

# Expense Reduction Analysts Global Insurance Services

Global Trends in Corporate  
Governance, Compliance and  
Risk Management Best Practice



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**LONDON (Reuters) July 3, 2008—Banks need to rethink ways of managing risk, replace outdated technologies in the area**

As the credit crisis rages, financial services firms are seeking better ways to guard against unexpected losses.

The credit crunch has so far led to more than \$300 billion in estimated writedowns and credit losses, as well as steep falls in banks' share prices.

The lack of investment in control systems stems from the fact that, unlike trading systems, they do not generate profit for the banks. "Risk systems must give an early warning of anything that might hurt the profit,"

"Everything we know about managing risk is out of the window since August 2007,"

"We have to raise it to its proper place in corporate strategy, which is at the highest level where the risk manager will soon sit between the CEO and the CFO," he added.

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**Effective Corporate Governance**  
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**Focus on Risk Management**

**Determines the Winners and Losers**

Corporate governance is the way an organization is controlled and managed to achieve its objectives.

Risk is the chance of something happening that will have an impact on objectives.

Good Corporate Governance and Best Practice require business risk to be recognized and managed.

Effective risk management is critical to an organization achieving its objectives

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**What Risks Need Managing**

Treasury Risk – exchange rates	Human Resources
Governance	Information Systems
Business – bids & contracts	Financial Risk Management - Income & Expenses
Legal Compliance	Political Risk
Built Assets, Plant, Cargo	Advisor
	'Remuneration' Risk

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### Five Key Insurance Governance Questions

What to ask when it comes to effectively managing your General Insurance Program as a part of your Overall Risk Management Process:

- 1. Do I have a BROKER SERVICE LEVEL AGREEMENT?**  
Is your Broker Service Level Agreement structured to remove all possibility of contingent commissions and create an incentive for your intermediary to find the best coverage for the most economical cost?
- 2. How does my coverage and cost COMPARE TO INDUSTRY BENCHMARKS**  
How do the indemnity levels, deductibles, premiums and the fees you pay your broker compare to industry benchmarks?

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### Five Key Insurance Governance Questions

- 3. Do I have the most effective INSURANCE PROGRAM in place?**  
Do you have the best program structure in place to ensure price tension? Are there areas of overlap, duplication or gaps in cover?
- 4. Did my broker execute a POLICY RENEWAL REMARKETING?**  
Did your broker diligently remarket the renewal of General Insurance program to the most appropriate insurers last year?
- 5. Do I have an INSURANCE ADVOCATE?**  
Is your broker providing independent and unbiased advice or is he acting for the insurer/s with whom he places your insurance policies?

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### Broker Partnership

A good Broker Partner should:

1. Assist in identifying, assessing and effectively managing risk
2. Develop insurance program in line with your risk appetite and capacity
3. Technical advice on coverage and cost after analysis of loss experience and exposure
4. Market your business in the most favorable manner, leveraging existing relationships, market intelligence and global strength
5. Encourage tripartite relationships as insurers respond favorably to a collaborative approach

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### Is your Broker actually the Insurer's Agent

**Judge: Agents don't have to counsel clients about coverage**

NEW ORLEANS\_A federal judge says insurance companies don't have to tell clients who buy the maximum federal flood insurance about additional coverage available from other companies.

U.S. District Judge Patricia Minaldi dismissed the Cameron Parish School Board's lawsuit against State Farm Fire and Casualty Co. and agent Enos Derbome.

State Farm paid the system's \$8 million in flood insurance.

The board says Rita did more than \$26 million damage. It says State Farm knew it wanted the highest possible coverage, and should have explained how to get more.

Minaldi says that, since Hurricanes Katrina and Rita, federal courts have ruled that insurance agents don't have any duty to identify clients' needs and tell them if they are underinsured. Her ruling was handed down earlier this month.

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### "Get serious on reputation" warns Chairman of Lloyd's of London, Lord Levine

Extract from Risk Management May 2005

*"... in the case of the insurance investigation it's the issue of the broker receiving payment from both the client and the insurance carrier... suddenly the question of who is working for whom is blurred and confusing. But if we are to retain the confidence of the key player in all of this – the customer – we need full disclosure and complete transparency about who is doing what exactly, for whom, on what terms and at precisely what cost. Indeed, without it, you simply do not have the economics on which to base accurate, efficient, management decisions."*

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### IT Company Premium Summary

Professional Indemnity/Gen Liability \$10M (1)	\$355,136	54%
Directors & Officers (2)	\$101,286	16%
Property (3)	\$65,790	11%
Excess Professional Indemnity \$5M (1)	\$52,531	8%
Crime (Fidelity)	\$24,980	4%
Broker Fee	\$25,000	4%
Employment Practices Liability	\$11,814	2%
Travel	\$4,162	1%
Total	\$640,700	

Three coverages account for 89% of the total cost

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### Premium & Fee Savings Comparison

	Benchmark	Broker A	Broker B	Broker C	Incumbent
Premium	\$640,669	\$430,263	\$528,840	\$630,135	\$552,572
Saving		\$210,406	\$111,829	\$10,534	\$88,097

Estimated Benchmark	Broker A	Broker B	Broker C	Incumbent
\$80,000 (\$25,000 plus \$55,000 est. undisclosed Brokerage)	\$60,000	\$82,500	\$55,000	\$55,000
Estimated Saving	\$20,000	\$2,500	\$25,000	\$25,000

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### Program Review

**Insurance Program Structure - Professional Indemnity:**

Policy wording needs reviewing;  
 Level of deductibles needs reviewing;  
 Virus Exclusion needs reviewing;  
 Security Breach Exclusion needs reviewing;  
 USA sub limits need reviewing;  
 Activities Limitation Exclusion needs reviewing;  
 Section B Public and Products for individuals needs reviewing;  
 Breach of privity Limitation needs reviewing;  
 Issues raised by overseas operations need reviewing;

Fraud and Dishonesty sub limit needs reviewing  
 Inclusion of Defence Cost needs reviewing;  
 Policy design needs reviewing;  
 IP Blanket Exclusion for Patent Breach needs reviewing;  
 Related Entity Exclusion needs reviewing;  
 Punitive damages exclusion needs reviewing;  
 Contractor issues need reviewing.

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### Conceptual vs. Traditional Price Request for Proposal

- Always avoid a Price RFP because Insurers are **reserved** to the incumbent broker.
- Conceptual RFP provides for **NO INSURER CONTACT**.
- Brokers provide an **indicative renewal program** based on:  
**Current Program – Insurers – Covers – Deductibles – Risk Profile**
- The successful Broker is appointed on **program innovation, extent of covers and premium savings**.

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### The Conceptual RFP Process

Preferred Brokers are requested to provide a **conceptual outline of the insurance program they recommend**, the rationale behind their recommendation and the **indicative cost** of implementing the program.

Within this process the broker/s outline their credentials, industry specialization, consulting expertise, Insurer relationships, determination of Insurer claims paying ability and total quality management systems and technical ability.

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### The Practice of Reserving

The incumbent intermediary, broker or agent, has **reserved exclusively to him all the incumbent insurers on your current insurance program**.

Once he is told that you intend to go to a bid (RFP) process **he will also 'reserve' any other insurers which he feels will provide competitive terms, thus eliminating competition for your business**.

Any other brokers or agents participating in the RFP process can not access a quote for your account from these insurers who have been reserved.

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### Captives can substantially reduce costs and improve risk management

Captives can substantially reduce the net cost of risks by:

- > Carefully analyzing risk exposure;
- > Transfers unacceptable levels of risk to others via commercial insurance;
- > Compliments safety and loss prevention measures by establishing a formal profit center

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### Advantages of forming a Captive

- Participation in underwriting profits;
- Underwriting stability;
- Risk management;
- Availability of cover;
- Cost reduction – cycle elimination;
- Cash flow benefits;
- Taxation advantages and
- Reinsurance benefits