ability to offset underwriting losses, and also are leading to significant reserve strengthening requirements for life insurers writing annuity business (because current market returns can no longer assure ultimate guaranteed payouts);
4. emerging torts like toxic mold are starting to have very serious consequences for certain carriers (mostly homeowners insurers) in certain states (California, Florida, and Texas, among others);
5. Directors’ and Officers’ claims/losses are skyrocketing post Enron and similar business board and officer malfeasance debacles;
6. asbestos losses have reemerged in a newly threatening fashion—with plaintiffs’ lawyers going after construction materials suppliers, asbestos installers, and architects/engineers that specified asbestos in design plans, all of whom were not previous targets of litigation;
7. the competitive “fallout” from financial services convergence legislation is beginning to have an effect;
8. litigation costs are at an all-time high; and
9. primary insurers are unquestionably being “pinched” by sometimes extreme increases in reinsurance costs, reduced capacity from their reinsurers, or both.

Having just said all this, what else is demonstrably true? It is inarguable that there are many insureds with excellent long-term incurred loss results, who also maintain high level and high quality risk control programs, and who can demonstrate consistent loyalty in relationships with their insurers, who nonetheless are having great difficulty renewing coverage with adequate limits, appropriate terms/conditions, and at affordable prices. This is simply wrong and indefensible. Professional underwriting always recognizes, indeed demands, a process of discriminating excellent risks, from good risks, from poor risks. When this doesn’t occur, then your risk (if good or excellent) has not been underwritten—it has been “book underwritten” (generally an oxymoron).

## So how do you fight back? You have to:

1. retain those losses that you can (consistently predictable ones that are within your budget, either because of your cash flow, or because you gradually fund for them)—don’t ever “trade



- dollars” with an insurer;
2. maintain a solid and consistent risk control program—preventing as many losses as possible—mitigating the severity of those you couldn’t prevent;
3. place your business with Catholic insurance programs (keeping the earnings generated by profitable underwriting “within” and controlled by “the family”—where they will be returned to you via dividends, increased limits, enhanced coverages, and improved services; and
4. negotiate, negotiate, negotiate—and “shop” when necessary.

## National Catholic welcomes three new shareholders

Since our last newsletter, two archdioceses and a diocese have joined the National Catholic family. We now have 60 shareholders, including 59 archdioceses and dioceses and Christian Brothers Risk Pooling Trust. National Catholic is pleased to welcome the Archdiocese of Indianapolis, Indiana, the Archdiocese of Portland, Oregon, and the Diocese of Birmingham, Alabama. We look forward to many years of years of service and friendship.

# Never just ‘minding your own business’ ever again

**EDITOR’S NOTE:** The following is a sample article from the subscriber portion of the VIRTUS *Online*™ website. This article is a training bulletin for adults. The subscriber area includes ongoing monthly training for all adults who have completed the Protecting God’s Children™ for Adults “live” training. It also includes monthly training for parents, trainers, investigators, victim advocates, and others who have completed specialized training from the Protecting God’s Children program or other components of the VIRTUS® programs. These are but a few of the many services provided to National Catholic’s shareholders and friends via our VIRTUS *Online* website at [www.virtus.org](http://www.virtus.org). For more information, call Jack McCalmon at 1-888-847-8870.

**By Jack McCalmon, Esq.**  
*Director of VIRTUS Programs and Services*

Approximately two years ago, my wife and I were on a business trip and we decided to walk through a shopping mall during some of our free time. Our otherwise pleasant experience came to an abrupt end when we witnessed something that, even today, disturbs me. In the open—for everyone on the same level of the mall to see—a mother was beating her screaming child.

When I write “beating” I mean beating. This was not a “swat” on the rear that I occasionally received as a small child. This beating consisted of repeated slaps to the child’s head, blows to the child’s back, and slaps to the child’s bare legs.

We both felt compelled to walk toward the adult and the child. While walking toward them, we couldn’t keep our eyes away from the scene. As we neared the mother, one of us asked, “Is that really necessary?” The mother, who was holding the child in the air with one hand so she could easily strike the child with the other, looked at us with rage.

“Mind your own %#\$@\*^& business,” the mother yelled at us. We continued to stare at her until, finally, she put the child down, grabbed the child by the arm, and walked away. Leaving, she muttered where we could “stick” our “self-righteousness.”

To this day, I am glad that we stuck our self-righteousness into her business. We interrupted something that a child should never have to experience from any adult—much less from her own parent. Although our actions created a confrontation and drew unwanted attention, it spared the child from continuing trauma—even if it was only for a brief moment.

The point of this training bulletin is simple. Most of us were taught to “mind our own business.” And, for the most part, that behavior has served us well. But when it comes to child abuse—including sexual abuse—minding our own business is what often allows abuse to continue. The abuser counts on us to mind our own business and not to ask questions.

When parents know the abuser, minding your own business is more difficult, because it is assumed that a parent is in the best position to protect their child. However, in some instances, the perpetrator has groomed the parent so that the parent routinely ignores obvious warning signs—physical or otherwise. In other instances, the perpetrator has so much influence over the parent—often in the form of intimidation—that the parent is afraid to come forward.

In the video, *A Time to Protect God’s Children*, a victim recounts how the person who abused him always visited with his mother at church and was very nice to her. Another victim, who was abused by a teacher, recounts how she couldn’t come forward because of a fear that her parents would side with the teacher (perpetrator) who claimed to be helping the girl improve her grades. The victim feared that if she did say something, her parents would only think that it was an attempt to avoid her tutoring session.

We know from our training that perpetrators provide warning signs (e.g., excessive touching, unusual or excessive gift giving, etc.). We also know that a perpetrator cannot abuse a child unless they can lure the child to a private location—a home, or even a private room or rarely visited location in a public building. When we see these warning signs, we must make it our business and report what we know.

Remember, it takes an entire community of adults—looking out for and intervening in suspicious adult-child behavior—to prevent child sexual abuse. When you consider the ramifications of child abuse and its long-term contribution to a number of other social ills, it’s easy to understand why protecting children is everyone’s business.



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