



The Guardrisk Update

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Incorporating Life Update

Mar/Apr 2004

A growing number of companies are shifting the onus of medical insurance to employees and there is increasing confusion about what companies are obliged to cover, and to what extent they can shift their responsibility (*Business Times*, 4 Apr). It is unclear whether an employer with a long history of subsidising its employees' post-retirement medical aid contributions can suddenly stop doing so.

GROWING consumer awareness has seen a 34% surge in the number of complaints received by the ombudsman for short-term insurance (*Business Day*, 21 Apr). At the same time the number of complaints settled by the ombudsman shrank from 31% to 22,5%, indicating that fewer complaints were justified.

FOR the first time since 1997, SA's short-term insurance industry has reflected a positive underwriting result (*Business Day*, 23 Mar). The big contribution to the positive result was generated in the property and accident, and health classes of business. The extent to which the underwriting cycle would continue depends on insurers' ability to provide cost-effective services.

ONE in four curricula vitae submitted by South African job seekers is said to conceal some kind of credential fraud, ranging from critical omissions, to exaggeration regarding performance and position, to outright lies and fraudulence (*Business Day*, 16 Mar).

GUARDRISK's postal address has changed to PO Box 786015, Sandton, 2146 – please update your records accordingly.

Business Interruption: a simple equation that so many get wrong

Business interruption (BI) is perceived as one of the biggest threats facing business today, yet companies are very often either inadequately or incorrectly insured. This often results in average being applied, the loss not being covered or, on the other end of the scale, the insured paying unnecessary premiums.

BI cover insures the loss of turnover and the increased costs (increased cost of working) specifically incurred in maintaining turnover following a loss. BI cover is always limited to an indemnity period nominated by the insured. This should allow sufficient time not only to replace the machinery and equipment damaged, but also to regain lost market share and return to normal profitability. If a company discontinues operations or a line of business, the policy would automatically be voided.

The increased costs of working cover could include advertising, sourcing products from elsewhere and contract manufacturing. This cover is limited to the value of turnover saved through the expenditure, in other words, one cannot spend more than a Rand to save a Rand. This cover can be supplemented by additional increased cost of working cover that picks up any other costs that are related to the loss.

Every loss of revenue claim is based on a simple equation: "lost turnover less savings (uninsured costs)". This would also be the basis on which the sum insured is calculated. The common error made when declaring the sum insured is that uninsured costs are often equated with direct costs. The problem with this is that not all direct costs are truly variable. A good example of this is direct wages, since it is not possible to reduce the labour force at short notice. True uninsured costs are those costs that will reduce in proportion with a reduction in revenue. Many companies declare their accounting gross profit as the sum insured, instead of the properly worked insurance gross profit, which is often higher.

There are many variations and extensions of BI cover but what all BI policies have in common is that the interruption is triggered by a loss under another policy held by the insured, usually an assets or engineering policy. The trigger policy will always be specified under the damage clause of the policy and the term 'damage' could include events not covered in another policy by way of a policy extension.



One of the problems with BI cover is that the onus is on the client to calculate the sum insured and the broker isn't always consulted. Experts warn that it's a simple equation but defining the variables makes it more complex. It is important that clients sit down with their brokers at least once a year to review the basis of their BI cover and to ensure that the sums insured are correct, and that expert guidance is sought if necessary.

It is important to remember that insurance is no substitute for sound risk management and a formally documented recovery plan that can be implemented in the event of a loss is an invaluable tool.

Risk Barometer

THE costs of global warming threaten to spiral out of control, forcing the human race into a catastrophe of its own making (*Business Report*, 4 Mar). The economic costs of global warming threaten to double to \$150bn a year in 10 years, hitting insurers with \$30-\$40bn in claims, or one World Trade Center attack each year.

PROPOSALS to allow UK companies to exclude directors' liability for negligence from insurance cover send out the wrong message to directors and investors (*Insurance Day*, 17 Mar). This follows fears that companies will have problems attracting the best individuals as non-executive directors in the wake of incidents such as a life insurer suing its former directors for £3.3bn.

MANY insurers in the UK and US have begun to remove cover for computer damage from commercial insurance plans as the increased use of intranet and internet provides more opportunity for cyber-bandit activity (*Insurance Day*, 13 Apr).

US risk managers are placing increasing importance on the financial strength of their insurance partners and the efforts to bring stability into the sector (*Insurance Day*, 21 Apr). The recent high-profile exit of some household names from the insurance market means US businesses now place greater importance on financial strength ratings.

THE insurance industry "got off lightly in 2003" and must try harder to understand the needs of the companies it covers (*Insurance Day*, 22 Apr). While the industry has seen thumping profits on the back of hard rates and few claims, the market faces major threats in the years ahead. Climate change and terrorism continue to pose significant dangers.

INCREASED attention to corporate governance issues can give risk managers an opportunity to develop enhanced risk management programmes within their organisations (*Business Insurance*, 26 Apr). Three years ago, corporate governance was not even on most corporate agendas, but recent accounting scandals and provisions in the Sarbanes-Oxley Act of 2002 have made governance a major concern for many corporations.

Life Update

Life Barometer

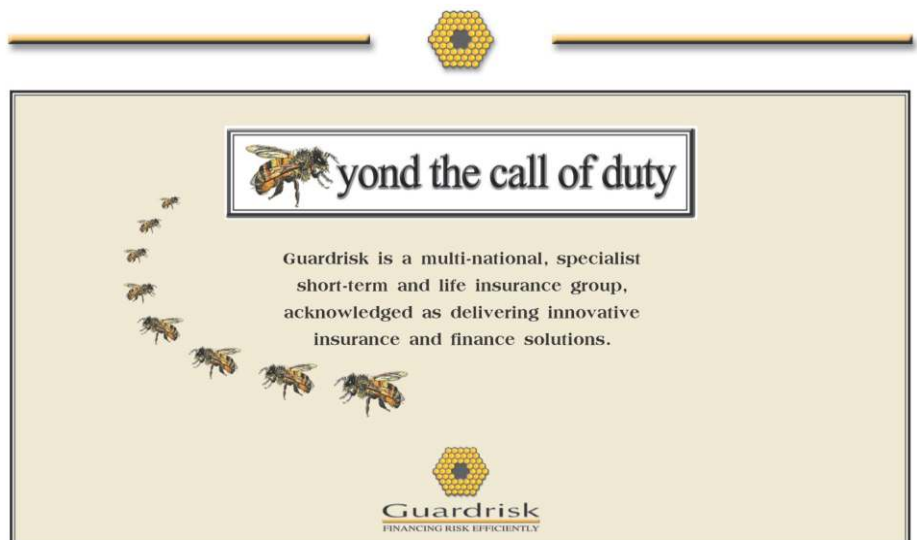
FRAUD cost the SA life insurance industry R214m in the first nine months of last year (*Business Day*, 8 Mar). Statistics, collected from all major insurance companies, reveal that there were 447 cases of fraud, with claims to the value of R72,6m. A further 1963 cases involving non-disclosure of relevant information and misrepresentation, with a claims value of R134,6m, were uncovered. These related mainly to HIV, where blood samples from HIV-negative people were passed off as samples of HIV-positive people in order to obtain insurance cover.

ONE sector of the financial services industry that will be uniquely challenged by the equity ownership requirements of the financial services charter is long-term insurance (*Business Report*, 25 Mar). The restrictions placed on these institutions by the Long-Term Insurance Act will require them to be innovative in structuring black economic empowerment transactions to meet the required ownership levels. Specialist knowledge and lateral thinking will be essential.

THE Financial Services Board intends to remove the audit exemption from retirement funds (*Business Day*, 31 Mar). After years of debate this is one of the most important changes to the Pensions Funds Act from a governance perspective. Previously, some funds were not subject to an audit. Now all funds will be subject to an audit. The removal of such audit exemption means that funds previously excluded will now be subject to scrutiny by trustees and independent third parties.

TRADING conditions for the long-term insurance industry continued to deteriorate in the six months to 31 December 2003 compared with the same period in 2002 (*Business Report*, 26 Mar). Total industry income fell 8% to R80.1bn for the same six months compared with the previous year and by 5% from R84.3 when compared with the six months to 30 June 2003.

A company cannot attach the pension funds of an employee found guilty of fraud or misconduct once the pension funds have been moved to another company, according to a ruling by the Supreme Court of Appeal (*Business Day*, 29 Mar). The finding has implications for companies that wish to take legal action against employees to recoup losses after the employee has resigned or retired. The only exception was when the pension benefits were still being held by the employer's pension fund, as the employer was still contributing to the fund, the court found.



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