

VIRTUAL ROUND TABLE

CORPORATE *LiveWire*

INSURANCE & RISK MANAGEMENT 2015



MEET THE EXPERTS



Carol Lyons - McMillan
T: +1 416.307.4106
E: carol.lyons@mcmillan.ca
W: www.mcmillan.ca

Carol Lyons is co-chair of McMillan's Financial Services Regulatory Group. She advises clients on a variety of corporate/commercial matters, including mergers and acquisitions, corporate reorganizations, contract procurement, and formation of strategic alliances. Carol specializes in working with clients in the insurance industry and her practice includes assisting insurers and reinsurers with transactions and regulatory matters. Carol is Chair and sits on various Committees of a leading Canadian reinsurance company that is a subsidiary of a multi-national reinsurer, past Corporate Secretary of two Canadian property and casualty companies, Advisory Board Member and Audit Committee Member of an Ontario insurance reciprocal and participates on various charitable boards.



Mark Goodman - Freeborn & Peters LLP
T: +1 312 360-6729
E: mgoodman@freeborn.com
W: www.freeborn.com

Mark Goodman is a Partner in Freeborn & Peters LLP's Corporate Practice Group. He has three decades of experience advising the insurance industry on corporate, regulatory and transactional matters. He has represented a wide range of clients in complex, high-profile matters, including insurance holding companies, insurers, producers, agents and brokers, and managing general agents. He also advises non-traditional sellers of insurance on insurance programs, including trade associations, retailers, banks and savings associations, and leasing and finance companies.

Mark has handled significant acquisitions and sales of insurers and brokers and acquisitions and sales of books of insurance business through reinsurance and other arrangements. He has the flexibility to efficiently handle unique and more unusual matters, from establishing a pet insurance program to the establishment of a private health insurance exchange. He also works regularly with issuers of extended warranties and service contracts, captive insurers and risk retention groups/risk purchasing groups, and specialty program managing general agents.



Paul Wordley - Holman Fenwick Willan LLP
T: +44 (0) 20 7264 8438
E: paul.wordley@hfw.com
W: www.hfw.com

Paul Wordley is global head of HFW's international Insurance and Reinsurance Practice Group. His practice is geared towards dispute resolution and coverage issues in the international insurance and reinsurance markets, acting for insureds, insurers, brokers, intermediaries and reinsurers.

Paul has been involved in a number of high-profile international disputes in recent years, including the Lloyd's litigation, the Svenska Kredit reinsurance litigation, the ME Ratty Pool disputes, the Kennecott insurance/reinsurance coverage and brokers negligence litigation, the Ericsson contingency business interruption claim, high profile regulatory proceedings at Lloyd's, arbitration proceedings arising from the September 11 terrorist attacks, as reinsurance counsel to a major Scandinavian insurer bankruptcy, claims arising out of the December 2004 tsunami and claims arising out of Hurricane Katrina. He has also advised on a number of recent mining claims, issues arising out of recent natural disasters in many parts of the world and is a leader on advising on issues related to the setting up and management of captives.

Paul has significant mediation experience, having represented clients in several successful multi-million dollar mediations.



Rachel Levitan - Levitan, Sharon & Co Law Offices
T: +972 3 6886769
E: rachellevitan@levitansharon.co.il
W: www.levitansharon.co.il

Rachel Levitan, LLM is the founder and senior partner at Levitan, Sharon & Co Law Offices.

The firm is a leading specialist in insurance and reinsurance matters.

The law firm handles all aspects of insurance and reinsurance matters.

In the last five years Adv. Levitan has focused mainly on advising insurance and reinsurance companies regarding complex D&O and BBB matters, as well as advice on reinsurance topics. Adv. Levitan has advised both reinsurance and local cedents.

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Gregory L. Dillion, Esq. - Newmeyer & Dillion LLP
T: +1 949 854 7000
E: greg.dillion@ndlf.com
W: www.ndlf.com

Mr. Dillion is a founding partner of Newmeyer & Dillion LLP, a Best Lawyers top tier law firm. He represents businesses in complex business, construction, real estate and insurance disputes. He is rated by Martindale-Hubbell as AV Preeminent and recognized by Best Lawyers in Construction, Insurance, Commercial and Real Estate Law and litigation and named by it as Orange County's Real Estate Litigation and Insurance Law Lawyer of the Year. He also is recognized by Super Lawyers as one of Orange County's top 50 and one of Southern California's top 100. He received his B.A. from Cornell University and his J.D. from the University Of Texas School Of Law.



David Kearney - Wotton Kearney
T: +61 2 8273 9916
E: david.kearney@wottonkearney.com.au
W: www.wottonkearney.com.au

David Kearney is Chief Executive Partner of Wotton + Kearney. With offices in Sydney, Melbourne and Brisbane the firm has established itself as one of Australia's leading insurance firms.

David is recognised in the 2013 Chambers & Partners Asia Pacific guide as a leading insurance and dispute resolution lawyer and for his "enviable reputation in the insurance space" in the Legal 500. His areas of expertise include PI, public and product liability, and construction and contract works claims. He has acted in a large number of high value, complex claims for a range of clients in Australia and overseas.



Joseph L. Petrelli - Demotech, Inc.
T: +1 614 595 3516
E: jpetrelli@demotech.com
W: www.demotech.com

Joseph L. Petrelli is the President and Founder of Demotech, Inc. Organized in 1985, Demotech, Inc. is a Columbus, Ohio based financial analysis and actuarial services company. Demotech, Inc. provides services to regional insurance companies, title underwriters, risk retention groups and specialty insurance markets. Financial Stability Ratings® of A or better are accepted by the secondary mortgage marketplace, virtually all mortgage lenders and an increasing number of umbrella insurance markets, insurance agents errors and omissions insurance carriers, hospitals and other informed third parties.

Prior to forming Demotech, Petrelli was employed by Nationwide Mutual Insurance Company, Countryway Insurance and ISO. Petrelli is a member in good standing of the Casualty Actuarial Society, American Academy of Actuaries, the Conference of Consulting Actuaries and the Society of Financial Examiners.

Petrelli and his wife, Sharon, reside in Columbus Ohio. They have two adult children, Vickie and Joe, and four grandchildren, JJ, Marissa, Luca and Ellis.

Insurance & Risk Management 2015

In our Insurance & Risk Management Roundtable we spoke with seven experts from around the world to discuss the latest changes and key strategies being implemented in their jurisdiction. Our chosen experts have looked at a range of topics including the cyber risks, and the consequences they can have on a business, to help businesses navigate the increasingly complex landscape of risk management.

1. Can you outline the current insurance & risk management landscape?

Petrelli: Excellent question for the group! There are paradigm shifts taking place on both the insurance and risk management landscapes. In the insurance landscape, alternative capital has discovered the property reinsurance marketplace. Primary carriers are utilising the availability of alternative capital, whether catastrophe bonds or other insurance linked securities, as an alternative to traditional reinsurance to save money and to leverage reinsurance rates per se. Concurrently, as reinsurance rates soften, multi-billion dollar reinsurers are evaluating or initiating merger opportunities to remain profitable as well as to remain relevant in the marketplace. As to risk management, changes in the level of documentation and corporate cultures are being driven by enterprise risk management and the implementation of the National Association of Insurance Commissioners Own Risk and Solvency Assessment process. These two emerging issues will reshape the insurance. The next generation of leaders should be watching, studying and understanding these phenomena.

Goodman: In the United States the insurance landscape is marked by continued soft market conditions in the property and casualty sector, distribution and generational challenges for the life and annuity industry, and rapid consolidation in the health insurance market such that we may end up with fewer than a handful of health insurers by year-end, creating a near oligopoly.

Wordley: Focus on holistic risk management i.e. across the whole organisation. Corporate governance driving the need for decisions about how to deal with risk – don't assume it in the first place, retain it, but manage it or transfer (insurance).

Lyons: Almost everything today has a “risk based” element to it. Although there are many possible perspectives on this question (e.g. publicly-traded companies, governments and government agencies), I am tackling it from the viewpoint of regulated risk management of insurance companies. Insurers in Canada are required to implement a system of enterprise-wide risk management that identifies the inherent risks in their activities and manages those risks to appropriately defined

levels. Regulatory reforms that address risk management of insurers and other financial institutions have dominated the landscape in Canada over the past few years. Recent initiatives put into place by Canada's federal insurance regulator include:

A. A revised guideline on Corporate Governance that requires, among other things:

- a board-approved Risk Appetite Framework;
- hands-on involvement by senior managers in risk management policies and practices;
- in appropriate circumstances, establishment of a dedicated Risk Committee; and
- appointment of a Chief Risk Officer with unfettered access and a functional reporting line directly to the board or Risk Committee.

B. A revised guideline on Regulatory Compliance Management, which communicates the regulator's expectations with respect to the management of regulatory compliance risk by insurers. The guideline makes the board of directors ultimately responsible for effective enterprise-wide regu-

latory compliance management and mandates a Chief Compliance Officer. Internal audit (or other independent review function) is to validate the effectiveness of, and adherence to, the insurer's compliance framework by regular “risk-based” testing.

C. A new guideline on Own Risk and Solvency Assessment (ORSA) that outlines the regulator's expectations with respect to the insurer's own assessment of its risks, capital needs and solvency position, and for setting internal targets based on the insurer's ORSA. The ORSA guideline also addresses the scope of the ORSA, its relation to enterprise risk management, the role of the board, senior management and other participants in performing, monitoring, reporting or reviewing the ORSA, and other key elements of the assessment process.

Dillion: The insurance marketplace continues to increase capacity with rates remaining somewhat stable. New capacity continues to come on-line especially in Bermuda fuelled by the private equity markets. This could change relatively quickly based on the recent wave of merger and acquisition activity in the healthcare and property

& casualty segment. Further the use of captive insurance companies for more discreet risks, including workers' compensation, is becoming more effective. The reinsurance markets are still relatively sensitive to risks with catastrophic exposure such as cyber risk, regulatory risk and hurricane, earthquake and flood exposed areas.

Kearney: It is probably fair to say that the Australian claims market remains relatively quiet. This is driven predominantly by a benign catastrophic claims experience in our region and a result of the slowdown of post GFC claims with many professional indemnity and financial lines matters having run their course. Management liability claims continue to provide a challenge for many insurers both from a product development point of view (clashes between insureds and insurers about what the cover "ought" to provide) and claims management perspective; primarily EPL and statutory liability. In the casualty insurance space there remains a steady flow of occupier's liability cases, particularly from owner/operators of retail premises, operators of licensed premises and those involved in the construction industry.

2. Have there been any recent regulatory changes or interesting developments?

Goodman: The costs and difficulty of complying with the Affordable Care Act ("Obamacare") appears to be driving the consolidation of the health insurers, as well as hospital groups and doctor groups, in what may be an unintended consequence of the law. The other regulatory development of note is discussion of government mandated data security requirements for insurers and their customers – ironically, at a time when the governments are being victimised by hackers.

Wordley: Solvency II continues to influence corporates with captives. Financial institutions very interested in adding independent NEDs with legal qualifications.

Lyons: A political war is waging in Ontario over automobile insurance rates. The Ontario government passed legislation in 2013 mandating a 15% overall reduction in automobile insurance rates. To try to make up for it, the government passed additional legislation in 2014 designed to reduce the cost of claims for insurers, including anti-fraud measures and streamlined consumer-insurer dispute resolution. Ontario automobile insurers are complaining that the 2014 legislation has not and will not sufficiently mitigate against the mandatory rate reductions, and some are calling for a complete overhaul of

the Ontario automobile insurance regulatory framework as well as the province's regulatory body (Financial Services Commission of Ontario).

The province of Saskatchewan has just revamped its insurance laws by passing *The Insurance Act*, designed to modernise requirements and harmonise provisions with the insurance statutes in Alberta and British Columbia. Changes revolve around, among other issues, fair and unfair practices, insurance intermediaries and self-evaluative audits. Key regulations have yet to be drafted.

The Canadian Council of Insurance Regulators (CCIR), which is made up of the Canadian provincial and territorial superintendents of insurance and a representative of the Canadian federal regulator, identified a number of priorities and strategic initiatives in its *Strategic Plan* for 2014-2017. The planned initiatives include:

- reviewing the travel insurance industry in Canada including activities of call centre support providers, policy wordings and exclusions, and adequacy of information provided to consumers (both on-line and in-person);
- reviewing and addressing the continuing issues that arise out of the use of technology, such as electronic "pink

cards" for auto, telematics (as an underwriting tool), claims handling, underwriting and data collection;

- considering enhanced methods for ensuring financial literacy so that consumers make informed insurance choices;
- reviewing the regulation of individual variable insurance contracts and assessing potential regulatory arbitrage, e.g. vis à vis the parallel regulatory framework for mutual funds;
- developing a common understanding with pension regulators, policy makers and pension and insurance stakeholders with respect to longevity risk transfer markets in Canada; and
- reviewing policy wordings for property insurance and disclosure issues relating to natural disaster coverage.

Dillion: The Consumer Financial Protection Bureau has only had a few years to make its presence known but has extracted significant penalties from a wide range of institutions, primarily financial. These risks are material to any company's balance sheet and must be examined carefully, both in terms of identifying processes that expose a company to outside risk as well as regulatory threats that can be partially addressed through insurance and other risk transfer mechanisms.

Kearney: Probably the biggest issue

for insurers, but a sleeper in many respects, is the increasing value and prominence of fines and penalties for civil liability offences under the ASIC Act, State OH&S Acts, FWA, Credit Act and CCA. This will continue to be a big challenge for insurers given the increasing propensity to offer fines and penalties cover in financial lines policies.

3. What risks are most likely to affect businesses, and which of these would have the biggest financial consequences were they to occur?

Petrelli: In terms of emerging issues, cyber liability, data breaches and related access to and the abuse of personal information have the biggest impact and capacity to create widespread financial consequences – for the consumers involved and for the entities that were unable to safeguard the information. Despite daily headlines of government agencies, health insurers and international retailers being hacked, I believe that the amount of protection purchased and standards for internal safeguards on IT infrastructure are woefully lacking. While the headlines have indicated that the number of records hacked can be staggering and the amount of information obtained incredibly detailed, I suspect that soft targets – restaurants, vendors, insurance agents, blue collar trades people

utilising credit cards, etc., – will eventually be targeted.

Goodman: Data security requirements, including cyber risk management and reporting requirements, will greatly affect the operations of both insurers and their customers, and drive up costs.

Wordley: Cyber risk is the big one that concerns clients in respect of management issues (take overs) and client confidential information and key operating risks e.g. powergen, utilities and automated processes/operations which can be remotely controlled.

Levitan: The risks may be divided into two categories:

(a) Acts of God – Hazards of Nature, earthquake, floods

(b) Manmade acts – fire, burglary, theft, embezzlement, cyber risks

The risks in (a) are catastrophic risks which may lead to a total collapse and loss of the business as a whole and its rehabilitation may require a long period. Even the individual person can protect himself vis a vis these risks at a very low level (e.g. in Japan which is very well prepared for earthquakes, the tsunami which occurred following the earthquake caused by the Fukush-

ima disaster). Therefore, the insurance for businesses should be for very large amounts which should also take into account the period of rehabilitation.

The risks in (b) except for fire, are not total loss risks and the emphasis should be placed on safety and protective measures to avoid the risk and a constant examination thereof during the period of insurance (for example: change and/or update of the sprinkler system and changes in firewall as a security against cyber attack, and constant audits and inspections in order to uncover embezzlement). For these risks the insurance should take into account the ability to rehabilitate the business and whether partial operation thereof is possible, etc.

The steps to be taken should be in accordance with the nature of the business of the client, e.g. if the client has a big fleet of cars, there is less need to insure damage to the cars but rather insure against damage to third parties.

As to the cyber risks, it has become more and more common that the biggest assets of the business are the human resources and the information of the business. A big risk is any harm caused to the information data, loss or theft of the data or an unauthorised use thereof.

Dillion: Cyber liability continues to be the biggest issue in the industry. Cyber has received a great deal of coverage given the issues encountered by Target, Sony and Anthem to name a few. Although the insurance industry has products to address the issue, many offerings included significant exclusions that might not provide coverage at all. Not far behind are regulatory risk, currency risk and wage and hour benefits risk.

4. How should different type of risk be audited and governed?

Levitan: The audit of the various risks is in accordance with the nature thereof, however any business should map out the risks and ask, for example in cyber risks, who may have access to the information from within the business or from outside. As to measures for avoiding the risks, the business should install security and safety systems, should give instructions to the employees, and control an audit on their work after setting written work procedures. Any business should prepare tools to handle any such risks and mitigate the damage. This also should be done according to written procedures and insurance.

The control and audit should be carried out constantly and a responsible

employee or committee should be appointed for this object and of course these operations should be regularly inspected by the management.

Dillion: Companies should focus on various measurement conventions, such as those provided by companies like Protiviti and the updated risk management protocol published and effective this year. Each potential risk should be considered and all activities of the company need to be analysed to determine how they might create risk, and a risk management team must then be formed that is composed of those with the expertise to address each of the risks identified. Governance should be cyclical and published so that all executives, middle management and others are aware of when risks will be audited and what steps should be taken in the interim to minimise risk.

5. What role can insurers have in driving improvements in cyber security risk management?

Petrelli: Although insurers should be encouraged to develop meaningful coverages that provide funds or assistance to consumers and businesses that have been hacked, i.e., attempt to unring the bell, the reality is that insurer options to drive improvement are somewhat limited. Premium differentials

based upon an insurer's assessment of the underlying cyber security risk management at a risk/insured must be approved by the respective departments of insurance. Although the insurance industry can accept or reject cyber risk based upon the insurer's underwriting criteria and its assessment of the consumer or business's cyber security, we may be approaching a situation where the tail of cyber liability might wag the dog of account acceptability. In other words, would an insurer decline a business owners policy, farmowners or commercial multiperil policy that has been profitable or is properly priced simply because the insured or prospective insured now requests cyber liability insurance and presents below average risk management function for this aspect of its exposure and therefore above average exposure to the insured? Will susceptibility to cyber liability become an underwriting criterion as opposed to an opportunity to provide another coverage to the insured?

Goodman: One of the advantages for an insured that goes through the somewhat painful application and underwriting process for cyber insurance is to focus them on risk management steps they should be taking. The detailed application process, along with discussions with brokers and under-

writers, can change the application and underwriting process from a chore into a learning experience. It is helpful to insureds when underwriters explain clearly the reasoning behind their questions and what best practices they would prefer to see.

Wordley: It is difficult as insurers may be a problem when there is a claim i.e. reserve their position on coverage. Legal advisers/insurance brokers will drive a proactive approach to cyber audit, breach response crisis planning and breach response crisis management.

Levitan: In cyber risks the insurers may have accumulated information concerning the ways to secure against these risks and they should transfer this know-how to the insureds by setting requirements for safety tools, security and inspection.

I may suggest that any insured who introduces such a plan should be encouraged by a reduction in the premium. Seminars for clients and newsletters sent by email are a very effective way through which the insurer may assist the insured in managing this risk.

Lyons: Insurers and other insurance professionals have traditionally been excellently positioned to drive im-

provements in risk management processes generally. Cyber security risk is a relatively new phenomenon, having arisen hand-in-hand with the electronic information and internet age. It is just one additional area where the insurance industry can play a key role in educating and equipping public or private sector organisations with respect to managing this emerging risk.

At one point in time, organisations may have assumed that losses due to cyber attacks or data/privacy breaches would be covered under their commercial general liability (CGL) policy. But, today, most CGL policies specifically exclude these risks, as they are perceived to have the potential to lead to an endless abyss of incalculable losses.

On the other hand, due in part to general overcapacity in the global insurance marketplace, insurers and reinsurers are looking to new products as avenues to increase business, and some are developing an appetite for cyber risk. Hence, specialised cyber risk insurance policies are now available, and are specifically designed to respond to losses due to a cyber attack or such things as privacy or data security breaches. But the scope and limits of coverage will necessarily be subject to the underwriter's due diligence regarding the nature and extent of the

risks they are assuming.

This means that insurers and the large institutional brokers that work with them have been working hard to gain as much expertise as possible with respect to assessing and managing cyber risk. They have had to acquire this expertise in order to calculate a potential insured organisation's exposure to these risks and assess its preparedness and ability to implement appropriate and effective measures to mitigate losses that may occur (to make coverage decisions and price the risk). Elements of this expertise are passed along to the insured organisation because to do so aligns the insurer's interests with the insured organisation as it relates to management of what is now the insurer's risk and, in turn, helps to keep premiums under control.

Organisations that, due to the nature of their operations, are vulnerable to cyber attacks or privacy or data security breaches and that wish to acquire insurance coverage against these risks should be prepared to demonstrate to the insurer that cyber risk is an integrated part of their overall enterprise-wide risk management processes and that appropriate risk management tools and processes are in place. They may do so by acquiring this expertise from the insurer and the broker. Oth-

erwise, the likelihood of obtaining coverage at a reasonable price is remote. Insurers, brokers and other insurance specialists will be involved in the process in order to analyse the risk as well as the effectiveness of the measures in place to mitigate losses. In this way, the insurance industry drives improvements in risk management.

Dillion: Insurers will mandate controls, upgrades and specific protocols for security and incident response as a condition of coverage. They may also require companies to utilise outside cyber security firms to implement systems company wide. They will provide coverage only to companies that incorporate mandated changes to their systems and the policies will include a number of exclusions. Current policies have large coverage gaps that companies may not discern until a claim occurs.

Kearney: Cyber insurance continues to be one of the headline topics in insurance. We are seeing increased measures by insurers to introduce cyber cover into traditional policies or to develop cyber-specific products. This is in response to the growing demand for organisations to undertake protection against cyber-risks and gaps in existing policy coverage. Insurers can drive improvements in cyber security by re-

quiring insureds to take reasonable precautions to improve their security measures as a condition of insurance cover. This may involve setting minimum standards around passwords and requiring reasonable updates to security software. As premiums are calculated according to the level of risk, insureds also have an incentive to improve their cyber security as this will likely lower the value of their premium.

6. What procedures should a firm take when outsourcing or contracting work which contains important data and security, and are there any legal or regulatory requirements that need to be taken into account?

Petrelli: An emerging verification criterion or consideration with regard to outsourcing or contracting work containing important data is to require that the vendor or contractor have successfully fulfilled the requirements of and can provide a Statement on Standards for Attestation Engagements 16, a protocol associated with an independent verification. The statement of controls may consist of a SOC 1 report, SOC 2 report or SOC 3 report. Traditionally, publicly traded carriers have requested these of their vendors. The specific situation under review determines whether a SOC 1, 2 or 3 would be applicable. For a smaller business, the

annual cost of a review and report can be equivalent to the cost of a part-time employee.

Wordley: Procurement requirement that data protection/safeguarding is equivalent to the firm doing the outsourcing. Most countries now have or are moving towards data protection legal requirements/regulatory oversight.

Levitan: In any dealing with an external supplier who receives sensitive information from the business, it is very important to ensure that the information is held by the external supplier in a secure mode and that he is able to protect the information. As to private businesses, they owe the basic duties of privacy, fiduciary duty towards clients, a duty of care, etc. A specific regulation under Privacy Law provides that the duty to secure the information, applies to both the original data holder and the service provider.

Regarding institutional investors and banks. In August 2013 (with effect from July 2014) the Ministry of Finance, the Department of Capital Market, Insurance and Saving, issued a directive of "outsource in Institutional Investors" which set rules for the use of outsourcing in these entities. Under these rules any Institutional Investors' entity should establish a policy for outsource-

ing its activity which would set ways of control and survey of the activity by the service provider under written agreement which ensures confidentiality, data security, periodical audits etc. The rules apply to Banks, Insurance Companies, Pension Funds etc.

Dillion: The firm outsourcing remains responsible for the security of the data turned over to the outsourced entity. Accordingly, the service level agreement that accompanies such outsourcing must be written carefully to protect the outsourcing firm, transfer risk and provide immediate legal remedies in the event of an incident at the outsourced entity. Liability also can attach to the outsourcing firm if it fails to audit the security procedures and protocols employed by the outsourced or contracted entity.

7. Can you talk us through the necessary safeguards and protocols to mitigate risk?

Wordley: See slides 1 -3.

Dillion: This is a subject for which there is no shortage of consultants and experts, more than a few self-appointed. The most important safeguard is to have the correct team of people internal to your enterprise who understand the common sense approach to

identifying risk in setting up protocols to minimise the likelihood of its occurrence and to further minimise or mitigate the damage of a risk incident. There are a variety of governmental resources published protocols and any number of proprietary products that may be used.

8. Why is it important to differentiate between risk analysis and risk management?

Petrelli: When I ask my grandchildren to do something and they agree to do so yet the deadline for completion passes without action, I remind them that ‘talking ain’t doing.’ I differentiate the two terms risk analysis and risk management as ‘talking’ and ‘doing’, respectively. Risk analysis is a preliminary step in the risk management process. It is necessary but it is not sufficient. Getting it done or at least moving toward a solution is implicit in the term ‘management’. From my perspective, the critical link between analysis and management is that the analysis component should create a sense of proportionality in the management phase so that you prioritise your time commitment. If you have limited resources, spend them where you get the superior return.

Wordley: Risk analysis consists of risk

identification, evaluation and qualification.

Risk management is the conscious decision making process once risks have been analysed. Informed decision making – manage, retain or transfer.

Dillion: Risk analysis is the business of identifying and studying the risks a company may create on its own or encounter in its operations and thoroughly dissecting the elements of each risk and what impact it may have. Risk management is the establishment of audit and review procedures and protocols to ensure the company maintains diligence in monitoring for risk and that management is committed to the process and that employees are educated in the identification and referral of risk incidents to those best positioned to manage them. You can’t manage properly that which you don’t understand.

Kearney: Risk management without proper risk analysis is a flawed approach which could be catastrophic to a company’s bottom line. Risk analysis involves detailed consideration of business risks which are rarely static and often involve a level of “imagination” to ascertain the nature and gravity of that risk.

Risk management involves the implementation of strategies to minimise or negate the prospects of a risk emerging and/or the financial consequences of a risk which crystallises into an adverse incident. Risk management can include both risk avoidance strategies (often changes in business process to ensure a risk can’t emerge) and risk mitigation strategies such as risk transfer (i.e. through commercial insurance).

9. To what extent is there a culture amongst board of directors to consider risk management as a luxury rather than a necessity, and why is it a grave error to possess this mind set?

Petrelli: With respect to the fine boards of the past, it seems to me that the more effective boards have changed their role and perspective. Other business cycles and eras have permitted, maybe even encouraged, boards to be passive in their interaction with key personnel. More recently, there have been revisions to corporate regulations as well as substantive changes in the procedures and practices of the independent parties that tend to report to boards. Two such examples are changes in the breadth and scope of statements of actuarial opinion as regards loss and loss adjustment expense reserves as well as changes in the breadth and scope of independent audits. There are dozens

of highly rated (by others than Demotech) insurers that self-report chronic loss reserve inadequacy. Although the level of reserve inadequacy does not appear to impair their solvency, it has a definite impact on the quality of their previously reported earnings. In my opinion, balance sheet integrity and quality of earnings should be a board level issue. How can one manage the risks associated with an insurance company if one does not first manage the integrity of the insurer's loss and loss adjustment expense reserves?

Goodman: In my experience that kind of mind set is a thing of the distant past for most corporate boards. I think that boards understand that while implementing business strategy is a function to be carried out by the officers, overseeing that implementation and guiding and analysing risk management is a key board function. There are enough examples from recent history, both before and as a result of the financial crisis, that teach board members that lack of adequate focus on risk management can be fatal. What is new is the types of risks that a company faces, from cyber risks to terrorism risks to risks from government fiscal calamities, but the overall need for board to focus keenly on risk management is something most board members have embraced.

Wordley: Some truth in this. Changing as a result of 2007/8 GFC. Most corporates taking corporate governance and risk identification/management seriously. Increasing demand for lawyers as NEDs.

Dillion: To the extent there has been a culture among board directors to consider risk management as an unnecessary expense, the very public examples and consequences of such a culture ranging from financial disasters such as the London Whale, to the facilitated tax fraud of international banks, to the blithe violations of the Foreign Corrupt Practices Act, to the more recent cyber incidents have killed that culture.

10. Can you talk us through the process of structuring multinational insurance programs?

Goodman: Structuring multinational insurance continues to be a challenge, given different insurance regulatory schemes throughout the world. Insurance company licensing requirements in different jurisdictions makes it difficult to use a single insurer, or even a single insurance company group, to meet all of an insured's needs.

Wordley:
(1) Identify core policy/coverage

wording;
(2) Structure (re)insurance layers;
(3) Ascertain local fronting requirements and arrange;
(4) Ensure contract certainty and consistency of risk transfer;
(5) Consider role of captive-financial mechanism as true insurer.

Levitan: The steps towards building such an insurance coverage would be first of all to carry out a risk analysis and an examination of the needs in each of the countries which are relevant to the insurance. Secondly, scrutiny of the applicable laws (especially in the field of employment laws, pensions, privacy protection, etc.) which vary from state to state. Thirdly, one should check the legal requirement in respect of insurance in any of the states: whether the insurer should be locally domiciled, or whether the policy may be issued by a foreign insurer and what policies are common in each of the countries. For example, whether it is common to insure a product on an occurrence basis or on a claims-made basis.

Above all this, one should check the advantage of having a global policy, both in regards to premium and wording of the policies compared with local policies with a second layer of a global policy which contains a drop down element.

11. How do you difference between political risk, political violence and terrorism insurance?

Wordley: Different insurances completely - pick specialist brokers.

Dillion: Political risk refers to the complications that businesses may face as a result of political decisions such as currency devaluation, nationalisation, and confiscatory taxation and regulation.

Political violence can be physical or mental and take a number of forms including war, police brutality, torture, genocide, and capital punishment. Non-action by the government can also be characterised as a form of political violence.

Terrorist activities can be violent acts or the threat of violent acts perpetrated for economic, religious, political, or ideological goals. Acts of Terrorism – covered by terrorism insurance are acts certified by the U.S. Government to be dangerous to human life, property, or infrastructure and to have resulted in damage within the U.S. and committed to coerce U.S. civilians or influence policy or conduct of the U.S. Government through coercion.

12. Can you outline the risk and insurance implications to companies with subsidiaries in Greece?

Wordley: See Grexit bulletin.

Dillion: RESPONSE A:

There are risk and insurance implications of Coverage, Premium Flow, and Claims.

COVERAGE: Current policy coverage would continue in the absence of any clause stating that cover would cease in the event of Greece exiting the European Union (EU). Greece currently allows EU Freedom of Services (FOS) policies, meaning that non-compulsory lines of cover for Greek assets and operations can be arranged outside of the country. If Greece were to rescind FOS legislation, local policies with locally-paid premiums would be required under global covers arranged outside of Greece, assuming the country were to prohibit non-admitted policies.

PREMIUM FLOW: Premium flow would continue in the contractually-agreed policy currency until amended. Additional and return premiums mid-policy term would also be paid in the agreed policy currency. A Greek insured would need to buy euros to make additional premium payments.

In the event of Greece exiting the EU, local policies issued under global programmes arranged outside of Greece would be able to show values, premiums, etc. in any new Greek currency

CLAIMS: Claims will be paid in the contractually-agreed currency. In the absence of a local policy, any implementation of exchange control legislation may have an impact if a claim is to be paid by an insurer based outside of Greece. If Greece were to exit the EU, and a claim is made post-exit under a global claims occurring-based liability policy for a pre-exit period, then the pre-exit policy terms and conditions will apply, with limits applying in the contractually-agreed policy currency. Notwithstanding, any damages may be stated in any new Greek currency.

Dillion: RESPONSE B

Greece will continue to struggle for some time. This is not just based on the specific Greek situation but the additional issues the EU faces with other countries. Most companies with subsidiaries in Greece face a business interruption exposure. This was tested recently with the shutdown of the Greek banks as well as the limitation imposed on their clients. Most companies that import goods into Greece were unable to take delivery because they were unable to pay for the goods

and raw materials. Companies will continue to struggle finding and training employees as many will choose to leave rather than stay and face atrocity. Further, the payment of premiums and claims may become complicated in terms of currency if Greece should exit the EU.

13. What key trends or strategies do you expect to see come to fruition over the coming year?

Petrelli: Demotech believes that a key trend in insurance is a move even further toward a barbell structure. Larger companies and smaller, niche players are at the ends with mid-sized companies being squeezed in the middle. The mid-sized companies must compete against the name recognition, capital and operating efficiencies of the giants while simultaneously being responsive and supportive of the needs of consumers and insureds that require the high level of personal service and consultancy associated with smaller insurers. An example of this situation exists in the United States domestic property and casualty insurance industry. If you count captive insurers, mutual protective associations, farm mutuals, risk retention groups, self-insured pools, public and private stock companies, mutuals, reciprocals and all risk bear-

ing entities operating in the US, there are likely to be more than 8,000 such entities competing for P&C business. 10% of these companies, 800, write in excess of 90% of the direct premium written in the US. 90% of the companies by count compete for less than of the business written!

Goodman: Continued consolidation among insurers and brokers is a trend that I do not think will abate, both within major markets and worldwide. The consolidations are being pursued not only to achieve economies of scale but also to pursue new opportunities by acquiring expertise and market access.

The other trend that I expect to continue is the role of private equity and hedge funds in providing capacity in the insurance marketplace, both through backing insurers and brokers and offering insurance linked securities and similar risk management tools. While some within the industry have decried the impact of this "alternative capital," I think that the better way to look at this development as a broadening of the sources of capital, which should bring both innovation and competition to the industry, and in the long run benefit consumers.

Finally, we can expect both the con-

tinuing use and acceptance of telematics in automobile, trucking and other insurance underwriting decisions, and at some point a regulatory pushback based on complaints that such underwriting invades consumer privacy and creates a bifurcation in the market that may disadvantage a large number of insureds.

Wordley: Emergence of cyber risk as the key coverage based on increasing awareness (Ashley Madison, Sony, Carphone Warehouse, US NSA attacks).

Increasing role of lawyers as NEDs.

Lyons: There is a recent trend of consolidation in the insurance industry in Canada, including insurers and the broker community as well. These transactions are often a Canadian component of multi-national transactions.

On the insurance product development front, longevity risk transfer transactions are cropping up in Canada, with a

major transaction involving the “transfer” of pension benefit liabilities of approximately Cdn. \$5 billion occurring in 2015. The first of these types of transactions occurred in Canada in 2013 and involved a Cdn. \$150 million annuity policy that transferred pension risk to a life insurer.

In a recent address to the property and casualty industry, the Canadian federal Superintendent of Financial Institutions indicated his office’s concern over an apparent trend of large cessations of commercial risks, particularly to unregistered affiliates, without any change in net risk retention. The Superintendent indicated that he is currently assessing the scope and potential impact that these recent changes in reinsurance practices may have on cedent solvency.

Insurance-linked securities (ILS) such as catastrophe bonds, as an alternative source of reinsurance capacity, are slowly creeping into the Canadian market. Although there has yet to be

a Canadian ILS issue, Canadian risks are increasingly becoming part of the covered risks in respect of issuances in other jurisdictions.

Dillion: Regulators are requiring business to acknowledge greater responsibility for risk management. Regulatory Deadlines must be known and attention must be paid, especially in the banking industry. Cyber security and risks are currently moving to the top of corporate agendas. Companies continue to increase their use of third party vendors – thus vendor management is increasingly important. It will be important to improve contract management and evaluations and assessments of all vendors. Expect to see greater staff shakeup. Recruiters are looking for stronger executives who understand the new operations risks, cyber risks and compliance issues. Companies resistant to this change will face many hurdles over time. Good risk management talent will decrease. Companies will be required to find more creative

ways to deal with their risk management and compliance issues.

Kearney: While specific trends and conditions will tend to vary for different lines of insurance, a common theme expected across the Australian insurance market is the pressure on pricing. This will largely be due to the continuation of softer market conditions which spurs increased competition. A number of new entrants, mergers and on-line based challenger brands are also expected to be extremely aggressive towards winning new business which will keep established policy providers on their toes.

There is no question that the issue of cyber security will continue to be in the spotlight with an even greater emphasis on educating businesses and organisations to be aware of the implications relevant to their industry and to ensure suitable insurance cover and mitigation processes are in place.

