i notes
Newsletter from India's Leading Insurance Broking House
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Summary

- Message from the Editor
- De-Tariffing
  – Views from the industry
- Managing contracts as a Risk Management Tool

India Insure
The risk managers

Message from the Editor

Dear Readers,

In less than two months from now, India will take its first tentative steps towards a completely shackle-free General Insurance market by partially withdrawing the tariffs that have been in place for more than three decades.

Although the market was liberalized in 2000 with the entry of Private players, for the insurance buyer, especially the commercial buyer, the real party starts only from New Year's Day 2007. With free pricing being permitted across all lines for the first time since Nationalisation, industry players are speculating on the shape of things to come. *Will there be a price war? Will good risk management be rewarded finally? Which products will become cheaper and which will become costlier?*

In light of the above, we at India Insure, opted to capture and reflect the voice of the industry rather than write our own article again, for this issue (our September issue carried "*Detariffing – a curtain raiser*"). We, therefore, present to you the views and predictions of 4 senior industry stakeholders – representing 1 PSU Insurer, 2 Private Insurers and a large buyer of Commercial Insurance.

We sincerely thank Mr Yogesh Lohiya (GM, Oriental), Mr Dalip Verma (MD, Tata AIG General), Mr Sandeep Bakhshi (MD, ICICI Lombard) and Mr Narayanan (Dy. General Manager, Crompton Greaves Ltd.) for sparing their valuable time and sending us their views.

The "interview" format is a first for ***i-notes***, and we hope you find it interesting and useful.

We also carry an article on "Managing Contracts as a Risk Management tool" – aimed at helping the construction industry.

V Ramakrishna
Editor – ***i-notes*** & Managing Director, India Insure

De-tariffing - *Views from the Industry*

- **With Detariffing just round the corner, what pricing trends do you foresee in the immediate future (Jan 2007- March 2008)?**

Yogesh Lohiya
General Manager
Oriental Insurance Company Ltd.

In a tariff free regime, pricing of insurance products is one of the areas which demands expertise in risk evaluation, to arrive at the most appropriate premium rates. The Indian insurance market is known for being very price sensitive. They are very particular about obtaining the best terms like minimum deductibles and maximum coverage at very competitive premium rates. The IRDA being fully aware of the ground realities and also of the experience of the insurance market when the marine portfolio was de-tariffed, has put in place a very elaborate frame work for insurers to adhere to while arriving at the price for their products. Obviously the IRDA frame work is prepared to ensure that the insurers maintain adequate solvency margin & AVOID RECKLESS UNDERWRITING.

In my view prudent insurers may alter the present rates as under:

Fire Insurance: Reduce rates by 20% to 25%.

Engineering: Reduce rates by 20% to 30%

W.C.: Reduce rates by 25%

Motor: a) Private Vehicles: Downward revision of the rates by 10%

b) Commercial Vehicles: Upward revision of the rates by 20%

- **What preparation has the Insurance Industry, and more specifically, your company done for the forthcoming transition?**

The IRDA has been from time to time giving directives to the Insurance Companies. They have given a road map listing the mile stones to be achieved for the insurers before the proposed de-tariffing date. All the insurers have been asked to draw an 'UNDERWRITING POLICY' for their companies listing out their underwriting philosophy, their profit expectations etc. The insurers were advised to have internal guide tariffs to facilitate the underwriting staff to accept business in normal course. .

Our Company has painstakingly collected statistics of premium and claims for various products and have compiled the same to arrive at guideline tariffs. We have identified nominated underwriters at all Regional Office level and at Head Office and have put them through a specially designed training module to equip them with the necessary skills. More than 300 officers have been trained in house so far.

- **Do you foresee a greater role for brokers post-detariffing?**

Brokers as intermediaries are still not wholly acceptable for the corporate &/or individual clients. The main reason

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being as pointed out elsewhere is the price sensitivity of the customer. The unhealthy competition in the market has also affected the professional image of brokers. The concept of brokers in insurance is relatively new in the insurance market in India. Professionalism in any field pays and in the insurance sector too professional brokers will prosper and find acceptance in the market, if not immediately, may be in a few years from now.

What advice would you have for Insurance Buyers? Brokers? Other Insurers?

Insurance buyers: Ensure that the product being bought is the one you are looking for. Check for coverage and exclusions. Do not go for the cheapest cover but look for the credibility, experience and standing of the insurance company.

Brokers: Follow the regulations laid out by the regulator. Be professional. Do not press for unviable rates. Educate customer.

Other Insurers: Follow the directives of IRDA. Do not aim at business for the sake of business with growth as the only objective. Resort to prudent, conservative premium ratings. Take care of acquisition cost, expenses of management, reserve and profit margin. Aim to create a healthy atmosphere devoid of reckless price-cutting.

Sandeep Bakhshi
Managing Director
ICICI Lombard General Insurance Company Ltd.

With Detariffing just round the corner, what pricing trends do you foresee in the immediate future (Jan 2007 – March 2008)?

In a detariffed scenario, insurance companies will arrive at premiums based on their assessment of risk on a case to case basis. Customers with a good risk profile would enjoy lower premiums. Initially the market may be volatile as insurance companies test their premium rating models in a competitive environ-ment but over time this would stabilize. The comfort of an anchor tariff rate has made the industry more transaction focused and we would now be required to transition towards a business and P&L driven approach. At the corporate level, intra-portfolio cross subsidization would be replaced by product level pricing, as a result of which Fire insurance premiums could see some reduction. Conversely Group Health and Marine insurance premiums are likely to move up with companies reviewing their coverage in order to optimize pricing. Motor Insurance is expected to gravitate towards risk based pricing.

What preparation has the Insurance Industry, and more specifically, your company done for the forthcoming transition?

The regulator has adopted a well planned and stable approach, giving the industry adequate time to prepare for the detariffed regime. Insurers are building robust and practical rating models that are able to arrive at the correct premium with the available data. The ongoing validation and refinement of these models would be based on the subsequent claims experience. To retain customers in a competitive scenario, insurers are focusing on superior customer service as a key differentiator. There will be an increase in the use of virtual channels to reach out to and service customers in order to reduce operational costs and pass on these benefits to the end customer. Investments in technology and operations will provide the backbone for an efficient and effective business operation.

Do you foresee a greater role for brokers post-detariffing?

Brokers will continue to play a significant role in enabling their customers to identify the best options for their insurance needs. With no changes in policy terms for the first 15 months, pricing and service levels are the key areas that brokers will focus on while assessing insurance options. Once there is full detariffing, the role of brokers will increase as they will need to compare the various product-pricing options that will become available. Transparency in data and earnings would define the relationship between Insured, Insurer and Intermediary.

What advice would you have for Insurance Buyers? Brokers? Other Insurers?

We are at an early stage of development and not competent to advise any of these constituents. We believe that we would learn from the global best practices, innovation of the competitors, expectations of the customers and inputs from the intermediaries and channel partners. We believe that transparency, corporate governance and fairness in dealings will ensure a win-win for all the constituents and enduring partnerships.

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- **With Detariffing just round the corner, what pricing trends do you foresee in the immediate future (Jan 2007 – March 2008)?**

Dalip Verma
Managing Director
TATA AIG General
Insurance Company Ltd.

Based on our experience in other markets and IRDA's determination to prevent a price war, we expect that the price decline will be contained within 20 to 25%.

- **What preparation has the Insurance Industry, and more specifically, your company done for the forthcoming transition?**

As far as Tata AIG General is concerned, we already have the infrastructure and people to do disciplined underwriting which is one of the cornerstones of the new regulations introduced by the IRDA. We have also met all the milestones laid down by the IRDA in its detariffing Road Map and subsequent guidance notes.

We have a very robust claims servicing infrastructure which has won accolades in different consumer surveys. Overall we are very confident that we will traverse the detariffed landscape successfully in our journey towards building a sustainable world class operation.

- **Do you foresee a greater role for brokers post-detariffing?**

The experience in most detariffed markets shows a migration of commercial lines business to brokers. Post detariffing we expect to see the same pattern develop here. Also the Indian trend has been that so far brokers have been used in most non-tariffed segments of business and detariffing will open up a window of opportunity for them.

- **What advice would you have for Insurance Buyers? Brokers? Other Insurers?**

Insurance buyers should follow the 6 "I"s of risk transfer judiciously - Introspection, Intermediary selection, Imparting Information, Inspection, Implementation and Intelligent choice of insurance service provider. If they navigate the above corrrectly they should at the end of detariffing be rewarded for good risk management, good claims experience etc.

- **With the proposed Detariffing wef Jan 2007, what are your expectations from the Industry?**

V. Narayanan
Dy. General Manager
Crompton Greaves Ltd.

Reduction in Premium by 40% in Fire Tariff

Other Non- tariff Premium to remain unchanged atleast for one year.

- **How are you, as a Corporate Insurance Buyer, preparing for Detariffing?**
  - Almost completed property related inspections as per detariffing requirements (as per discussion with our underwriter).
  - Started collection of data with respect to past claims with the help of Brokers.
  - Have been in discussion with Brokers for their advise regarding to detariffing.

    We are looking forward for inputs from Brokers as they have a wider perspective and source of information.

- **Do you foresee a greater role for Insurance Brokers post-detariffing?**

Yes

  - Standard rates would be done away with in the 1st year and the new rates will require negotiated settlement. The expertise and experience of the Brokers will be useful in arriving at the appropriate rates.
  - In the next year when the Underwriters will have the liberty to have their own wordings the role of the Brokers will be widened.

- **What would be your advice to other buyers? Insurers? Brokers?**
  - In my Opinion the Brokers will have to strengthen themselves in terms of man power & Knowledge especially with respect to International practices.
  - The brokers should be able to help the client in bringing wordings to suit the client needs.

Disclaimer

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Managing Contracts – a risk management tool

Contracts are an integral element of doing business, particularly in a complex industry such as construction. Their importance cannot be overemphasized, regardless of whether you are a contractor, subcontractor or a wrap-up sponsor. Well-written contracts clarify agreements, improve project outcomes and create good working relationships between the contracting parties. Unfortunately, construction contracts are often an under-addressed or even overlooked step in the risk management process. Here, we focus primarily on how contracts can be used to transfer risk.

Understanding The Construction Contract

A contract is a legally enforceable promise between two or more parties. In construction, these agreements often require one of the parties to pay or indemnify the other party for a loss they suffer in fulfilling the terms and conditions of the contract. For a contract to be legal, there must be an offer, an acceptance and consideration. Contracts have important legal and insurance consequences that will impact your business. When used properly, contracts are an effective way to manage risk. Contracts may be written or oral. Written agreements, when properly drafted, provide a clear understanding to which each of the parties has agreed. Unwritten agreements, while legally enforceable, often create problems. Agreements and understandings negotiated in good faith are sometimes misinterpreted at a later date, particularly after a loss has occurred.

Identify Your Risk Management Goals

Before negotiating an agreement, you need to understand your company's approach to risk management. Risk management is a systematic and practical process by which your business cost-effectively manages its resources and activities to achieve a business objective. It involves organizing, planning, directing and controlling resources to minimize the financial impact of an event upon your business. Drafting your contract should begin long before you reach the negotiating table. You should have a clear vision of your company's risk management objectives in mind. This will allow you to make decisions that:

*****Are cost effective.* ***Balance expenditures for risk financing with those for risk control.* ***Support the proper allocation of funds among an organization's risk management activities and its general operations.*

Key Elements of a Contract

If you decide to use a contract to address indemnification, your construction contract should address the following elements before you begin doing any work. Although there may be more, depending upon the scope of the project, the agreement should minimally address:

- Who the parties are, including names and addresses.
- The work being done. The description of the job should be specific, particularly if some of the work is being done off-site. You would also need to address change orders, completed operations and defective work claims.
- All the terms and conditions of the agreement. Agreements that are incomplete, or those not executed in a timely manner, often lead to problems. Be sure to include every aspect of the job, even if it seems inconsequential.
- Incorporation by reference problems. The contract should include all of the agreements as part of the document. Generally, courts look unfavorably upon agreements that attempt to expand a party's liability by reference to another document. By carefully considering and addressing this issue beforehand, you have an opportunity to help a court interpret the agreement consistent with your intent.
- The actual indemnification agreement.
- Insurance requirements, if appropriate.

Managing Risk Through Insurance Agreements

To adequately protect your business from loss, you should understand what your liability insurance policies and those of the other parties cover. Generally, contractual provisions obligating one party to obtain insurance for the other do not violate anti-indemnity statutes. If the firm you are doing business with is using an insurance company, there are important issues to consider whether you are a general, prime or sub-contractor or even a wrap-up sponsor which include

*****The limits* ***Named Insured / Additional Named Insured* ***Primary Insurance* ***Severability of Interest / Cross Liability Clause* ***Indemnification and Hold Harmless* ***Waiver of Subrogation* ***Cancellation Provisions* ***Certificates of Insurance.*

With careful planning, you can create a contract that effectively manages risk while improving project performance, reducing costs and establishing a strong working relationship among all the parties involved.

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