i-notes
Newsletter from India's Leading Insurance Broking House
September 06

Summary

India Insure
The risk managers

Message from the Editor

Dear Readers,

For a company helping in creating a new industry category altogether, a big pay-off (*apart from commercial success, of course!*) is the support from various stakeholders for our efforts in creating a world-class Broking company. As the **15th** issue of ***i-notes*** goes to press today, we are grateful that our simple offering has received so much support from you.

When we launched ***i-notes*** 2 years ago, we wanted it to be a non-commercial, editorial-based platform, aimed at informing the corporate insurance user and de-mystifying insurance concepts and products. For every issue, we selected topics which would be topical and / or useful, and attempted to present them in a manner that most corporates and insurers would find interesting. Over several issues, we covered topics like – *Plain English, Alternative Risk Transfer, Fury of the Floods, How to evaluate an Insurance company / broker, etc*. As the insurance industry gets more interesting, we find there is so much more to write about and so little time and space.

In this issue, we have started the debate on **Detariffing** - the next big event in General Insurance after privatisation. We find that a large section of the mid-market is unaware of the finer points of and the implications of de-tariffing, although it is just 3 months away. We start with a curtain-raiser in this issue – merely presenting the salient features from different stake-holders' perspective. We plan to follow it up with a more detailed discussion in our November issue. We also discuss a novel Insurance product – the **Marine Sales Turnover Policy**, which merits attention from all large and medium companies for its sheer simplicity and usefulness.

We hope, as always, that you find the issue useful.

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

Detariffing.... a curtain-raiser

INTRODUCTION

The Indian Insurance industry has seen a great deal of change since the year 1999. All of a sudden, the otherwise dull and unheard of Insurance Industry has been in the news and making waves even in Parliament. The years of government monopoly came to an end and Private Insurers made an entry in the year 2000. The year 2003 saw yet another leap of faith with Brokers entering the fray.

Yes! Insurance in India has become a "happening" industry.

THE JOURNEY SO FAR

The opening up of the industry was done with the idea that this could help the economy meet its growing insurance needs, initiate the growth of rural areas and promote India as a regional reinsurance hub. True to expectations, the insurance sector in India has shown rapid expansion over the past few years. Increasing demand for consumer and industrial products & services plus elimination of a few of the trade and investment barriers have been the main drivers behind an exponential growth of the insurance sector in India.

Private General Insurance players have grown rapidly to capture a third of the market and helped in pushing the industry growth rate to 16.5%.

Amidst this, the non-life Insurance sector has been running a 3-legged race, thanks to the continued presence of Tariffs.

TARIFFS

A tariffed market is one where the premium rates, policy terms and conditions and deductibles are controlled. Presently, in India about 70% of the market (property other than mega risks, engineering, motor and WC) is tariffed ie. policy wordings and minimum rates are fixed and each company is free to quote the guided rate or higher. In other words, a tariffed market robs the market of the fundamental component of liberalization i.e. free market and open competition.

As a result,

- Premium is collected based on a pre-fixed rate-chart – both "good" risks and "bad" risks within a category pay the same rate.
- Fire premium rates remain at artificially high rates in India – leading to super-profits for insurers and cross subsidization of other loss-leading lines like Health & Marine insurance.
- Motor portfolio is not adequately priced (various pressure groups have ensured this) leading to huge losses for insurers.

Tariffs have been done away with in most markets around the world and India is today the only country where such a high proportion of the market is still under Government control.

DE-TARIFFING

Detariffing is the opening up of the market to **free pricing** and **flexible policy terms and conditions**. While the need for dismantling of Tariffs has been acknowledged and supported by all stakeholders, IRDA has chosen to tread cautiously here – lest the industry new-borns bleed to death in a cut-throat race to the bottom.

It has waited a full 6 years after liberalization to open up the market – as it feels the players now have the maturity and the required shock-absorbing capacity. It has, however, chosen to open up in stages – initially it will only be free pricing (Jan 1, 2007) with existing policy terms / conditions. Flexi-wordings is being proposed for April 2008.

All Insurers have been given a road-map to follow and preparations for January 1, 2007 are on in right earnest.

We believe that, after licensing of Private players in 2000/ 2001, de-tariffing is the next big event in the Indian Non-life insurance space. …..

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WHAT LIES AHEAD ..... implications and concerns

The impact of de-tariffing will be different for each of the parties involved. The industry involves the Insurer, the intermediary and the regulator with the fulcrum being the customer or the Insured (we focus here on the Corporate Customer).

Let us analyze what lies ahead for each of us.

For the Customer

For the Corporate Customer, the initial picture appears to be rosy. When the curtains unfold, the market is expected to turn quite chaotic. The market expects a storm, with the eye that remains calm, being the customer. There is going to be flurry all around with insurers and brokers concentrating only on giving their customer the best (read: *lowest*) price.

- there is some degree of disappointment among large corporates on the delay in opening up of policy wordings (which means delay in new products development).
- Focus will be on negotiating with the insurers and brokers for the lowest price only.
- The logical next step would be to showcase "sound risk management" practices to enjoy a lower premium rate. However, in reality, we will have to wait & watch to see what happens. A full-blown price war among insurers (for top-line growth) may sideline the importance of risk-management, at least initially.
- While there would be a drop in the fire & engineering lines (subject to favourable loss ratios), health and motor premium may go up.
- Come mid-2008 and the restrictions on the policy wordings will also be lifted. It is then that the concerns of the customer begin. Apart from prices the intricacies of the policy coverages would play a very crucial role. The customer would need to be more aware of the product he is purchasing.

He will however stand to benefit from a much wider choice of products. It would be convenient for him to get a tailor-made product very specific to his requirement.

For the Insurer

We expect fierce competition among insurers. Insurance rating being a function of the probability theory, would require the insurers to keep themselves equipped with sufficient data before taking the plunge.

There are apprehensions that, at least initially, premium (top-line) growth would dominate at the cost of viability or "risk rating" – which can affect solvency margins. Each proposal will need to be studied and the rating to be done on sound technical grounds.

- Marketing teams & underwriters, sandwiched between the internal guide book and competitive market trends, will need to be guided along the right lines.
- Decision making could turn a bottle neck with the head offices having to take crucial decisions of how much and to whom to decentralize.
- Internal training of employees will have to be taken up in right earnest.
- With the 20% upward / downward slab being lifted by IRDA there will be a plunge in the premium incomes.
- Inspection of risks above specified limits would become critical unless the broker takes on this role.
- Insurers need to set aside personnel for product innovation.
- Internal monitoring mechanisms would need to become more stringent. Actuaries would start playing a more vital role and we may see them soon turn into underwriters.
- While the top line would see a plunge of about 25-30% initially (it may start hardening after a couple of years), the bottom line may take a drastic hit. Insurers would spend more time on risk profiling through risk inspections and data collection.
- PSU insurers, with their 3 decades of claims data and healthier reserves are expected to give private players a run for their money.

For the Broker

A de-tariffed market would certainly enhance the role of the broker. Both, the insurer as well as the customer would need the services of a professional broker. While it might mean difficult days for the small time, frivolous players who have been in the market only as routing agents, the big ones would be here to stay.

The brokers would not merely participate in the price war but would need to give quality submissions to the insurers conveying all the material and non material aspects of the risk to be covered. He would need to become the **eyes of the insurer** and the **voice of the customer**. He would need to assist the insurer in evolving a Code of Conduct for keeping the competition on a sound technical footing. He would be the catalyst between the customer and the insurer and assist in guiding the competition along healthy lines and ensure the sustenance of the parties involved.

The market may shift from a commission market to a fee model and the broker may get a pre decided fee from the customer. He will play the role of a consultant in the true sense and risk management would be required.

For the regulator

IRDA will require to closely monitor market behaviour and may have to step in if the methods of competition become harmful to the long-term good of the market

The regulator is keen to see that the industry should flourish in the new regime. He would ensure that there is prudent underwriting with sound solvency margins and good corporate governance in running the business. A constant vigil would be required until the market matures and each of the players understands his roles.

Clear rules would be required to be laid down for handling of cases if (god forbid) a company approaches insolvency. Acquisition and merger rules would need to be put in place.

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Marine Sales Turnover Policy

INTRODUCTION

Marine insurance dates back in history to as early as trade began on vessels moving into the informidable seas. The ship owner used to borrow money from the banker or money lender on his ship and cargo with the agreed condition that should the journey end well he would return the money along with an agreed interest and if the ship did not reach the destination due to the vagaries of the ocean, he would return neither the principal nor the interest.

Over the years it kept developing and today is an integral requirement of every manufacturing company and also other industries having material coming in or going out of their premises. Whether one is involved in importing, exporting or simply moving own cargo or somebody else's, one is exposed to risk.

Marine insurance covers loss or damage to goods in transit. The perils covered are perils on land like fire, accident, theft, pilferage and non delivery, maritime perils like sinking, stranding etc. of the vessel, damage due to entry of sea water in the cargo hold etc and various other related perils.

A Marine cover starts from the time the loaded goods leave the warehouse either by road, rail, sea or air as the case may be. It continues during ordinary transit including trans-shipment and concludes when the goods are unloaded into the warehouse of the consignee.

MARINE POLICIES – the conventional product and related problems

Marine policies are generally either "specific-voyage" policies or "declaration" policies for either imports, exports, indigenous transits of raw material or finished goods, customs duty, transits from anywhere to anywhere in the world and to and from job works. While for a specific policy, the cover is issued from commencement to landing at the final destination, the other policies are generally continuous policies issued on an annual basis or for a specified period of time for an agreed value of transits based on the insured's estimate of goods movement for the specified period. **It is mandatory for all transits in the agreed period to be declared**. The company will need to keep track of whether the goods are covered every time and also send periodic declarations to the insurer on the number and value of goods dispatched during a particular period. In addition to this, the company will also have to keep track of the balance available with the insurer for the purpose of covering all transits.

There have been operational lapses resulting in claims getting repudiated for declarations not made or insufficient balance of Sum insured at the time of claim and many a client has been caught unaware. Discovering that a particular damaged or lost consignment was unfortunately not covered, and hence the claim not payable, can be very frustrating for an otherwise-diligent insured.

It has been a nightmare for the executives handling insurance in companies to manage this portfolio and a serious need was felt to have a comprehensive policy to take care of all the above activities and still remain adequately insured.

MARINE SALES TURN-OVER POLICY – coverage & benefits

In this context, a marine turnover policy has come in as a blessing for companies. It cuts down the administrative cost and time drastically and gives you peace of mind.

The Marine Sales Turnover policy has been designed by one of the Private General Insurance Companies. It covers a **company's sales turnover** unlike the other marine open policies which cover the value of goods which are offered for insurance.

The company's **annual estimated turnover** can be covered as a single amount and all a company needs to do is to provide sales turnover figures periodically to the insurance company (usually quarterly). All the requirements of a company's Marine policies can be met by a single comprehensive policy.

The usefulness of this policy will be better appreciated if we compare this policy with the conventional marine policies.

Comparison of Marine Turnover Policy Vs Normal Marine policy

Conventional Marine Policies	Sales Turnover Policy
Separate policies, at times with different policy periods issued for various kinds of transits	Single Policy is issued for all kinds of Transit including the following: Imports Duty Deemed duty Exports (FOB & CIF) Domestic Inward Domestic Outward Inter-unit Movement Return Transits (limited cover) Intermediate Storage (Fire & Burglary cover)
Separate policy for companies of a group	Single policy can be issued for covering all the transits of all group companies
Monthly declarations to be submitted in agreed formats	Declarations are not required to be submitted
Insured has to keep a track of various sums insured and balances under all the policies	Insured does not need to track any sum insured except the actual sales figure
Insured may erroneously miss out on declaring some shipment	Insured does not have to make any declaration. All movements till the time insured turnover is exhausted are covered
Insured has to keep a check on available balances under all policies	Insured just needs to track the sales figure
Insured may forget to declare on CIF + 10% basis and may lose out in case of claims	All shipments are deemed to be valued at CIF + 10%

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Detariffing.... a curtain-raiser ....contd. # 2

For the Industry as a whole

The industry faced its first upheaval with the entry of the private players and de-tariffing would be the second major upheaval. The big boys will be here to stay and there could be a shake-out of the small time insurers and intermediaries. Imprudent underwriting in the long run could see some companies shutting shop.

The market would begin to see the cycles of ups and downs with the market softening initially and subsequently hardening depending upon the demand and supply and the highs and lows of the risks. Insurers may begin to cherry pick not wanting to see their bottom line in the red.

Detariffing may lead to over regulation. With the past experience of marine de-tariffing, the regulator will be more watchful.

Liberalisation is also expected to bring substantial market expansion and focused penetration together with technology up-gradation fine-tuned to international standards. New and innovative products would make their presence felt along with improved focus on customers and better service standards.

There is bound to be more product innovation, higher service standards and specific risk underwriting.

CONCLUSION

Maturing progressively, the insurance sector in India appears to be one of the most talked of sectors amongst the foreign investors. Numerous opportunities are available in this sector for both domestic as well as international players.

With the liberalization of the market, interest has been shown by U.K. US, Japan, European and other countries in the insurance sector in India. In view of the potential growth prospects, the insurance sector in India may introduce Foreign Direct Investment of up to 49 percent.

It is quite clear that the big action in Insurance, especially Non-life, is yet to start and we will experience paradigm shifts over the next few years. Watch this space for more on this front, and here's wishing all of us the best of luck and success in dealing with this change.

Marine Sales Turnover Policy.... ....contd. # 3

Sum insured: The annual sales turnover forms the sum insured. On expiry of policy the refund of premium on downward revision in case the turnover is less than the turnover declared is made. An enhancement in sum insured is permissible during the currency of the policy

Pricing: The premium rate is arrived at considering the total number of transits taking place including the inward outward movement for job works and the rate is applied on the Annual sales turnover and is hence marginally higher than the standard marine policies.

Other Conditions: An added advantage of this policy is that it is generally on "All- Risks" basis with War and SRCC and the risk of loading being inbuilt.

CONCLUSION

This policy has come in as a blessing for companies having large number of transits where there are several persons handling the marine portfolio and a tangible risk having missing out declarations for insurance. It will put an end to the laborious work of verifying balances and handling declarations and certificates. This probably is the beginning of many more customer friendly policies which we can look forward to in the post de-tariffed market.

Disclaimer

Contact us

India Insure Risk Management Services Pvt. Ltd.

Ahmedabad # 102, Shivam Complex, Nr. Silicon Towers, B/h, Samartheshwar Mahadev Mandir, Ellisbridge,Ahmedabad- 380 009 Tel: 079 30009660, Fax: 079 30009664
Ms. Chinar Baxi email : chinar.baxi@indiainsure.com

Bangalore # 13, 3rd Floor, Mother Theresa Road,1st Stage, Austin Town, Bangalore - 560047. Phone: 080 - 51128056 - 58 Fax: 080 - 51128597
Contact: Mr. Anurag Bishnoi email: anurag.bishnoi@indiainsure.com

Baroda 315, Race Course Tower, Nr. Natubhai Circle, opp. Citi Bank, Gotri Road. Baroda - 390007. Tele Fax : 0265-2352031, Mobile : 09898566579
Contact : Mr. Deepak Kwatra email : deepak.kwatra@indiainsure.com

Chennai Sri Valli Griha, Flat GA, Ground Floor, New # 34, (Old # 26), Raman Street, T Nagar, Chennai-600 017. Ph: 044-5202 3797/98 Fax: 044-52023799
Contact: Mr. Srinivasan Rangarajan email: srini.rangarajan@indiainsure.com

Coimbatore #1023 "Eureka Chambers" Avinashi Road, Coimbatore- 641 018
Telefax: 0422-4380539 Contact : Mr. T.R. Sridharan
email: sridharan.tr@indiainsure.com

Gurgaon # 519, Galleria Complex, DLF Phase IV, Gurgaon 122002 Haryana
Ph : 0124-4115254, TeleFax : 0124-4148348
Contact: Mr. Anuraag Kaul email: anuraagkaul@indiainsure.com

Hyderabad # 405, Archana Arcade, St John's Road, Secunderabad - 500025
Ph: 040-27822989/90/91, Fax: 040-27822993
Contact: Mr. Vippin Chandra email: vippin.chandra@indiainsure.com

Mumbai **Branch & Corporate Office :** # 427/428 Chintamani Plaza Chakala, Andheri-Kurla Road, Andheri (East) Mumbai - 400 093.
Ph: 022-56791416-20, Fax: 022-56791421
Contact: Mr. V. Ramakrishna email: ramakrishna.v@indiainsure.com

New Delhi # A-70, Sector-2, Noida NCR, Dist. : Gautam Budh Nagar (UP) - 201 301
Ph : 0120-4320666, Fax : 0120-4320667
Contact: Mr. Anuraag Kaul email: anuraag.kaul@indiainsure.com

Pune # 101, Premium Point, Opp. Modern High School, J.M. Road, Shivajinagar, Pune - 411005, Tele Fax: 020-56030713
Contact: Ms. Deepali.A.Rao email : deepali.rao@indiainsure.com