i notes
Newsletter from India's Leading Insurance Broking House
July 2010

Summary

India Insure
The risk managers

Message from the Editor

Dear Readers,

Greetings!

The insurance industry has been in the news all through the last quarter. The Customers in the Insurance industry are going through a rough time. The Life and the Non-Life Insurance industry are witnessing radical and rapid changes. First it was the regulations concerning ULIPs; now it's the battle between Insurance companies and the hospitals.

While IRDA has emerged victorious in a high-profile tussle over the regulation of the unit-linked insurance plans, with the government ruling that IRDA and not the stock market watchdog SEBI would oversee the product; the customer is seeing a sea change in the products and the returns being offered. The prolonged and public battle has left the customer confused on what the future has to offer.

The abrupt decision of the PSU Non-Life insurance companies to withdraw cashless facility under the Health Insurance scheme for the Retail consumers has again been a bombshell for the customers. The change in cashless networks is the prerogative of the insurance companies but customers in all fairness need contract certainty and advance notice.

The policy was issued, specifying the terms and conditions and the network hospitals where the customer could avail the cashless facility. The overnight change in the network has left the consumer stranded in the middle with no choice but to arrange for the payment from their pockets. The hospitals are happy in spite of the public expression of protest as they get upfront cash instead of waiting for the TPA's to pay them. They will also charge what they want as the individual consumer is in no position to bargain on fair medical costs and the TPA shall disallow costs at their discretion creating a double whammy for the customer.

The Insurers fight with the hospitals is justified and the unending losses from health portfolio are threatening the very viability of this Line of insurance. Urgent active measures are the need of the hour. What could have been done was to reduce the network on all new policies issued after the specified date and enough advance notice could have been given to the consumers. It is a moot point that the hospital industry has got the message as they are not dependent on the Insurance industry for their survival. The whole matter has now got embroiled in legal controversy with the Delhi high court giving directives for cashless treatment restoration. Another well intended measure that will now get side tracked.

The time is probably right for the insurers to come up with a wider array of health products to choose from. While the premium charged presently is not adequate to meet the claims on the policies, the industry should look to give the customer different products for different classes of desired treatment. It would be similar to a choice of a traveller choosing to fly a full service airline or a low cost airline! At the time of policy design itself the choice of service network should be given with varied premiums. So it would be a win–win situation for both the Insurer and the customer too.

Along with this there are a couple of unanswered questions too.

Will Private insurers follow suit? Looks unlikely as they have priced their products differently and have been very pro active in managing their claims. We could see the market moving towards the stand alone health insurers who have come out with innovative products.

Will this policy get extended to those covered under the Group health policy too? The insurance companies have already clarified that under the group schemes they have a chance to reset the price hence this measure is not needed. Though with each renewal, the insurer can load the premium by any percentage they desire depending on the severity of the past claims, with the stiff competition in this segment, the pricing adjustment is limited and they may have to move on to cover this segment too with restricted networks.

Another issue making the rounds is the imposing of service tax by the Government on Cashless facility. The stand being taken by some of the insurers is that this tax will form a part of the sum insured, which implies that the overall sum insured of each policy holder shrinks by about 10%. Has the customer been made aware of this by the insurer or will he be in for a rude shock when he gets to clearing his hospital bill?

How valid is this stance? The insurance company will get a set off from the service tax payable, so the customers sum insured being reduced is questionable at best. This again should have been anticipated and customers told in advance rather that get a rude shock at the time of discharge from the hospital.

Times are changing and customers need to be handled with care and lot more sensitively, for its they who keep the business going! At this rate the customers will prefer to stay away from insurance rather than go through these confusions.

Moving on to other issues India is turning out to be an attractive destination as a global outsourcing hub and manufacturing base for original equipment manufacturers (OEMs), especially after the global economic downturn. We hence thought it appropriate to put together an article on the Risk exposures in the Auto components industry in this issue. We also have Mr Arjya Mishra of RSB Transmissions sharing his views on the issues effecting the auto component industry over the past one year. Our sincere thanks to Mr. Arjya Mishra for sharing his valuable insights with our readers.

We trust you will find this issue interesting!

V Ramakrishna
Editor – *i-notes* & Chairman – India Insure

News TitBits

IRDA wins ULIP battle: Govt to amend laws to revive sales
Source: Economic Times

Insurance industry regulator Irda has emerged the victor in a high-profile tussle over the regulation of so-called unit-linked insurance plans or Ulips, with the government ruling that it and not the market watchdog Sebi would oversee the product. The government is clarifying by way of an explanation that life insurance business shall include any unit-linked insurance policy or scripts or any such instruments.

Risk Exposures in the Auto-Components Industry

Automotive Industry Overview

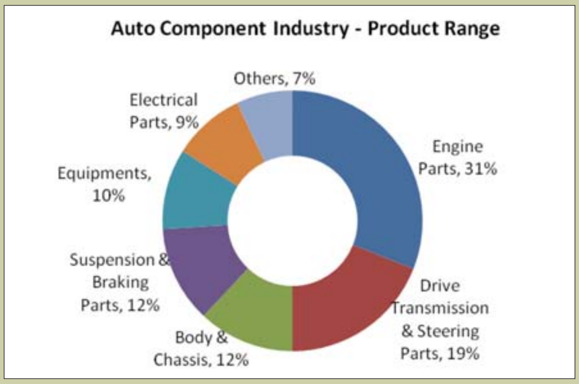
The Indian automotive industry is worth around USD 39 billion in 2009-10 and contributes about 5 percent of India's gross domestic product (GDP). It produces over 14 million vehicles and employs – directly and indirectly – in excess of 13 million people.

The industry is rapidly transforming itself to become one of the fastest growing in the world. Though the global slowdown did dampen the spirits for a while, the Indian auto industry has emerged stronger from the crisis. Confidence is higher, while growth and new investment are back on the agenda. So, what is driving this growth? Higher incomes have guaranteed a vehicle market that is growing considerably faster than GDP rate, not to mention improved roads and easier access to finance.

There are two distinct sets of players in the Indian auto industry: *Automobile Component Manufacturers* and the vehicle manufacturers, which are also referred to as *Original Equipment Manufacturers* (OEMs). While the former set is engaged in manufacturing parts, components, bodies and chassis involved in automobile manufacturing, the latter is engaged in assembling of all these components into an automobile.

Presently, India is the

- Second largest two wheeler market in the world
- Fourth largest commercial vehicle market in the world
- 11th largest passenger car market in the world and is expected to be the seventh largest market by 2016



The component industry is the fastest growing sub-sector of the Indian auto industry. From a low-key supplier providing components to the domestic market alone, the industry has emerged as one of the key auto components centers in Asia and is today seen as a significant player in the global automotive supply chain.

The industry is still relatively fragmented with hundreds of small component manufacturers – but the largest players now have the scale and capability to compete in international markets. 11 Indian auto component manufacturers have even won the prestigious DEMING award in recognition of their quality. Global automobile manufacturers today see India as a manufacturing hub for auto components and are rapidly ramping up the value of components they source from India.

Risks – Auto Components Industry

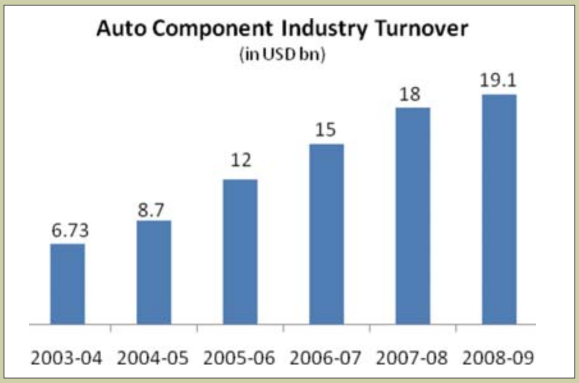
But even as optimism grows, some key concerns are becoming more pressing. Many of the changes occurring in the global marketplace today - tightened credit markets in a capital-intensive industry, declining consumer confidence, increased government involvement, bankruptcies are combining with familiar industry challenges to create an environment fraught with risk. This article throws some light on the risks facing the auto component industry.

Market Risks

Auto Component Industry is closely related to the overall growth of Automotive Industry. Historically, the Automotive Industry has witnessed periodic fluctuations in demand for vehicles. Demand for vehicles depends to a large extent on social, political and economic conditions in a given market and the introduction of new vehicles and technologies. Demand may also be affected by factors directly impacting vehicle price or the cost of purchasing and operating vehicles such as sales and financing incentives, prices of raw materials and parts and components, cost of fuel and governmental regulations (including tariffs, import regulation and other taxes). Auto Component Industry is affected adversely if the demand for automobiles remains weak leading to increased inventory resulting in a further downward price movement.

Global Competition

India is competing in the global auto component space with China, Thailand, Brazil, East Europe, Turkey and many more particularly for labour intensive products. ACMA* has found that the difference between Indian and Chinese auto component companies' factory-to-factory cost – taking into consideration the cost of transport, octroi, customs duty and others is a huge 45 per cent in China's favour. Severe competition has led to reduced pricing flexibility and profitability of auto component companies. Cheap imports of spurious auto parts from neighbouring countries are also affecting the industry in India. The spread of fake parts is acting as a big disincentive for a multinational to step into India, because it loses control over its intellectual property rights (IPRs). A recent ACMA report estimates the proliferation of counterfeit parts has caused the auto component industry a whopping loss of $1 billion (Rs4,590 crore) till date.



Technological Changes & Innovation Capabilities

The automotive industry is innovation driven. But many auto component companies in India have not moved up the technology ladder and don't have capabilities to design the products end-to-end. While technology capability of a supplier is assessed on qualitative parameters, spend on R&D could be an indicator of a company's commitment towards product development and innovation. Spend on R&D in the Indian auto components industry is very low and currently averages only 2-3% of the annual turnover. Indian companies have never really believed in treating R&D as an important activity and investing in it and so technology has always been sourced by Indian component manufacturers from their collaborators.

**ACMA - Automobile Component Manufacturers Association*

(Contd... 03)

Risk Exposures in the Auto-Components Industry..... Contd. # 2

In today's environment, Research and development capacity is not an optional extra for automotive suppliers – it is the *sine qua non* of participation in the global automotive chain.

Production Risks

Manufacturing efficiency plays a critical role in the automotive industry and hence the huge production lines and complex nature of machinery requires diligent quality standards across the organization. Because the automotive industry relies heavily on just-in-time delivery of components during the assembly and manufacture of vehicles, a disruption in the supply of a key component by occurrences such as technical failures, natural calamities, fire, explosion etc. could adversely affect the business.

Product Liability & Recall

Auto component manufacturers are exposed to product liability claims in the event that their products fail to perform as expected. As suppliers become more integrally involved in the vehicle design process, automakers are increasingly expecting them to warrant their products and looking to them for contributions when faced with product liability claims or recalls.

The recent Toyota recalls are a grim reminder of how important it is to have the right protection in case of a liability claim. The costs associated with an automotive recall can be substantial, creating a huge business risk for suppliers. And unfortunately many suppliers are carrying this massive exposure without insurance. Despite a series of recalls in the country, including the biggest by Maruti Suzuki of 100,000 A-Star cars for faulty parts, Indian companies are not paying enough attention to the risk because they do not think it is something they will need. But unlike other industries, product liability clauses are very stringent, especially in the US market and unless appropriate processes and risk control measures are in place, it could wipe out entire companies.

Pricing Pressures

Downward pricing pressures by auto manufacturers are a characteristic of the automotive industry. Stricter regulations and increasingly demanding end-consumers have forced original equipment manufacturers (OEMs) to provide more features, at a time when they are finding it hard to sustain their profitability. In turn, they are demanding purchase price reductions from their suppliers, thus exacerbating the already cut-throat price competition among supplier markets that are fraught with overcapacity.

Supply Chain Disruptions

The complexities of the global supply chain pose a monumental task for any automotive player. Automotive supply chains are deep and broad. The difficulty of negotiating a worldwide system of suppliers and sub-suppliers with a range of capabilities and skills poses significant challenges. In recent years, many costs and responsibilities—including critical issues such as product warranties—have been pushed down the supply chain from tier to tier. In the highly competitive auto component sector, the margin for error is very low and companies always operate on the knife edge. Hence extreme efficiency along the supply chain is very important to avoid potential bottlenecks like supply interruption and quality problems.

In mid-2007, an earthquake at Chuetsu in Japan showed just what can happen when production is disrupted. Riken Corporation, a company that supplies essential motor and transmission parts to the Japanese auto industry, experienced a total breakdown in production even though only a few machines had suffered minor damage. Not long after this, the production lines of all major Japanese car manufacturers stood idle. The loss in production amounted to some 120,000 vehicles.

Essential components in the automotive industry are usually supplied and delivered as required "just in time" or "just in sequence". In an effort to manage the costs, many auto-component companies have been consolidating their supply base resulting in them being dependent on single or limited sources of supply for certain components. The result has been the creation of interdependencies between companies. The downside is even relatively minor disruptions can have huge consequences and bring entire areas of production to a standstill.

Commodity Price Risk

Automotive suppliers are facing years of uncertainty regarding the costs of basic raw materials and energy. Volatility in prices of raw materials used in manufacturing components such as steel, precious metals, non-ferrous alloys leads to higher production costs for parts and components. The inability to pass on price increases to customers when material prices increase rapidly negatively impacts the supplier's profitability.

Financial Risks

- **Currency and Interest rate fluctuations**

  Since exports constitute around 20% of the turnover of the auto-components industry, companies are exposed to a risk of gain or loss from changes in foreign exchange rates whenever they enter into a purchase or sales agreement in a currency other than the Indian Rupee. Movements in exchange rates and volatility in interest rates have an adverse effect on operating results.

- **Default Risk**

  Default risk is the uncertainty surrounding a firm's ability to service its debts and obligations. In today's business environment, several automobile majors are in severe financial distress. As a consequence, the receivables from these OEM's are under risk and the loss suffered by the supplier in the event of default is usually significant.

Environmental Issues

In India, the Centre for Science & Environment had carried out a Green Rating Project to track the environmental performance of the Automobile sector and they fared badly - the sector as a whole scored only 31.4 per cent. Globally, road transport contributes 14 percent of total man-made carbon dioxide (CO_2) emissions. Although new cars now emit significantly less CO_2, road transportation remains one of the few sectors where emissions keep rising due to the growth of freight transportation, vehicle ownership and increased mileage.

Today, with green issues very much to the forefront, Governments have imposed stringent environmental regulations on OEMs for emissions control and fuel economy which is ultimately passed down to the suppliers. Environmental considerations are now driving system and vehicle design and development putting additional pressure on suppliers.

Infrastructure Deficit

Issues related to poor basic infrastructure like power, roads, port facilities and transport/ logistics are one of the major worries for component manufacturers located across the country.

- **Power:** Power shortage is a major concern for many companies located in several industrial belts across the country. Lack of adequate power supply leads to the usage of generators, thereby increasing the operational cost and finally the cost of the end product, leading to lowering of competitiveness in global market.
- **Logistics/ transport:** Poor logistics/ transport infrastructure and seemingly cartelization of transporters are also areas of concern. It increases the overall logistics cost, which adds to the final delivery price to the customers.

(Contd... 08)

Interview – *Corporate*

Very few sectors are as international or involve such a diverse range of highly specialized disciplines as today's auto-component industry, which is constantly evolving at high speed. However, the more specialized and global production within an industry becomes, the more vulnerable it is to risks and disruptions. In this issue we talk to Mr. Arjya Mishra, HR Head of RSB Transmissions on the issues affecting the auto-component industry in India.

What are the prominent changes/issues that have affected the auto-component industry over the last one year?

- Investment was high in this sector across India.
- A number of new products have been launched by OEM's & they asked to increase the quality standard of the auto components.
- The auto – component manufacturers have to increase their capacity to adhere to the market.
- Immediate crunch of skilled manpower
- Crunch of fund.

How much growth have you witnessed in the last fiscal? How did you overcome the recessionary period?

The growth was almost 65% higher than last fiscal year. Production was reduced to two shifts rather than three shifts. The recessionary period was overcome by

- Reducing floating manpower
- Various cost reduction measures
- Consolidation of raw material line
- Involving maximum workforce on various KAIZEN initiatives

According to you, what are the three biggest risks facing the auto-component industry today?

- A substantial amount of investment has to be done in R&D sector
- There is always the pressure to become cost competitive
- Threat from China

How are risks managed at RSB so that the potential losses are minimized? What controls & monitoring procedures do you have in place?

- Rationalising a number of product platforms and partnership with the vendors
- Substantial investments have been made in R&D sector
- Continuous working on the pricing policy to become cost competitive
- Control and monitoring process through management review meetings & business models like X matrix analysis

There's lot of talk about outsourcing becoming a big business in the Indian auto ancillary industry. But one danger of outsourcing is that should something go wrong, you will be slapped with a recall liability that can wipe out a medium size company. How prepared are Indian auto component manufacturers to handle a recall in case they ever face one?

- Product to be manufactured as per the customer's design specifications.
- Quality standard of the product to be continuously monitored
- While doing the costing of the product, the recall cost percentage to be taken care of either 5 to 10%.

What impact is the cheap imports of auto parts which have increased significantly especially from China having on the Indian auto component industry?

Cheap imports of auto parts from China have intensified the already cut-throat competition. However they have ensured that the Indian auto component industry

- Remains cost conscious
- Make optimum utilization of resources
- Make improvement in operational process
- Improve the supply and quality standard

What are the critical success factors in today's automotive environment?

- Innovation
- Cost and product differentiation
- Agility to market.
- Retaining the existing customer

What is your long-term outlook for the auto-component industry?

- India is going to be sourcing hub for the auto component industry.
- Possibilities of forward and backward integration to add more value to the product.
- Launch of new products ranging from passenger cars to SUV's in near future.

{Views expressed herein are purely personal and do not reflect the views of the company}

News TitBits

Now, 10.3% tax on cashless mediclaim

Source: Times of India

Mediclaim policy holders will now have to contend with another insurance squeeze — a service tax of 10.3% on every claim made using the cashless facility. Only patients who claim cashless facility will have to pay the service tax while the patients who go in for reimbursement won't have to pay extra "TPAs had asked the insurance companies to clarify whether this new service tax would be claimed from the claim sum or from the existing service tax that is paid on the policy bought by a customer. They categorically told us that the service tax has to come from the claim sum", said an executive at a TPA.

Report Card - June 2010

Gross premium underwritten by non life industry for and up to the month of June 2010* (Rs. In crores)

INSURER	JUNE		GROWTH OVER THE SAME PERIOD OF PREVIOUS YEAR	APRIL - JUNE		GROWTH OVER THE SAME PERIOD OF PREVIOUS YEAR
	2010-11	2009-10		2010-11	2009-10	
New India	623	482	29.33%	1994	1649	20.94%
United India	461	370	24.58%	1556	1270	22.53%
National	486	379	28.34%	1466	1152	27.23%
Oriental	420	336	24.96%	1375	1173	17.26%
ICICI-Lombard	342	221	54.83%	1071	852	25.65%
Bajaj Allianz	228	210	8.34%	718	635	13.14%
IFFCO-Tokio	149	142	5.29%	483	426	13.31%
Reliance	153	172	-11.24%	429	557	-22.98%
Tata-AIG	79	55	43.54%	324	262	23.82%
HDFC ERGO	84	45	85.71%	320	181	76.36%
Royal Sundaram	90	66	36.20%	262	209	25.16%
Cholamandalam	78	66	18.39%	245	233	5.09%
Future Generali	44	29	52.48%	160	92	74.46%
Shriram General	50	18	172.06%	140	62	124.06%
Bharti AXA	38	13	183.99%	129	42	210.25%
Universal Sompo	28	08	257.00%	78	35	122.30%
SBI General	1.2	0		1.58	0	
Raheja QBE	0.4	0		1.42	0	
PRIVATE TOTAL	**1363**	**1045**	**30.45%**	**4360**	**3585**	**21.61%**
PUBLIC TOTAL	**1990**	**1566**	**27.03%**	**6390**	**5243**	**21.88%**
GRAND TOTAL	**3353**	**2612**	**28.40%**	**10751**	**8829**	**21.77%**
1.Credit Insurance						
ECGC	74	66	14%	208	190	9.66%
2.Health Insurance						
Star Health	98	75	30%	320	226	41.37%
Apollo MUNICH	11	05	133%	42	19	116.18%
Max BUPA	1.28	0		2.31		
Health Total	**110**	**80**	**38%**	**364**	**246**	**48.23%**
3.Agriculture Insurance						
AIC	52	52	1%	149	132	12.84%

* Source : IRDA

Observations: Performance for Apr- June Period

- The industry (incl stand alone health insurers) have collected premiums of Rs.11116 crores recording a growth rate of 22.49% in Apr-June compared to Rs. 9075 crores during the same period last year.
- The private players have registered a growth of 21.61% during this period compared to 1.21% during the same period last year.
- The PSU's have registered a growth rate of 21.88% during this period compared to last year's 7%.
- The stand-alone insurers have registered a growth of 48% compared to last year's 87%.
- The accretion achieved by the PSU's during this period is Rs.1147 crores; the private players: Rs.775 crores and stand-alone health insurers: Rs.119 crores towards the overall market accretion of Rs.2041 crore.
- The major contributors for the performance in the period Apr-June 2010 have been New India with an accretion of 345 crores, National with an accretion of 314 crores, United India with an accretion of 286 crores and ICICI with an accretion of 218 crores. Looks like National & ICICI Lombard are pretty aggressive this year.
- Reliance (-22.98%) has recorded negative growth during this period.
- At the end of this period, the four public players have collectively increased their market share to 59.44% from 59.39% during the same period last year.

News TitBits

IRDA vows cashless mediclaim revival

Source: Economic Times

The four public sector general insurers had withdrawn the cashless facility w.e.f July 1st in top city hospitals in the 4 metros on the grounds that they had padded up their bills and were unwilling to accept rates offered by these insurance companies. The Delhi High Court came down against the regulator - IRDA for its failure to sort out the dispute between insurance companies and city hospitals and directed IRDA to make arrangements to restore the facility. "Now that the High Court has given direction, we will follow that", IRDA chairman J Hari Narayan told.

Assured return for pension plans

Source: Economic Times

The insurance regulator has ordered life insurers to offer customers a guaranteed return of 4.5% per annum on pension and annuity plans as part of its new, tighter norms for the sector, a move that is expected to force companies to slash commissions to agents and invest more in government securities.

Richer India moves up in insurance ranking

Source: Economic Times

India's ranking among life insurance markets has risen from number 10 last year to the number 9 position, displacing Taiwan. When life insurance industry was opened for competition in 2000, India ranked number 20 among life insurance markets and accounted for a mere 0.5% of the world premium. Ten years on, the share has improved to 2.45%.

Reliance General, Royal Sundaram submit merger proposal to Irda

Source: Economic Times

Reliance General Insurance and Royal Sundaram Alliance have submitted a proposal to the insurance regulator to merge their businesses. The proposal will pave the way for UK insurer, the RSA group, acquiring a 26% stake in the second-largest private insurer and would also result in Sundaram making an exit from the business.

Insurers to revise cargo cover terms

Source: Economic Times

Non-life insurers plan to revise the terms of their marine cargo insurance policies, whereby they will not pay for claims for cargo damaged due to accidents caused by the vehicle not being roadworthy. The exclusion will, however, not apply if the transporter uses an unfit vehicle without the knowledge of the insured. Another proposed variation is that insurers will now reject claims where the packaging was inadequate for the particular transit undertaken. The revised conditions also specifically cover shipments through courier service providers — an area where the clauses were ambiguous so far.

Readers Speak - *The Future of TPA's*

The advent of Third Party Administrators (TPA's) was expected to play an important role in the health insurance market in India in ensuring better services to policyholders. Their presence was aimed at ensuring higher efficiency & standardization in claims settlement and improving penetration of health insurance in the country. But, a decade since they started operations, TPAs find themselves in the spotlight for all the wrong reasons. While Customers are angered by denial of cashless treatment facility and delay in reimbursement claims; Insurers seem unsatisfied with TPA's ability to control claims and hospitals complain of delayed and short-settlement of bills. Even the Insurance regulator is of the opinion that the current working of the TPA system poses a threat to the entire health insurance sector.

But, what actually went wrong? Why is the concept that started with very high expectations a pain in the neck today? Who is to blame? Did TPA's fail in achieving their responsibilities? How do TPA's enforce standardization without any kind of regulation on healthcare rates? Are customers & Insurance companies better off without TPA's? Is it the end of the road for TPA's in India or is there a bright future awaiting them? How do they move forward?

Your opinion is solicited!

Please send your responses in 200-300 words to knowledge@indiainsure.com

In the last issue of inotes, we had asked

"Do you think your task will become simpler if the regulator or any independent rating agency rates the insurance brokers on various parameters like understanding of the market, technical expertise, responsiveness to customer needs, business retention, professional standards etc..?"

Below are some of the responses we received

Response from Mr. Amit Sharma, Chief Insurance Officer, Bosch Group

No I don't agree on this as it totally depends on companies risk management philosophy and different companies used different techniques and methods to evaluate Broking firms and Insurance companies. Thus role of the regulator or independent rating agency in rating is almost negligible. Apart from that, looking at the level of corruption at least I will never depend on third party to make my decisions. May be I might use some information from them, it can be 1% of my overall selection methodology.

Parameters to be considered for rating:

- I will say it depends on company to company. No doubt price is one of the factors while making decision but not the prime factor. There are various factors which are kept in mind while deciding any broking firm like Good will, retention ratio, Service, Domain knowledge etc.
- The rating has to be done by the company itself without depending on external parties, it is a company's risk manager who can better understand his/her needs and wants w.r.t. to risk management. For me personally, I collect lot of information before selecting broking firm or insurance company. Currently I use 7 techniques comprising of 120 questions for selection of broking firm.
- Most reliable technique I can say is to get feedback from those corporates which a broking house have lost.

Response from Mr. K Ramesh Kumar, President – Operations, KSK Energy Ventures Ltd.

A Corporate insurance user will typically have his own unique "perceived need" for a specific set of qualifications/ capabilities that he looks for in the Broker. Once these are met and satisfied, he goes ahead with the selection. In this context, I have my doubts on whether third-party rating of insurance brokers would make the choice any easier.

In the initial years, we at KSK experimented with several brokers based on our comfort level. Over the years, we have gradually been able to separate the chaff from the grain and now concentrate on only 3-4 brokers. We have devised a Broker Evaluation methodology based on various parameters like market penetration of the broker, premium placed, broker's experience in our industry, technical expertise, service capability etc. A capable and knowledgeable insurance broker is a valuable asset and so the selection process is important. By using a specific set of selection criteria, a good choice can almost be guaranteed.

Rating will have its own loopholes especially if it is optional. Similarly, a new company might not stand too much of a chance with the rating agency in spite of it being started by promoters with good experience in the broking industry. Finally, I think it is a company's personal choice depending on their requirement of an insurance broker.

Response from Mr. Jan Mumenthaler, Head – Insurance Services Group, International Finance Corporation

A broker needs to be considered a service provider and this hopefully goes beyond chasing for the cheapest premiums. Having said that, a broker's "rating" should be word of mouth. In my experience, a broker firm's service is as strong (or as weak) as the individual broker's performance. Belonging to a professional association (which ensures that the firm adheres to certain minimum standards) should be a bare necessity. Other than that, I do not see any particular need for rating agency monitoring of brokers.

{Views expressed herein are purely personal and do not reflect the views of the company}

Claims Case Study: *Think you're covered!*

Claims Case Study- *Think you're covered?*

The purpose of business interruption (BI) coverage is to compensate the insured for lost income if it has to suspend operations due to an insured peril. Although the idea of business interruption coverage is simple, the coverage itself is not. Since BI risks come in many guises - including natural perils, man-made disasters and supply chain breakdowns - many organizations may find that they do not have right insurance cover when a claim arises.

Background: Reddy Motors maintained a car dealership in Rajahmundry, Andhra Pradesh close to the banks of River Godavari. On 12th August 2006, a flash flood struck the place and a part of the road leading to the dealership was washed away. This caused the dealership to be inaccessible for around 3 weeks until the roads were rebuilt / repaired. The roof of the dealership also collapsed partially due to the storm that accompanied the rains. At the time of the flood, Reddy Motors was insured under a standard fire insurance policy (that covered storm, tempest, flood & inundation) and also a Fire Loss of Profits policy that included protection against loss of income resulting from the suspension of business due to a covered peril under the Fire policy. The insured filed a claim under its fire policy for damage to its roof due to the storm and the insurer paid the claim. The insured also filed a claim to recover income allegedly lost because of lack of access to the dealership & the resulting business interruption due to the flood and storm. The insurer denied the claim for business interruption loss and so Reddy Motors filed an action in Court seeking damages.

The Issues & Outcome: The issue before the Court was to decide on the availability of business interruption coverage for the time during which the dealership was closed. The insured argued that its inability to gain access to the dealership due to the flood rendered the business as lost to the insured as it would have been "had the flood submerged its premises," and that this loss triggered coverage. The insurer contended that, except for the partial damage to the insured's roof, which was covered by the policy and did not result in any interruption to the business, there was no "direct physical loss or damage" that resulted in a loss of business income during the period of restoration so as to come within the business interruption coverage. Thus, we must determine the meaning of the policy's language.

The policy wordings read like this

"We will pay for the actual loss of Business Income you sustain due to the necessary suspension of your "operations" during the "period of restoration." The suspension must be caused by direct physical loss of or damage to property at the premises described in the Declarations"

Based on the language used in the insurance policy, the Court held that the business interruption clause is not applicable to the facts in this case. Reddy Motors could not offer any proof that its lost business income was due to damage to the roof rather all the evidence pointed that the loss was proximately caused by the insured's inability to access the dealership due to the road being washed away in the flood. The roof damage was not the proximate cause of the loss of business income and there was no suspension of business due to the roof damage or the repairs thereto. Therefore the Court held that, under the language of the business interruption clause of the policy, coverage is provided only when loss results from suspension of operations due to damage to, or destruction of, the covered business property by reason of a peril insured against.

Hence, the Court denied recovery, because the lost revenue did not result from actual damage to the property insured.

Our Learnings: As a general rule, in any business interruption claim, the insured must establish the following elements in order to trigger coverage: (1) a necessary suspension of operations (2) due to physical damage to covered property (3) caused by a covered cause of loss.

However add-on covers are provided in the areas of – "Suppliers' Extension", "Customers' Extension", "Utilities Extension" and "Denial of Access Extension".

Denial of Access will be an issue in any incident that affects a significant common area or where companies use common or adjoining means of accessing their premises. Such claims point to the need to carefully analyze the specific language of the policy at issue and ensure coverage for events that do not cause physical damage to the insured property but can prevent access to such property. Customers & their risk managers should not feel content simply because they have purchased "business interruption coverage."

Conclusion

No one doubts that Reddy Motor's loss here was genuine. The question the Court confronted was whether Reddy Motor's had transferred the risk of this kind of loss to its insurer; under the policy language at issue it was fairly clear that they did not do so.

News TitBits

PSU insurance companies to float own TPA

Source: Economic Times

In order to bring down the high claim ratio due to alleged "fraudulent practices", public sector health insurance companies have decided to overhaul the existing system by floating their own third-party administrator (TPA) for management of claims.

IRDA issues Ulip guidelines, raises lock-in period to 5 yrs

Source: Economic Times

Irda has tightened the norms for ULIP schemes by raising the lock-in period to 5 years from the current 3 years and ensuring that they have uniform/ level paying premiums. Further, all unit linked products, other than pension and annuity products shall provide a mortality cover or a health cover thereby increasing the risk cover component in such products.

Arbitration in Essar Oil's claim for Vadinar refinery begins

Arbitration proceedings to decide one of the largest insurance claims in India, Essar Oil Ltd's claim for Rs. 3,020 crore from United India Insurance Co. Ltd. has begun.

Law soon to allow class action suit for huge damages

Source: Advisen

Taking the Bhopal gas tragedy verdict and the paltry compensation for victims as a huge lesson, law minister Veerappa Moily has proposed a radical law that would bind corporate bodies with vicarious liability both under criminal and civil laws and allow class action suit to be brought against them.

Aban gas rig loss to jack up energy cos' insurance costs

Source: Economic Times

Insurance costs for Indian energy companies are likely to rise with the sinking of Aban Offshore's $240-million gas exploration rig Aban Pearl in the Caribbean sea off Venezuela. The sinking of the rig comes in even as insurers worldwide are trying to come to grips with the oil spill in the Gulf of Mexico caused by an explosion in BP's oil rig off the US Gulf Coast. "This will be bad news for Indian energy companies," said an energy specialist with an insurance firm.

Life insurers clock 25 per cent growth & Non-life insurers clock 13.4 per cent growth in 2009-10

Mitsui Sumitomo scouting for life insurance partner in India

L&T General starts non-life insurance operations in India

IRDA bans over 4,000 corporate agents

- **Port facilities:** The prominent ports in India are congested and as a result there are delays in shipment of consignments leading to longer lead-time for exports. These delays in turn lead to delay in receiving payments.

Availability of trained manpower

Due to emerging employment opportunities in new manufacturing units and service industry, retention of skilled manpower is proving to be a challenge for auto component manufacturers. Players are able to get an adequate number of people however getting people with the right skill sets is an issue, especially at supervisor levels and technician levels. The quality requirements from the industry are changing with the global requirements and achieving skill development for a new set of employees on a regular basis is a challenge.

Political, Regulatory and Legal Risks

The automotive industry is subject to various laws and governmental regulations including those related to vehicle safety and matters such as emission levels, fuel economy, noise and pollution. As companies conduct business across multiple locations, they become exposed to varying and sometimes contradictory regulations. Given the variance of regulatory frameworks around the world and the lack of will to harmonise these into a single global standard, automotive companies may need to develop multi-pronged strategies to minimise risks and maximize returns.

Many governments also impose tariffs and other trade barriers, taxes and levies and enact price or exchange controls and companies incur significant costs in complying with these regulations.

Risk Management & Insurance Solutions

Managing and controlling risk is the key to running a successful organization. Properly managed, it drives revenue and efficiency for companies across all industries. Poorly managed, it can wreak havoc. Of course, risk has always been an inherent part of the automotive industry. But the current economic environment and the changing business model driven by new technology, new products and new markets have all put more pressure on companies to focus on risk management.

Some risk exposures can be taken care of by insurance while others need to be controlled through a holistic risk management program. Below is the risk matrix that identifies the risks exposed to by auto component manufacturers and the availability of an insurance cover:

Risks associated with	Availability of insurance cover
Product Development	No
Plant & Machinery	Yes
Production (damage to raw materials or machinery)	Yes
Storage	Yes
Supply chain (Transit & Business Interruption)	Yes
Price controls	No
Exchange rate fluctuations	No
Intellectual Property	Yes
Regulatory Changes	No
Political Interferences	Yes
Credit Default	Yes
Product Liability & Recall	Yes
Business Interruption	Yes
Environmental Pollution & Contamination	Yes
Third party bodily injury & property damage	Yes
Employee Health & Safety	Yes
Employee Dishonesty	Yes
Natural calamities	Yes
Terrorism	Yes
Directors & Officers liability	Yes

Conclusion

In the space of a little more than 15 years, India's auto sector has passed a critical turning point – it has become a well integrated part of the world's global automotive manufacturing hub. However to continue on the path of growth momentum, many companies will have to reinvent themselves to adapt and succeed in a tougher, leaner and far more complex marketplace. A "business-as-usual" approach is no longer viable – instead, a proactive approach with a sharp focus on managing the evolving risks should be the chosen way forward if automotive suppliers hope to move from merely surviving to actually thriving. The fast paced changes within the industry call for a unique approach to risk management to successfully achieve corporate objectives.

Disclaimer

Contact us

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