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JLT SPECIALTY LIMITED
Q1 2015

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The losses that struck the aviation insurance market in 2014 have left the sector in something of a fragile state as it moves into the new year.

The aviation insurance industry has been left in a fragile state following on from the losses that hit the market in 2014, according to the chairman of JLT Specialty’s aerospace division Nigel Weyman.

Following on from the claims that struck last year, Weyman predicts insurers will fight hard to preserve the progress they made in imposing rate increases in 2014. But, the surplus of capacity that resides within the sector means there is already pressure on rates to come down again. Furthermore, those insurers who lost market share during 2014 will be doing their best to reclaim it.

“This will add a tension to the rate levels and could result in some easing off of the premium levels, particularly as there is some disparity of rating between the renewals of the first and of the second half of the year,” said Weyman.

“However, recognising the marginal year that most insurers will have had in 2014, particularly those with the double loss [on both Malaysia Airlines disasters], any adverse loss experience in the early part of the coming year could have an impact on what happens. It remains a fragile environment.”

Last year was split into two halves for the aviation insurance sector. The first continued in much the same way as 2013, with new capacity entering the market which brought about further pressure on market shares. As a consequence, pricing reduced on those renewals that took place.

But that changed in the second half of 2014 when a quartet of losses took their toll on the market.

The losses involving Malaysia Airlines flights MH370 and MH17, the hull claims following on from the bombing at Tripoli Airport and the AirAsia QZ8501 disaster have, in general, brought an end to those reductions.

“[For the hull and liability market], the first part of the year saw renewal results in the 10% to 20% rate reduction area, very much a continuation of what we saw in the last quarter of 2013,” explained Weyman.

“This changed after the second Malaysian loss to small increases in rate and generally an increase in premium dollars on typical risks (good record and modest growth). This in itself was quite a large swing in the opposite direction and a healthy injection of dollars in a marginal market.”

While these increases were imposed, the extent of the rises was less than what underwriters had initially proposed.
“There was of course a lot of ‘noise’ in the market that increases of some greater significance were going to be imposed but this did not happen and the market quickly settled down to a more measured and possibly sustainable level of premium,” said Weyman.

That two of the claims will fall onto the hull war market, as opposed to the pure hull sector, has also impacted the extent to which rate rises can be enforced. The MH17 catastrophe and the bombing in Tripoli have brought claims of up to $700m onto a market that only generates some $60m of premium each year.

Following those losses, hull war underwriters were adamant pricing would have to increase substantially to offset the high level of claims. However, Weyman said the hull war market “was a classic case of its bark being worse than its bite”!

There is little doubt the 2014 loss ratio for the hull war class will make poor reading, and there was an expectation that underwriters would look for substantial price increases to make up for the claims – something in the region of 50% to 100%. But, as Weyman explained, it did not quite work out like that.

“After about a month of these types of increases, one major emerging market offered to lead two of the largest renewals with minimal increases and as a consequence the market collapsed. This was the trend from then on.”

This dynamic may surprise some when reflecting on the losses it suffered in 2014, but with the war market representing more a catastrophe cover than anything else, it can go many years without experiencing any claims. Consequently, underwriters will look at the returns they have made over a long period of time and, as Weyman explained, they amortised 2014’s result into something they can justify.

“Maybe you need rose tinted glasses to make this work but on that basis it seems underwriters find the business is hard to walk away from.”


JLT Specialty Contributor Nigel Weyman, CEO, Aerospace
The cost of insuring satellite launches is set to rise for some operators, but better risks should enjoy favourable conditions as underwriters look to reward the use of more reliable rockets and satellite technologies.

The space insurance market is tough, with fierce competition and a run of losses in 2013 and 2014. The sector was shaken by two high profile losses in October following the failure of an Antares 130 rocket and the loss of Virgin Galactic’s SpaceShip II, a reminder that supporting the burgeoning commercial space sector is likely to be a bumpy ride.

On 28 October an Orbital Sciences Antares 130 rocket carrying an Orb-3 cargo craft to the International Space Station (ISS) came to a fiery end just seconds after lift-off. It generated a $48m insurance claim. Just days later, the Virgin Galactic SpaceShip II crashed during a test flight over the Mojave Desert killing one of its two pilots. The space plane was reportedly insured for $40 to $50m, underwritten by aviation insurers led by AIG.

The two losses in October will not in themselves turn the soft space insurance market, but they do come at “a challenging time for space underwriters.

“For most clients this is a good time to buy space insurance, but it’s a challenging time to be an underwriter of space risk,” according to Peter Elson, Chief Operating Officer Aerospace at JLT Specialty Ltd. “There’s plenty of competition putting pricing under pressure, while space underwriters are now having to manage a much more volatile and fragmented book of business than they did over the last 10 years,” he said.

Underwriting margins are already thin for space insurers that will find it difficult to turn a profit this year, explained Jan Schmidt, a space underwriter at Swiss Re in Zurich. Rates for launch plus one year [in-orbit] are around half of what they were in 2010, he said.

The 2013 underwriting year produced a loss. 2014 has already seen above average losses and lower premiums. Total space market premium in 2014 currently stands at around $750m, compared with an average of $1bn. However, claims so far this year total about $650m, suggesting a breakeven year for space insurers, or even a small profit.

Despite low rates and increased losses, the space insurance market remains attractive for insurers because it provides potential profits and a source of premium from uncorrelated risks.

“Many in the market believe that rates are not sustainable at this level, but it remains a question of supply and demand,” said Mr Schmidt. “The market remains attractive even though many players are not making money,” he said, noting that there have not been any significant withdrawals from the market.

While launch failures are both spectacular and costly, underwriters have also suffered some expensive claims for satellites in orbit, pointed out Mr Schmidt. This year has seen four O3b Networks telecommunications satellites suffer a power anomaly and the malfunction of the recently launched ABS-2 broadcast satellite, which has reportedly resulted in a $214m insurance claim.
According to Mr Elson, space insurers have enjoyed a good run of satellite and launch reliability as well as strong profits over most of the past decade. However, in the last two years there has been an increase in insured losses. This escalation is the result of setbacks in new satellite and rocket configurations combining with continued random failures of proven systems.

“We now face the real prospect of a relatively small number of partial losses wiping out the annual premium for the entire space insurance market. For the in-orbit insurance segment, that number could be just one,” said Mr Elson.

As a result, space underwriters are becoming much more selective to avoid losses in a softer market. “We’re seeing far higher differentiation for launch plus one year cover, with the less well-perceived risks priced as much as three times more than the most attractive,” said Mr Elson.

Recent losses are helping stabilise an otherwise soft space insurance market, according to Denis Bensoussan, Space Underwriter at Beazley. Launch vehicles or satellites that have experienced failures in recent years have seen significant rate increases, he said.

“This is a market with two faces. Reliable risks attract competition, and for good risks the market remains soft. But a significant and growing section of the market containing challenging risks is attracting higher rates,” according to Mr Bensoussan.

“It is only fair that underwriters reward operators that favour reliability over costs,” said Mr Bensoussan.

“Technical differentiation is part of the value insurers bring. It is our responsibility as underwriters to provide premium that adequately reflects the risks and rewards those demonstrating long-term reliability,” he said.

However, more expensive insurance can have a big impact on the cost of satellite procurement and launch, with insurance on average accounting for one third of the total amount. Balancing cost and reliability presents some interesting challenges for space operators.

While new commercial launch vehicles from Orbital Sciences Corporation and SpaceX have increased choice since NASA’s Space Shuttle was taken out of service in 2011, there remains only limited reliable launch capacity.

Ariane, the leading commercial launch provider, and SpaceX, its emerging competitor, can only supply a limited number of launches each year, while US rules on exporting satellite technology prevent operators using the Chinese Long March launch vehicle.

The cheaper Russian Proton vehicle, subject to both launch failures and delays in recent years, is proving a risky choice. Following six launch failures in almost four years, Proton-M rocket launches have already seen significant rate increases.

Just over ten years ago, the market perceived broadly consistent risk profiles across the main launch vehicles and satellite systems but considerable differences have emerged in the past few years, according to Mr Elson.

“Not so long ago, clients could look at their total mission costs and view insurance as a significant, yet reasonably consistent element. But today there are huge differences in risk pricing,” said Mr Elson.
"WITH ONLY ABOUT TWENTY LAUNCHES EACH YEAR REQUIRING INSURANCE, THESE CONDITIONS ARE ALSO MAKING IT INCREASINGLY DIFFICULT FOR UNDERWRITERS TO BUILD A DIVERSE AND BALANCED PORTFOLIO, MR ELSON EXPLAINED."

With only about twenty launches each year requiring insurance, these conditions are also making it increasingly difficult for underwriters to build a diverse and balanced portfolio, Mr Elson explained.

Higher value western-built satellites gravitate to the more reliable launch vehicles—like the Ariane 5—which attract the most competition from underwriters. However, the Ariane 5 is capable of carrying two high-value satellites into orbit, with a combined insured value roughly equal to that of a whole year’s premium for the space market.

“The space market is inherently volatile with relatively few events. This is now being compounded by the challenge for underwriters to secure the lines they want across what is already a very narrow spread of risk,” said Mr Elson.

The space market is not growing currently, but there are some favourable trends. For example, the development of smaller and cheaper micro-satellites coupled with more efficient and reusable space vehicles could entice new players into the satellite market, predicts Mr Schmidt, who noted that commercial operators are more likely to buy insurance than government-funded ventures.

The development of the commercial space sector was aided by NASA’s decision not to replace the ageing Space Shuttle in 2011. Rather than develop a new launch vehicle, NASA awarded contracts to commercial operators Orbital Sciences Corporation and SpaceX to resupply the International Space Station, with the intention of using commercial operators to ferry cargo and astronauts to the station in the future.

In addition to SpaceX and Orbital, several private companies, including Blue Origin, Virgin Galactic and UK-based Reaction Engines Ltd, are also looking to build commercial reusable launchers capable of taking people and payloads into space, albeit low orbit. The development of the commercial space sector is a positive for both satellite operators and insurers, although underwriters could potentially face higher claims as new launch vehicles mature, explained Mr Schmidt.

An increasing number of reliable commercial launch vehicles will give satellite operators more choice and will help diversify risk, he said. For example, if a problem arises on one launch vehicle, there would be a greater number of alternatives available, he added.

However, while the diversification of launch supply is important for operators and insurers, it only helps if they are reliable. With the market’s annual premium currently riding on just two main launch vehicles, uncertainty creates even more unpredictability in an already volatile market, explained Mr Bensoussan.

“Recent losses are a sad reminder that space is a tough and unforgiving business. Insurance traditionally plays a critical enabling and supporting role to help new players get into the commercial space business, but underwriters will have to be cautious and patient by only rewarding enduring maturity and reliability and not be blind to the risks,” said Mr Bensoussan.


JLT Specialty Contributor Peter Elson, Chief Operating Officer, Aerospace
Claims management in the corporate space needs a tailored and clearly communicated approach, so how can insurers and brokers eradicate the grey areas to deliver this successfully?

It is often said the point of claim is the only time customers interact with their insurers, but in the corporate sphere this approach is simply unworkable. Corporate clients have insurance programmes that are designed to their individual needs, and as such there needs to be clear guidance on exactly how every aspect of the programme will perform on a day-to-day basis.

Programmes will vary in everything from the size of the deductibles to the use of captives and self-insurance strategies. The underlying risk appetite of a corporate customer will also play an important role in determining the nature of its insurance programme, as will the scope of covers demanded by external stakeholders such as trading partners and legislation.

“I do not think we have two client programmes in the large corporate sector that look the same,” says Warren Downey, managing director at JLT Specialty.

Discussing the approach JLT Speciality takes to claims in the corporate space, he adds: “The process is all individually set by the client – some clients, for speed, would like to directly report to an insurer and we get involved one minute after that.

“You have some that want to see everything come through us. Our standard operating procedure is to have a claims protocol that describes everything for an individual client in terms of what happens in the event of a claim – regardless of its size or its source – so everyone knows what the process is, from the date of loss through to settlement.”

One of the challenges in catering for a corporate client’s claims needs is that they range from low-frequency major losses all the way down to high-volume small losses. This sliding scale demands varying levels of both expertise and automation, and getting the mix right is fundamental to the overall experience enjoyed by the corporate customer.

Graham Gibson, director, claims at Allianz Insurance, says the firm has a team of consultants whose function is to make sure claims operating procedures for corporate clients are clearly established and effectively managed.

“We have claims business consultants who actually go out with the renewal team or the new business team and sit with the client,” explains Gibson. “We talk about what the client needs from us in terms of claims handling in the event of a loss. We have a team of 17 people whose job is to do that procedural piece before we have even got the policy up and running. For a large corporate it is important that the process is quick, efficient and slick.”
Both Allianz Insurance and JLT Speciality say they do not look to outsource claims handling and they point to the in-house expertise they can bring to claims as large, multi-national organisations. “We have 100 businesses in over 70 countries that deal with a vast array of different areas and issues,” says Gibson. He also points to specialist firms within the Allianz group of companies like Euler Hermes that can be called upon to provide specialist knowledge where needed.

Downey is equally keen to promote JLT Specialty’s capabilities, mentioning its subsidiary Echelon Claims Consultants and the expertise it has in disciplines ranging from forensic accounting to chemical engineering.

But no broker or insurer can claim to be all things to all corporate customers – as Downey accepts: “No reasonable insurance broking entity can say they can cover every base and every specialist – and if they do, they are probably fibbing. Therefore, what we do is try and have the most critical and the most common expertise in-house. When it is more likely that [other] companies will be able to provide better service, we align ourselves with those third parties.”

Where third parties are appointed, their role has to be in supplementing rather than replacing the skills brokers and insurers have. In addition to technical expertise, they can also bring project management skills that are essential in making sure the various parties feed into the claims process effectively and bring it to a swift resolution.

Kevin Larman, director, client relationships at Cunningham Lindsey, comments: “There are a lot of different things that can happen [on a major loss] and it is the project management and attention to detail that [corporates] get from an adjuster that is the key. You do need someone onsite who is a central point. You need someone at the centre of all of the activity to co-ordinate.”

Further down the scale, smaller, more attritional losses might not require the same level of technical expertise, but they do demand an efficient solution that is increasingly underpinned by data analytics. As Gibson explains: “If you have a fleet of 1000 vehicles you know you are going to have around 250 claims a year. You might be getting on for one a day and a claims manager does not want to have to phone each one of those in.”

To that end, insurers are under pressure to design bespoke digital solutions for their clients and adapt their own technology to suit the needs of their corporate customers.

Gibson adds: “Absolutely they want to drive it through a portal and look at the progress of claims as and when it is convenient to them.”

But it is not just convenience and speed that is fuelling corporate customers’ appetite for digital solutions – they are all now striving to generate improved performance and competitive advantage through better understanding of their claims experience.
“WE HAVE A TEAM THAT WILL RUN SCENARIOS THAT ARE OUTSIDE OF THE DAY-TO-DAY CLAIMS HANDLING TEAM,” EXPLAINS DOWNEY.

“You cannot over-emphasise just how important data is,” says Larmar. “Some of the work we are doing with corporates is all around how much data we can give them and how we can enrich their own data by giving them information from the claims space.”

In addition to improving their performance, corporate customers want to ensure the insurance programme will respond as necessary at every turn. When there are so many different lines of cover in place and the scope of a corporate customer’s operations are so wide, this can be difficult.

To combat this, JLT Speciality has a team working purely on claims scenario testing. “We have a team that will run scenarios that are outside of the day-to-day claims handling team,” explains Downey.

“We will do that every week and we perceive that as being a very important process – it helps the client understand the scenario, it helps us prepare to respond and it helps the market answer some grey area questions long before the event.”

The more of these grey areas the industry can eradicate through upfront and detailed communication, the easier it will be to create certainty for corporate clients at the point of claim – and that will benefit every stakeholder in the insurance programme.

This article was published in the 5 February edition of Post magazine.
The escalating, extremist-spawned terror crisis threatening security across the Middle East, parts of Asia, north Africa, east Africa, the Sahel, west Africa and, increasingly, major cities across the globe has been listed among four key geopolitical risks, which present grave medium- to long-term consequences.

Lawrence Nazare, Executive Director of Continental Reinsurance, said other likely geopolitical risks of concern include: “Right-wing nationalism threatening the welfare of immigrants in most developed nations; renewing racial and sectarian divisions; a new Cold War precipitated by events in the Ukraine resulting in a new bipolar schism with no fundamental ideological base; and, finally, territorial claims motivated by resource prospects, for example in the South China Sea and Antarctica, that are threatening future global peace.”

He added: “A major possible risk in 2015 is another global meltdown from the oil price war going on. If the Organisation of the Petroleum Exporting Countries (OPEC) maintains production, oil prices will fall below the economic production price for US oilfranking and may lead to another US recession, with a consequent ripple effect on the rest of the world.”

His concerns are echoed by Amy Gibbs, Associate in the Credit, Political & Security Risk team at JLT Specialty. Among the risks she highlights in 2015 are:

- The end of the commodities supercycle, bringing renewed political risks
- The continued growth of ‘galvanised extremism’, primarily in the shape of IS, presenting greater security risks
- New credit crises in 2015 as many emerging market sovereign debt levels become unsustainable
- Regime changes in oil rich countries, brought about by the collapse in global oil prices.

In Africa, Mr Nazare pointed to ‘the leapfrogging’ into the information age, which presents opportunities but also a crisis of identity and relevance for the African economy that effectively now straddles multiple epochs from medieval, pre-industrial, agricultural/resource and industrial, to high-tech, information-driven.

He added: “Changes in the global economy in 2015 are expected to come from the slowdown in China and the drastic change in OPEC, particularly Saudi views on crude oil prices that will negatively impact established oil-exporting countries in Africa and all the new and other expectant countries looking forward to a hydro-carbon inspired boom.

“At risk in 2015 are sectors requiring intensive capital—for example, mining and hydro-carbons facing severe capital constraints and revenue reduction as well as infrastructure, power and transportation sectors facing stagnation due to slowing investment.”
Social unrest and tensions in disadvantaged populations, particularly the urban youth, are also a concern. Africa’s growth story, in gross domestic product (GDP) expansion, has not been permeating to its lower socio-economic groups.

Speaking on the state of the tourism sector, Mr. Lazare said: “The tourism sector faces the risk of further slowdown due to increased extremist activities and a bad image resultant from the Ebola crisis.”

Meanwhile, he said: “Lower commodity prices leading to GDP growth stagnation, currency pressures, high inflation and balance of payments constraints are economic risks that will impact Africa’s fastest growing regions in 2015. The slowdown of African economies due to depressed commodity prices, particularly oil leading to capital flight, fiscal pressures on governments, negatively impact all sectors—particularly insurance.

“The lack of fiscal space for governments and reduced budgetary commitments to social services and infrastructure and relapse of fragile economies into extreme poverty are economic risks that could potentially face Africa’s fastest growing regions in 2015.”

However, opportunities remain. Mr. Nazare said: “Opportunities on the African continent are expected to come from the consumer-driven sectors—such as FMCGs, real estate, telecoms, and health—seeing sustained expansion due to Africa’s expanding middle-class.”

JLT Specialty Contributor: Amy Gibbs, Associate, Credit, Political & Security Risk
Broker JLT has warned that a number of risks are likely to grow in 2015, including sovereign default.

The Risk Outlook for 2015 contains a number of threats that were not foreseen for 2014, according to broker JLT’s Risk Outlook 2015, released on December 30.

JLT noted that at the beginning of 2014 “many of the risks were a continuation of 2013’s volatility”. These included a slowdown in Chinese growth, economic difficulties in the eurozone and the US, war in Syria, Islamic extremism and resource nationalism.

But in 2014, JLT observed, “new crises have emerged that have challenged our perceptions of risk in the post-financial crisis world”. These include the caliphate Islamic State, the outbreak of Ebola in West Africa, riots against the Chinese administration of Hong Kong, and “the end of the commodities super cycle”.

The Commodity Metal Price Index rose by more than 220% between 1998 and 2008, while oil prices rose gradually, reaching $133 a barrel in July of 2008. However, JLT warns that the end of this super cycle places at risk those countries that rely on metals, minerals and oil for their wealth. JLT provides a long list of countries that face worries from the change in the cycle: Chile, Peru, DRC and Zambia (copper), Russia, Peru, South Africa, Uzbekistan and Ghana (gold) are just two groups of countries facing economic volatility from the new pricing.

JLT warns that “pressures on finances mean heightened risks of government interference in strategic sectors”.

Islamic State (IS) now has assets estimated at $1bn and controls a significant part of Syria and Iraq. There are concerns about “sleeper cells” in countries neighbouring Syria. JLT predicts that IS will attempt to radicalise Sunni groups in Lebanon, while in the southern Jordan city of Ma’an there is clear support for IS. “Sleeper cells of not, the greatest worry for the rest of the world is that the IS media machine has the capability to inspire extremist acts”. This could lead to increased instability in the northern Caucasus – Kazakhstan, Turkmenistan, Uzbekistan and Tajikistan. “A contributing factor to the rise of Islamic terrorism across Central Asia is the lacklustre economic and social conditions and the fact that wealth is concentrated in the hands of the political elite” says JLT.

A number of elections will be held in 2015 that could have implications for political risk. Nigeria, Tanzania, Argentina, Sudan, Guatemala, Yemen, Niger and Burkina Faso (Upper Volta) are also holding polls. JLT warns that the North-South divide in Nigeria will polarise that particular contest. “While Goodluck Jonathan is expected to clinch a second term, his re-election will cause further disaffection in the north”.

JLT also notes that emerging market debt issuance doubled in 2014, but asks, “will a sovereign default see investors exit positions?” The low-interest rate environment proved a boon to emerging markets seeking to load up their debt levels or to refinance existing debt, but JLT is concerned that “some countries may be over-committing to unsustainable levels of debt, as many of the issuances have been based on the assumption that resources wealth will act as guarantee”.

In Europe the continuing crisis in Ukraine is the major threat to economic stability. Russia is on the brink of recession, and leader Vladimir Putin is thought unlikely to back down over the Ukraine, which makes the country “a possible candidate for default” in 2015.
COMMENT:

JLT’s outlook for 2015 is not rosy, and rightly so. The low-interest-rate and low-inflation environment that is increasingly looking to be long term in the US and western Europe has led asset managers and businesses headed by the 40-plus generation to seek the wrong solution. Instead of reassessing businesses according to the new normal, they are seeking interest rates compatible with the old normal. But they are ignoring the increased risk that comes with what a decade ago were considered blue-chip rates, but which now are at a much higher risk of loss of principal. That was evidenced by the flow into emerging market debt in 2014. A $2bn debt offering from Kenya, for example, was four-times oversubscribed. There is nothing intrinsically wrong with investing in Kenyan debt, but even the Kenyan government would not claim that it is on a par with US Treasuries.

The end of the commodities supercycle will have worrying implications for emerging markets in political terms. It is a sad fact that liberal democracy tends to thrive on rising general wealth, while autocracies tend to appear when crises strike. There was a “golden age” of democratic emergence in Europe from 1974 on. There are many more democracies in the world today than there were 40 years ago. But, rather than being an evolutionary trend, there is a high chance that this too was a “political supercycle”.

Insurers in 2015 can see likely future developments as a double-edged sword. After all, if there is no risk, there is no need for insurance. Therefore if the world becomes a riskier place, that should be good for insurance. But, of course, it is not that simple. For insurers the ideal world is one that companies or people with disposable income think is dangerous but which is really relatively safe. A system that companies and people think is safe but which is really rather dangerous is of no use to insurers at all. There is a danger that 2015 will be that kind of year. Two countries stand out – Russia, and (a controversial selection here) Australia. For Russia the glue holding the country together at the moment appears to be the fact that most citizens back the Putin view of the world – that being a steady encroachment by foreign powers on Russia’s zones of interest. But if living standards and the economy collapse, political sympathy for the Putin view might take second place to economic needs.

In Australia, society has had more than two decades of commodities-backed comfort. Only Canada comes close to rivalling this level of benefit in the developed world. Two decades is long enough for the populace to come to think of that standard of living as a right rather than as something that has been generated by exploiting mineral wealth developed over millions of years. Australia has perhaps the most unsustainable long-term economic model of any developed nation, and it is a very different country now from 40 years ago. It is multi-cultural, sophisticated, and Sydney could well call itself “the Paris of the south”, were it not for the fact that Sydney would perhaps not want to be compared with Paris at all.

The current Australian administration led by Tony Abbott faces some of the toughest economic decisions faced by any Australian administration since Gough Whitlam in the early 1970s. Australia has lived well on the commodities boom; it will now have to cope with the commodities bust.

There were many shocks to the global system in 2014. Amy Gibbs of JLT CPS suggests this year will be no different – and gives clues as to what we should be looking out for.

What a difference a year makes. Throughout 2014, new crises emerged that challenged our perceptions of risk in the post-Financial Crisis world: Islamic State, Ebola, war in Europe, riots in Hong Kong, and the end of the commodities super-cycle. The signs point to 2015 being equally as turbulent.

With heightened risk across the board, investors must continually challenge their perceptions of country risk in order to safeguard commercial opportunity. Here we identify several risks for the year ahead.

**COMMODITIES DOWNTURN, POLITICAL RISK UPTICK**

During the commodities super-cycle, a number of countries benefited from the export of metals and oil, as high international demand continued to be coupled with long-term supply availability. The Commodity Metals Price Index increased nearly 223 percent between 1998 and 2008, and countries with metals and minerals wealth enjoyed steady foreign direct investment (FDI) inflows. Over the same period, oil rose gradually until a dramatic fall in December 2008 when the Financial Crisis hit, before recovering over 2009-2010, rising to and then hovering around an average of $110 per barrel during 2011-2013.

The end of this super-cycle now places those countries with an over-reliance on extractive industries under immense strain. Already governments that underpin their budgets with oil or metals have seen currency values plummet, foreign exchange reserves erode or current account deficits rise.

Mining companies are freezing or axing investment in response to low prices. With energy making up as much as 50 percent of the production cost for metals, theoretically lower oil prices should aid production. However, mining costs, including labour, power and taxes have increased, so the oil price fall is less impactful.

The dramatic fall in oil prices will see oil firms following suit; it is estimated that around $250 billion of capital expenditure (capex) may be frozen annually until 2018 if the price per barrel hovers around $70. With the oil price already falling well below that mark, a number of projects, particularly those requiring expensive technological investments such as deep water drilling, become uneconomical.

After a decade of strong revenues during the super-cycle, public expectations have been lifted. Governments must now rethink their strategies towards foreign investment if they are to avoid mediocre economic performance. While governments recognise that they still need to seek foreign investment, pressures on finances mean heightened risks of government interference in strategic sectors, such as mining, oil and gas, or infrastructure.

Acts of ‘creeping’ expropriation, where host government action gradually erodes the investment return to the point where a project becomes unviable, are also more likely in 2015. Such actions could include: changes to the tax...
code; changes to labour law; export embargoes; and changes to local banking laws that leads to the risk of currency inconvertibility and inability to transfer or repatriate funds.

A further consideration is politically enforceable environmentalism. Some emerging markets are recognising the environmental cost of large-scale oil and mining operations and are turning away from the 'growth at any cost' mantra. Expect non-compliance with environmental law to be met with steep fines and a political backlash.

REGIME CHANGE

Elections are always volatile periods. Risks include protests during campaigning, poll day terrorist attacks, post-election contractual agreement repudiation, changes in the direction of economic policymaking, or upticks in nationalism that prompt expropriatory acts.

In 2015 we will see a number of regional leaders holding elections including Nigeria and Tanzania in Africa, and Argentina in South America. A number of states already grappling with serious security issues - Sudan, Guatemala, Yemen, Niger and Burkina Faso - are also holding polls.

The Nigerian election in particular, in Africa’s largest economy and key oil state, will be watched keenly. The election will be the most closely-fought election since the country’s return to democratic rule, and the north-south divide will polarise the contest. While Goodluck Jonathan is expected to clinch a second term, his re-election will cause further disaffection in the north.

Following Argentina’s sovereign default this year, the economy will continue to deteriorate into 2015. Inflation is now over 30 percent, while foreign exchange reserves are rapidly falling and growth is stalling. The country’s lock-out from international markets means that the odds are stacked against it finding the appropriate funding to develop its large reserves of shale gas. However, reform by the government will not be popular. Populist policymaking, isolationism and belligerence towards investors combined with low oil prices and the country’s default have now created the perfect storm for renewed unrest.

In those countries where living standards could now decline as a result of reduced government spending, or ineffective economic policymaking due to lower commodity prices, there is a risk of protests.

For the monarchies of the oil-reliant Gulf states, the lower oil price is a direct risk to stability. During the Arab Spring, the United Arab Emirates (UAE), Bahrain, Kuwait and Saudi Arabia among others experienced a wave of large-scale protests over corruption, unemployment, cuts in subsidies and economic decline. Despite the abilities of the royal families and governments to mitigate the risk of revolution, suppressed oil prices could heighten the risk of protests in the medium term in the Gulf states if spending is again reduced as foreign exchange reserves cannot be utilised to prop up government spending indefinitely.
“GOVERNMENTS MUST NOW RETHINK THEIR STRATEGIES TOWARDS FOREIGN INVESTMENT IF THEY ARE TO AVOID MEDIocre ECONOMIC PERFORMANCE”

SOVEREIGN DEBT OVERLOAD
With interest rates low, the opportunity to refinance short-term debt has proved attractive to governments needing additional funds in the wake of lower commodity prices. The concern is that some countries may be over-committing to unsustainable levels of debt, as many issuances have been based on the assumption that resources wealth will act as guarantee. With oil and metal prices at their lowest levels for a number of years, the subsequent delays to energy capex will have a knock-on effect to project development and ultimately, the reliability of revenue streams.

For those countries facing security threats, political instability or further delays to developing the essential project infrastructure required to capitalise on natural resources wealth, these new debt obligations may further undermine economic stability.

With a number of countries likely to see economic downturns on account of the end of the super-cycle, we may see several countries teetering on the brink of default. Venezuela’s economy has been in decline for some time and investors are now concerned that the serial defaulter may strike again. Venezuela has relied on per barrel oil prices of $140 to $175 to achieve fiscal break-even since 2011.

With oil prices having fallen so far, government reserves are severely affected as the government loses $700 million for every dollar drop in the oil price. In addition foreign exchange reserves are decreasing dramatically, there are shortages of many basic goods and inflation is over 60 percent. Credit default swaps and bond yields in October increased to multi-year highs. The country will be reliant on emergency credit lines from allied nations, such as China, to prevent default.

Meanwhile in Europe, the ongoing Ukraine crisis is putting a severe strain on economic stability. A $3 billion bond repayment is due to Russia in December 2015, while the International Monetary Fund (IMF) warned in December 2014 that it is facing a $15 billion shortfall in emergency funding for Ukraine, on top of a $17 billion IMF lifeline that Ukraine secured in April 2014.

The country’s 7 percent GDP contraction, drop in exports, capital flight and declining foreign exchange reserves that have occurred as a result of the conflict with Russia, has put Ukraine dangerously close to defaulting on its sovereign debt obligations. However, given Ukraine’s pivotal position vis-à-vis Russia, Europe or the US may support the country in the worst-case scenario.

Most importantly, if international bond investors begin to re-focus on country risk rather than concentrating exclusively on low interest rates and low liquidity, we may see abrupt changes in bond prices as investors exit positions.

Amy Gibbs is a senior consultant at JLT CPS (Credit, Political and Security risk) in London
The last decade has seen thousands of highly publicised and cost-heavy cyber incidents which have impacted organisations across the globe as well as a range of industry sectors. No company or industry is immune.

As the pace of technological change continues unabated, organisations’ reliance on computer networks and the information they hold has become critical to their ability to offer products and services and to interact with customers and employees.

This shift in emphasis from tangible assets, like buildings and machinery, to intangible assets, like networks and data, didn’t immediately result in a similar shift to specialised insurance policies. The landscape of cyber insurance was slow to grow at first but is now advancing at rocket speed.

WHEN AND WHERE DID IT ALL BEGIN?

In the late 1990s and early 2000s, insurers first began to offer products with slivers of today’s cyber coverage. Early products mainly dealt with the liability resulting from transmitting a virus to a business partner and business interruption suffered after a cyber attack, but the triggers tended to be much narrower and the coverage more restrictive.

Despite being revolutionary, there was relatively little uptake in the early days as companies were uninterested in a product they didn’t understand and felt was expensive. With regulators not in the picture and few headline claims in the public sphere, insurers found that their cyber products weren’t flying off the shelves.

SO WHAT HAS HAPPENED SINCE 2003?

California’s law and others like it have brought thousands of data breaches to light since 2003. In fact, now forty-seven states, the District of Columbia, Guam, Puerto Rico and the Virgin Islands all have some form of breach notification regulation, making it tougher to legally keep incidents under wraps these days. Many large incidents became hugely expensive, and insurers responded with policies covering more and more of the cost of suffering a data breach. Those companies who suffered from a breach now incurred a range of additional expenses; notably for consumer notification, credit monitoring, forensic investigation, call centres, public relations, legal advice, and other crisis management expenses. Unlucky companies also faced legal costs - both in responding to regulators and civil litigants - as well as ever larger settlements and fines.

Despite not having the same data breach notification laws as the States, companies in the UK are increasingly put under pressure by the Information Commissioner’s Office (ICO). The ICO state that organisations should take suitable precautions to safeguard any personal data they hold. In the event of a breach the company should notify the ICO within 24 hours. Depending on the level of
damage caused by the breach, all those who are affected may require notification as well. If and when the new EU Data Protection Regulation passes, as many expect it will in 2015, the obligations to notify consumers and data regulators of incidents will swing far closer towards the onerous US regime.

This increasingly difficult cyber exposure environment has not gone unnoticed by corporate risk managers. Particularly in North America, cyber insurance purchases have grown exponentially; with many large insureds seeking more capacity than the market can offer. Demand for cyber insurance education in Europe and Asia has never been higher, with companies reacting to daily headlines and changing regulatory landscapes. Purchasing behaviour has also accelerated rapidly over the past 12 months.

Cyber concerns and solutions today stretch beyond simply data breach risk for companies reliant on personally identifiable information. Attacks on industrial control systems have recently caused companies in energy, mining, heavy industry, and manufacturing to reconsider their cyber risk exposure and insurance solutions. Companies in all industries are thinking more critically about their reliance on technology, online communication, big data, and the business continuity impacts that a technology failure could create.

FROM OPTIONAL TO CRITICAL?

With the proposed EU Data Protection Regulations set to be finalised by 2015 and with fines of 2% global turnover or euro100 million for noncompliance, data breach risk isn’t going to become any less expensive. Neither is our collective reliance on technology showing any signs of reducing the exposures. Cyber risk is a multifaceted issue that stretches from the data centre to the boardroom.

The most forward thinking companies no longer view cyber insurance as merely optional, but rather a critical weapon in their cyber risk management arsenal.

JLT Specialty Contributor Sarah Stephens, Head of Cyber, Technology and Media E&O, Financial Lines Group
Your role has changed significantly since the Lloyd & Partners/JLT Specialty merger took effect at 1 January. How would you describe your new role in terms of responsibilities, personnel etc?

At Lloyd & Partners I headed up the energy technical team, overseeing the client-facing account handlers/executives, slip production, contract wordings etc. I also assumed responsibility for the team’s day-to-day operations, which is something I have always taken a keen interest in, although that function was essentially run centrally at Lloyd & Partners.

At JLT Specialty the individual operating divisions are responsible for their own operations function and I have been appointed divisional chief operating officer, energy.

The Lloyd & Partners and JLT Specialty energy teams have merged to create a substantial business with around 150 people, operating globally in the upstream and downstream oil and gas sectors.

A lot of our business emanates from working closely with JLT’s retail offices and JLT Network partners around the globe, including in all the major energy industry hubs where we have offices - such as Brazil, the US, Canada, Australia and Asia.

We also retail major clients from our London office, and maintain our important independent broker wholesale business (predominately from the US) where we operate as Lloyd & Partners.

I am still heading up the combined technical team, and still have individual major client responsibilities that I am continuing to carry out, so from that perspective there has been no significant change.

And how has the energy team’s focus changed, if at all, with regard to classes of business, geographies, the balance of upstream/downstream business etc?

At Lloyd & Partners we primarily focused on North American wholesale business (from independent US retail brokers), while JLT Specialty’s energy team were mainly non-US focused and more retail oriented.

The only significant change in the merged team is that the JLT power and alternative energy business has now been re-positioned within JLT’s property, casualty, mining and power division.

The rest of the two teams have successfully merged together to create what we believe is the largest energy team in London in terms of both staff numbers and premiums placed into the global energy insurance market.

What early indications are there that the collapse in global oil prices is having a material impact on energy construction projects?

Most construction projects that had got as far as having their insurance needs discussed or worked on are likely to continue as many of the oil companies are already too committed to cancel, so we don’t see there being an immediate impact.

However, if the oil price stays where it is over the longer term - or falls further - it will almost definitely result in a downturn in construction activity. A more immediate impact is going to be reduced sums insured for those clients buying business interruption or loss of production income coverage, which is directly linked to oil prices, meaning less premium income for the market to fight over.
Drilling budgets are also immediately being cut, which will result in lower insured exposures and less premium. In addition, as insured’s assets earn them less revenue, insurance values are likely to be reduced, meaning a further pressure on the market’s premium pot.

What are your predictions for rate movements in the Gulf of Mexico upstream market this year, as well as for the wider offshore market?

It will definitely be a buyers’ market next year and probably the best in two decades for clients. The Gulf of Mexico wind product will see double-digit reductions, whilst “operational” risk products will fare even better than wind.

That’s with existing markets, but if an insured wants to take a short-term approach to buying and is not interested in maintaining relationships with markets they may have been with for many years, they will be able to save even more money by totally re-marketing their risk where they can. That is unlikely to be possible, however, for buyers of large wind limits or capacity operating risks.

The driver for all of this is ever-increasing surplus capacity, as investors see insurance, and specifically the energy sector, as a profitable haven for their money. Unless other investment markets return sharply we see no end to these current market conditions, and with capacity at the levels it is at we can’t see any individual insured loss being big enough to change the market.

And downstream?

Downstream is equally affected by the same dynamics and meaningful reductions should be available in that sector as well.

What effect will recent consolidation in the broker space have on energy business?

Part of our rationale for the merger was the conclusion that scale is important. Ever larger insurers (created as insurers themselves find it hard to survive without sufficient scale) will look to partner with brokers that can deliver large premium volumes. This is likely, in our opinion, to lead to further broker consolidation.

There has been a lot of talk about covering cyber exposures in the energy market - are products for these types of risks gaining traction?

In short: no. Most insureds we represent view the resultant damage from cyber events as an “all risks” peril that should already have been priced into their current premiums. We agree - and we believe that the pressure to include resultant damage in all risks programmes will increase.

Individual insureds may buy the bespoke data protection-type covers being offered but we don’t see a huge demand for, or take up, of that product at the moment.

http://www.insidefac.com/_1253130/size-matters

JLT Specialty Contributor John Cooper, Chief Operating Officer, Energy
MANAGING THE RISKS OF DECOMMISSIONING

As a range of North Sea assets mature and will need to be dismantled and removed in the next few years, decommissioning is high on the agenda for oil and gas companies.

The first major North Sea structures were built in the early 1970s and some are still working 40 years on – well beyond their expected life span. However, a large number are now nearing the end of their working lives.

In addition, companies that originally had assets in the North Sea tended to be very large – such as Exxon and BP. Today, lots of the assets have been bought by smaller companies, which have purchased new technology to get more out of the reserves. They potentially do not have the same resources at their disposal, so the cost of decommissioning could now be more of a concern.

Decommissioning offshore oil and gas installations and pipelines can be expensive and complicated, and companies need to consider the full range of risks involved. They also need to acknowledge the risks can differ substantially from those involved in construction. Companies need to abide by the Department for Energy and Climate Change’s (DECC) decommissioning rules. Anything above water has to be removed and anything below the water should also be removed – although companies can occasionally agree with the DECC to leave something on the sea bed, in exceptional circumstances.

A decommissioning incident might involve removing a piece of equipment from a structure and something breaking off as it is being lifted. In that scenario, the company will then be responsible for removing debris from the sea bed and for clearing up any pollution that occurs. The costs involved are likely to be considerable, as getting specialist equipment to raise something from those depths is very costly, as is pollution clean-up.

There may also be third-party risks to consider. For example, your structure may be connected to other structures or pipelines that are owned by other companies. Therefore, if you had an incident that affected their property, you would face third-party exposures such as business interruption. While some of those liabilities may be picked up by the protection and indemnity (P&I) insurance of the vessel dismantling your structure, there may well be specialist operations involved that fall outside their P&I limits for such operations.

Finally, when assembling an offshore plant now there tends to be a planned sequence of events. But for some early structures – including many of the North Sea assets – it was not always thought through how a platform would be removed. That lack of forward planning can still be an issue today. Where once a company might have built a 1,000 ft platform, they are now likely to build a sub-sea production unit – something cheaper to put in, but also potentially unknown in terms of how difficult it will be to decommission when the time comes.

COSTLY EXPOSURES

Pollution is a key risk in the decommissioning process because it is difficult to clean up and it can be very expensive. For example, if a company dropped a piece of equipment on the sea bed containing PCBs (polychlorinated biphenyls), they would be obliged to remove it because of the potential for pollution, the cost of which could be considerable. BP’s Gulf of Mexico spill may not have been caused by a decommissioning incident, but companies need to be aware of the potential for an incident when they undertake decommissionings. The BP example
also highlights the fact that perhaps the biggest impact of a pollution incident can be on your company’s reputation.

For the construction phase, an energy company will generally buy good, broad insurance cover. However, as decommissioning is seen as just being a cost, it can be tempting to reduce the cover the insurance offers – something companies should carefully consider before doing, given the potential scale of the risks involved. There are a range of insurance products that can help, including removal of wreck; property damage (if the platform has a residual value); pollution and clean-up liability; and third-party liability. These can be put together in a tailored package specifically for the decommissioning operation.

Some companies may have removal of wreck cover throughout the lifespan of their asset. However, they are likely to need to extend it: while on day one your asset is worth, say, $100m and your policy will pay up to 25% of the insured value ($25m) for removal of debris, when you remove the asset the depreciated value may only be $5m, so you would only be able to recover $1.25m for debris removal. However, clearing up an incident would be likely to cost far more than that, especially as removal costs increase over time. Parts of the asset may also have a high residual value, which is why taking out property damage cover for any property that could be resold can be important.

Companies should consider the scrap or resale value of the operation they are decommissioning and any equipment they are removing, such as generators or separators, as this may represent a considerable loss to the company if physical loss or damage occurs. For example, an asset may still be worth $10m at the end of its life, so companies need to decide if they could weather such a loss.

Similarly, pollution cover is often purchased to protect a company’s balance sheet because of the scale of the exposures involved. We sometimes get asked for “life” insurance for removal risks, but such cover has not become standard because of the long-term nature of the risks, the fact it ties up funds that might be used elsewhere and other financial considerations companies have.

DEVELOPING AREA

One issue that companies come up against is while the insurance market is well developed for construction and has a highly specialised WELCAR wording that is generally accepted by all parties (oil companies, contractors, brokers and insurers), there is at present no equivalent wording for decommissioning. Not having a comprehensive, commonly accepted wording means companies need to make sure any insurance product they are buying does exactly what they need it to do.

In addition, there are no standard industry contracts for demolition, so companies need to be very careful about what liabilities they are taking on in any contract. Overall, probably the most important thing for companies to keep in mind is the same care and attention is needed when planning all elements of the decommissioning process – including insurance and contracts – as was used for the construction process.

Tim Hyams and Peter Portman are both partners in the energy division within JLT Specialty

JLT Specialty Contributors

Tim Hyams, Partner, Energy
Peter Portman, Partners, Energy
New hires follow on from four regional PI appointments in 2014

JLT Specialty’s Financial Lines Group has appointed James Frost and Matthew Baker from Aon to strengthen its regional solicitors’ professional indemnity (PI) team.

Frost will be based in Birmingham while Baker will operate from Bristol, and their roles will be to grow JLT Specialty’s regional solicitors’ PI business.

They will be joining the business during Q1 2015.

The appointments follow those of Tony Brown, Toby King, Joel Harding and Gareth Greaves-Milner in 2014, giving JLT’s growing client base nationwide access to PI specialists.

JLT Specialty’s Financial Lines Group head of professional indemnity Adam Codrington said: “We are delighted that industry professionals of the calibre and experience of James and Matthew have chosen to join JLT.

“We are intent on building our reputation as market leaders in this area and they bring with them a huge amount of sector knowledge and a commitment to service excellence in line with our client first philosophy.”

JLT Specialty Contributor Adam Codrington, Head of Professional Indemnity, Financial Lines Group
TOP CLAIMS TIPS: HOW TO TURN DISASTER INTO AN OPPORTUNITY

Published 2 March 2015, aimic NEWS

For multinational companies future prosperity can depend on your ability to bounce back after a major claim. But co-ordination of the claim, across many jurisdictions with multiple insurers and local culture considerations, can be a complex affair. JLT Specialty’s Wendie Le Vey offers practical advice for risk managers.

Too often companies place all the emphasis on finding the right insurance programme. But when complex programmes are made up of different coverage layers involving large numbers of insurers, this can lead to differences of opinion when it comes to achieving a settlement. To avoid this and to put yourself at an advantage when something goes wrong; you need a clear strategy for handling claims throughout the life of the policy.

The first step in agreeing claims protocols before a major loss occurs is to identify the expertise within your own organisation as well as your broker, insurer and claims adjusters. This should include geographical spread, IT systems and pro-active risk management support. You should then ensure there are no unforeseen ‘gaps’ in cover and that control of the loss is maintained between the broker and insurer.

Ultimately companies must rely on trusted relationships, robust local service delivery with global co-ordination, and a consistent approach to claims and risk management.

Crucially, companies need to rehearse what may happen in the event of a major global loss. It’s not a simple task. There are a lot of considerations from understanding potential reactions from customers and suppliers to ensuring first-class communication between teams. The alternative, however, is a nasty surprise.

A claim should not be a disaster – it could become an opportunity to reinforce the brand and business strategy. A successfully made claim should also provide the firm with meaningful data and portfolio analysis, and lead to improved risk management.

In coordinating claims we need to look at four central areas: processes, people, data and funding. If you fail to get the right balance in each area, you will jeopardise the claim outcome. We look at these areas in more detail below.

PROCESSES

Overseas operations should have clear procedures that set out:

- When and to whom an incident should be notified. It is useful to provide templates of the information required for the main types of incident to ensure the information is captured at the outset;
- Monitoring of claims against aggregate or inner limits in external insurance policies and captive insurance arrangements;
- Delegated authority limits and notification;
- Service level agreements (SLAs) and key performance indicators (KPIs) for all parties involved with a claim so that expected responses are known and appropriate;
- Identification of any potential conflicts of interest and their impact on the resolution of incident, future business relationships and individuals concerned;
- Complaints procedures should be extended to include any complaints that arise out of an overseas incident.
PEOPLE
Sufficient numbers of suitably skilled and qualified people are required to resource the claim. International businesses should also consider the people element of overseas claims, taking into account local cultural sensitivities, and reflect these in any processes and procedures. There must be an awareness of local legislation so that local licences, visas and authorisations can be obtained quickly to facilitate people movement.

DATA
Recording information correctly will ease the claims payment process. Companies, brokers, claims adjusters and insurers all retain massive amounts of data. Transparency and easy access to information is critical, so that all involved in a claim can see the same information at any point in the process.

However, holding data comes with its own set of risks and companies processing personal information may be subject to myriad privacy laws: the cost of getting it wrong can be enormous.

In general the rules apply to individuals who can be identified by the information which is held so it is important to collect only the minimum information that is needed. If you are able to achieve your purpose without collecting or processing personal information then the privacy laws won’t apply.

As a general guide, we suggest firms:

- Collect only what data is needed for the claim;
- Tell the affected parties what is being collected, for what purpose and by whom;
- Don’t use it for another purpose (unless you notify the relevant parties);
- Keep data accurate and up to date;
- Keep data safe and secure;
- Don’t keep data longer than you need to;
- Make sure individuals’ rights to access their data are maintained;
- Don’t transfer data to another country.

FUNDING
Ensuring that adequate funds are available when needed is critical. Given the potentially significant sums that will need to be moved about the world, the processes need to be clearly understood beforehand.

While businesses may have an internal common currency and agreed exchange rates for budgeting, the external market may create significant discrepancies simply by using current market rates.

There are several countries where it is hard to move money, so companies need to consider where they operate and, in the event of a claim, where they would like to receive payments. Making that decision upfront can help companies to avoid complicated tax scenarios and reduce overall costs.

Wendie Le Vey is head of global services risk practice at JLT Specialty. The content of this article is based on a workshop JLT Specialty and Crawford & Company recently hosted.

JLT Specialty Contributor Wendie Le Vey, Head of Global Service Team, Risk Practice
Brokers will favour insurers who abide by the terms of the Insurance Bill now rather than waiting for it to become law, according to a senior spokesman for BIBA.

Graham Terrell, deputy chair of the BIBA casualty and accident committee, gave evidence on the Insurance Bill to the House of Lords in December. The Bill has been strongly endorsed by Airmic as giving buyers protection and increasing the efficacy and dependability of insurance policies.

Terrell, who is also casualty technical specialist at JLT, has worked closely with the Law Commission in the drafting of the Bill. He spoke to Jessica Titherington about the proposed changes and the battles still to be won.

Jessica Titherington: Will you favour those insurers that apply the law even before it is enforced?

Graham Terrell: Yes. Speaking with my JLT hat on, I’m confident that we will be pushing for insurers to accept and to agree to its terms prior to Sept 2016 [when it is likely to be enforced after a period of transition]. What has been agreed should be very clear by then and we would expect the market to honour it accordingly. I hope the market will be receptive. The initial signs are optimistic with the promises that insurers are already making in the press. It is certainly in their commercial interest to do so.

JT: Will the Bill impact the international competitiveness of the UK and London insurance market?

GT: I think it can only be a positive for the UK as it addresses a number of glaring and archaic imbalances between the rights of the insured on the one hand and the right of the insurers on the other. Any advantages that insurers can use to show that the terms of business for commercial buyers are fairer in some way can only serve to be a good thing.

JT: BIBA, the British Insurance Brokers Association, is an advocate of the Insurance Bill in its current form, but has pushed for the reinstating of clause 11 concerning irrelevant warranties. Why is that?

GT: As it stands, a breach of warranty that in practice has nothing to do with the claim can, legally speaking, lead to the claim being avoided by the insurer even though it’s entirely unrelated to the breach. This is absolutely unfair and so we called for the clause in its reworded version to be reinstated.

JT: Why has there been resistance to this clause in some parts of the market?

GT: People are inherently cautious about change. Some are concerned because the current position has the benefit of being very clear and straightforward: any breach of warranty leads to an automatic right to avoid a claim. When you bring in the issue of causation, you inevitably bring in the possibility of arguments on both sides about what caused the breach and to what extent.
However, in our view, you have to balance that against simple commercial fairness. At the end of the day the insurance buyer is the customer: they have bought into a promise that the insurer will pay the claim should certain circumstances happen. The mere fact that a totally irrelevant warranty has been breached should not be used as an excuse not to pay an otherwise perfectly valid claim.

JT: If the law in its final form does not address all concerns of buyers, will you encourage redressing this through contract wording?

GT: Yes absolutely. I think Airmic and BIIBA have a strong commercial bargaining position to try and push for as many positive amendments within the Bill as far as possible. The open and constructive discussion with the Law Commission has resulted in a very good opportunity for that even, for example, in the unwelcome event that clause 11 isn’t reinstated.

How possible that will be will have to be assessed on a case-by-case basis. Ultimately, it’s a matter of commercial negotiation but buyers are now in a good position and insurers know that an amount of commercial goodwill will be obtained.

JLT Specialty Contributor Graham Terrell, Casualty Technical Specialist, Risk Practice
WHY FIRMS SHOULD SWITCH TO GREEN ENERGY DESPITE DROP IN OIL PRICES

Published 30 December 2014, StrategicRISK

Tumbling oil prices may affect growth in the renewable energy market, but businesses should seriously consider switching to cleaner forms of fuel.

In its latest report, the Intergovernmental Panel on Climate Change (IPCC) warns that if climate change is not addressed, it could cause “severe, widespread and irreversible” damage for people and ecosystems.

Global warming that is limited to 2°C will reduce climate-change related risks. For instance, the risks associated with temperatures at or above 4°C include substantial species extinction, global and regional food insecurity, consequential constraints on common human activities, and limited potential for adaptation in some cases. On the other hand, risks associated with extreme weather events, are moderate to high at temperatures 1°C to 2°C above pre-industrial levels.

In addition, under one of the scenarios in which global warming remains at 2°C, fossil fuel reliance will reduce. The global share of electricity supply from low-carbon energy sources would increase from its current share of approximately 30% to 80% by 2050. Fossil fuels would be phased out almost entirely by 2100.

However, reducing fossil fuel consumption would mean bucking a global trend. Consumption of fossil fuels has risen consistently for more than 25 years, according to BP’s Statistical Review of World Energy 2014 and a significant reduction is arguably less likely considering the recent drop in global oil prices.

BP reports that global oil consumption grew by 1.6% in 2013 and that proven oil reserves at the end of 2013 were sufficient only to meet 55.3 years of global production.

In addition corporates are using new methods to extract such fuels. A boom in shale exploration has seen the US significantly increase its oil reserves. In 2013, the US produced one of the world’s biggest year-on-year increases in oil production, which coincided with the country recording the world’s largest increment in oil consumption that year, outpacing China’s growth for the first time since 1999.

Furthermore, global coal consumption grew by 3% in 2013, which was the fastest growing fossil fuel that year and proven coal reserves were sufficient to meet 113 years of global production. Proven reserves of natural gas, the dominant fuel in Europe, Eurasia and the Middle East, were sufficient to meet 55.1 years of global production at the end of 2013 and global consumption rose by 1.4%, higher than the rate of increase in global production (1.1%).

This rise in fossil fuel consumption is not surprising given the acceleration of human population growth in the past century. However, the rate of consumption increase was below the 10-year average for the past three years, and low-carbon energy sources grew their share of global output.

A growth in low-carbon energy output is likely because renewable energy, such as solar power and onshore wind, has become attractive for investors, which has fuelled growth in the sector, according to JLT renewable energy insurance practice leader James Green.

Renewable energy has received a lot of Asian investment since the 2011 Fukushima Daiichi nuclear disaster because it presents a safer and cleaner alternative to nuclear and fossil fuels, according to Green. In 2013, nuclear output accounted for 4.4% of global consumption.
– its smallest share since 1985 – and renewable energy accounted for a record 5% of global electricity production.

**ATTRACTING INVESTMENTS**

Solar and onshore wind farms are attracting investment from financial institutions because of their long-term returns, says Green. Moreover, government subsidies and reduced tariffs for renewable projects are also incentivising investors.

In the UK for example, feed-in tariffs (FiTs) subsidise property owners with installed renewable energy generators. FiTs include a fixed income for every kilowatt hour of electricity generated and an additional fixed income for every kilowatt hour of electricity sold back to the national grid.

“Generally, firms will invest in operational projects that have been built by a developer because they can buy and hold the assets for a long period of time. They do so to benefit from the subsidies and tariffs in the various regional and national regimes, and also from electricity sales,” says Green.

“Investors are beginning to take on the construction risks for renewable energy projects and can generate an internal rate of return of between 7% to 10% on a ground-mounted solar PV project, which is typically more profitable than investing in the stock exchange.”

Corporates taking proactive steps to transfer some of their energy reliance include UK retailer Marks & Spencer. The firm announced it would complete installation of the country’s largest single roof mounted solar panel array on one of its distribution centres in early 2015. It forms part of the retailer’s initiative to self-generate 50% of electricity used by its buildings by 2020.

An emerging risk that promotes self-generation is energy security. This relates to high concentrations of fossil fuel reserves in politically high-risk countries, such as Iran and Russia, which hold the largest proved reserves of natural gas. A breakdown in relations with either nation could arguably jeopardise energy supply for firms in importing countries.

“Green target policies are important but a growing reason for companies to invest into renewable energy is energy security,” says Green.

In the event that a major energy exporter decides to halt supply, Green says “firms that can generate electricity through renewable energy reduce the risk of interruption and are less reliant on others.”

This pursuit of fossil fuels makes the IPCC’s targets to reduce CO2 emissions less feasible. However, current fossil fuel reserves are not sufficient to support global energy demands for future generations, meaning businesses will need to switch to alternative energy sources to sustain operations.

As UN general secretary Ban Ki Moon said at the launch of the IPCC report: “Science has spoken. There is no ambiguity in the message. Leaders must act. Time is not on our side.”

JLT Specialty Contributor James Green, Renewable Energy Practice Leader
After-the-event (ATE) premiums in insolvency litigation will no longer be recoverable from the paying party from April, according to JLT Group.

This is likely to have a detrimental effect on how and, if at all, cases are pursued.

The group also claimed that it is imperative that practitioners consider their options now in order to unlock the full value of their portfolio in order to maximise creditor return, and have introduced a new service as a result.

Working closely with a litigation funder, JLT has decided to offer disbursement funding for insolvency cases.

The group stated: “Being that cases are reviewed by experienced solicitors and counsel at first instance it is possible to remove unnecessary delay and excessive due diligence from the process.”

JLT’s case assessment team, including two experienced underwriters and a practicing solicitor, will assess the case and then, subject to it meeting its criteria, can arrange swift access to funds without what it calls the “bureaucratic hindrances presented by additional underwriting layers”.

Under the current rules for insolvency cases pursued in England and Wales, the premium for ATE insurance is still a recoverable cost in litigation.

This means that if the case is successful, the insolvency practitioner can claim the cost of the insurance premium from the losing party as part of the legal costs, separately to the damages awarded.

This differs from other areas of litigation where the insurance premium is not recoverable for insurance policies taken out after 1 April 2013, and therefore typically falls to be paid out of any damages recovered.

Ed Brittain of JLT said: “Obviously, while there is still time left to secure cover before regulations change, in future it is going to become necessary for insolvency practitioners to look at alternative ways to enable mitigation of risk around the cases they pursue.”

“We at JLT are confident that our new proposition to the market will offer the most comprehensive solution which will also promote hassle free access to funds through close collaboration with clients we’ve been able to identify the key concerns posed by this change in the law and address them in order to create a well-honed product that is truly best in class”.

The recoverability of litigation insurance premiums in insolvency cases provides a significant benefit to insolvency practitioners and creditors, as it potentially avoids dilution of the damages recovered and therefore maximises the net recovery for creditors.