

airmic

EXPLAINED

GUIDES

THE PURPOSE, PRINCIPLES AND PRACTICE OF GENERAL INSURANCE

In association with:



Acknowledgements

About Airmic

The leading UK association for everyone who has a responsibility for risk management and insurance in their organisation, Airmic has over 450 corporate members and more than 1,500 individual members. Individual members are from all sectors and include company secretaries, finance directors, and internal auditors, as well as risk and insurance professionals. Airmic supports members through learning and research; a diverse programme of events; developing and encouraging good practice; and lobbying on subjects that directly affect our members and their professions. Above all, we provide a platform for professionals to stay in touch, to communicate with each other, and to share ideas and information.

www.airmic.com

airmic

About Mactavish

Mactavish is the UK's leading independent outsourced insurance buyer and claims resolution expert. We support our clients by helping them identify their risks, design their insurance programmes, improve the reliability of their cover, and manage costs down.

We work independently to represent policyholders' interest only and receive no commissions or fees from insurers or other third parties. Our clients value this independence and see us as a powerful force for change in an industry that all-too-often takes its customers for granted.

Our roots are in deep analysis of risk and insurance contracts, and we played an instrumental role in designing key legislation such as the Insurance Act 2015. Building on that heritage, we have developed a unique offering that combines unrivalled technical and legal knowledge, with commercial know-how and buying power.

Our clients come to us when the insurance market has let them down. They never go back to the old-fashioned way of doing things.

www.mactavishgroup.com



01	Introduction.....	4
02	The Purpose of Business Insurance.....	8
	2.1. Reasons to Buy Insurance.....	8
	2.2. The Role of Insurance in Society and Business.....	8
	2.3. Different Types of Insurance Cover.....	9
	2.4. Alternative Risk Transfer.....	14
03	Selecting an Intermediary	16
04	Choosing an Insurer	18
	4.1 The Hard Market.....	19
05	Insurance buying process	20
	5.1 Outlining the Buying Process.....	20
	5.2 Understanding Insurance Contracts.....	20
06	Insurance Act 2015	24
	6.1. Insurance Act and Interpretation.....	24
	6.2. Managing Duty of Fair Presentation of Risk.....	25
	6.3. Impact of Warranties Explained.....	26
	6.4. Abolition of Basis Clauses Explained.....	26
07	Scenario Analysis.....	27
08	Getting Claims Paid.....	30
	8.1. Pre-Loss Priorities Explained.....	30
	8.2. Claims Resolution.....	30
	8.3. Learning from Losses.....	31
09	How Insurance Supports Risk Management.....	32
	9.1. What is Risk Management?.....	32
	9.2. ISO 31000	32
	9.3. Insurance Conditions and Risk Management	32
10	Glossary.....	34
	10.1. Terms and Principles.....	34
	10.2. Insurance Stakeholders and Roles.....	38
	10.3. Alternative Structures and Insurance Markets.....	40
	10.4. Insurance Policies and Covers.....	41

The concept of insurance is based on spreading the cost of the misfortune of the few across the good fortune of the many. It is a concept which dates back millennia.

There are two main types of insurance: life insurance and general insurance.

Life insurance is often referred to as 'assurance' and pays a lump sum or regular payments if an insured event happens during the length of the policy. Life insurance companies sometimes provide pension schemes or may provide an insurance policy called an 'annuity'. This provides a guaranteed income for the life of the annuitant or a reduced amount to a named beneficiary on the death of the annuitant.

General insurance protects the things people and businesses care about and want to protect. In some cases, businesses may have a legal or regulatory obligation to insure those for whom they have a duty of care, for example, employers have a duty to provide insurance for their employees. General insurers sell insurance to protect against events such as fire, natural catastrophes or liabilities, and can be at the forefront of developing risk management solutions to help their customers understand and mitigate risks or to respond to emerging risks such as those relating to cybercrime and climate change.

General insurance policies are typically shorter than life insurance policies, and many are renewed annually. This guide focuses on general insurance.

A Brief History of Insurance

Insurance in some form can be traced back to prehistory with communities bartering goods outside their own community without money by using mutual agreements, such as neighbours agreeing to rebuild a home if it is destroyed, or the creation of public granaries for crops to help indemnify communities against famines. In medieval Europe, the guild system emerged with members paying into a pool, which would be drawn on to cover any losses. Insurance provides protection against financial loss for people and organisations.

Insurance companies are paid to take risks from customers who could not afford to pay for the loss if the risk turns into reality.

Of the insurance we are more familiar with today, marine insurance is the oldest. Merchants were vulnerable to losses at sea due to storms or piracy, and as significant sums could be at risk, marine traders from the 14th century in what is known today as Belgium developed a way of spreading a financial loss that could not be borne by a sole trader. In particular, this practice developed around merchants sailing to the New World, who would seek multiple investors to spread the risk of loss more widely.

After marine, in the 16th century, fire insurance was developed in Germany and Italy. Established in 1676, the Hamburg Fire Office was the first officially established fire insurance company. Property insurance as we know it today can be traced back to the Great Fire of London in 1666, which devastated London and converted insurance "from a matter of convenience" into one of urgency – a change of opinion reflected in Sir Christopher Wren's inclusion of a site for the 'Insurance Office' in his new plan for London in 1667. A number of attempted fire insurance schemes came to nothing, but in 1681, economist, physician and financial speculator, Nicholas Barbon, and 11 associates established the first fire insurance company, the 'Insurance Office for Houses', which became the Phoenix, at the back of the Royal Exchange in London, to insure brick and frame homes.

Following this development, many similar companies were established, each one creating its own fire department to focus on the prevention and minimisation of damage from extensive fires involving the properties insured by them. They also began to issue fire insurance marks (also known as fire plates), which were plaques marked with the emblem of the



insurance company and often a cover number, or as we call it today, a policy number. These were fixed to the front of insured buildings to indicate which company had insured the building and acted as a guide to the fire brigades, which at the time were owned by the different insurance companies, before municipal fire services were formed. The first company to use these marks was the Sun Fire Office, established in 1710.

The Hand in Hand Fire & Life Insurance Society was founded in 1696 at Tom's Coffee House in St Martin's Lane in London. It was structured as a mutual society and ran its own fire brigade for 135 years. At first, the firemen were volunteers who had their own jobs, but this system was unsustainable and soon the insurers recruited permanent firemen. By the early 19th century, the London insurance companies had banded their fire brigades together and this was the first step towards the fire brigade being taken over by local and national government. Similar systems developed globally, especially in the USA, where many buildings were built of wood and therefore vulnerable to fire.

With the growth of the Empire, the UK marine insurance market continued to flourish. With regards to other lines of business, specialist insurers offering single cover products continued to grow. This would continue until the early 20th century when, following a wave of mergers and acquisitions, composite insurers emerged offering a variety of new 'composite' insurance products. Fifteen of the UK's 35 biggest fire insurers had been absorbed into larger groups by 1925, and Commercial Union, one of the UK's largest composites, absorbed 21 companies between 1900 and 1939.

The two world wars, which ruptured the trade partnerships that had developed over the prior hundred years, turned the international insurance industry upside down and accelerated the rise of non-British insurers. Nonetheless, the development of new geopolitical partnerships and the postwar technology boom (and the new hazards it heralded) presented new opportunities for UK insurers, and despite the growth of international markets and the ups and downs of the UK economy, the London market retained its status as an international centre for complex and high-value risks (partly fuelled by the consolidation that had begun at the beginning of the century).

Today, we live in a world vastly more complex and interconnected than what Edward Lloyd – owner of the coffee house that grew into the insurance market Lloyd's of London – could ever have imagined. Yet, insurance remains an invaluable source of financial resilience against a whole variety of risks.

Insurance Buying in the 21st Century

Given the increased interconnectedness across the economy and the operational complexity of risks facing organisations in the modern world, the process of buying insurance has grown equally complex. Nor can they always achieve appropriate coverage on commercial terms. Consequently, buyers need to review and give due attention to the detail of their policy terms, to identify any onerous clauses, inappropriate exclusions and gaps, or overlaps in coverage.

Similarly, they need to focus on the risk information they provide to their insurer and on which their

01 Introduction

policy reliability depends, given the importance under UK law of not only answering questions accurately, but also ensuring a 'fair presentation of the risk' to insurers (as prescribed by the Insurance Act 2015), including accurately declared values, and so on. These are but a handful of the challenges that insurance buyers face every day if they are to successfully avoid surprises in the event of a claim. [See Section 4 – Insurance Buying Process]

This guide sets out the purpose of commercial general insurance and how organisations can use insurance to support their objectives. It summarises some of the fundamental principles on which insurance is based and explains the relationship between good risk management and good insurance practice.

The guide introduces a number of current concepts and aims to provide sufficient detail to be useful for those who are new to commercial general insurance and who are seeking signposts for further reading, or for those who – as is increasingly common – have commercial general insurance as one of a number of other business responsibilities.

This guide describes how a business can identify the general insurance it needs and how to buy this cost-effectively. It will discuss the role of the insurer, insurance broker and other stakeholders in the process, and what they will expect from the business. Purchasing appropriate insurance is an essential part of successful business planning. Doing it well will save a business money and help it to achieve its objectives.



Given the increased interconnectedness across the economy and the operational complexity of risks facing organisations in the modern world, the process of buying insurance has grown equally complex.

01

INTRODUCTION



02 The purpose of insurance

Insurance creates value for society. Risks are becoming more complex, fast-changing and interconnected, as a result of issues such as climate change, globalisation and technological development.

Insurance should help communities and society to become more resilient, to prevent risk and to take more risk to convert into opportunities. The premiums invested in capital markets also help to finance businesses and projects that are important for society.

Insurance is a contract whereby an insurer promises to pay the insured a sum of money if specified events occur in the future. Businesses buy insurance to protect their assets and income streams; to protect the assets of the directors and officers of their organisation; to pay compensation to third parties in the event of a claim against the organisation and, in certain circumstances, because it is a legal obligation.

Almost all businesses buy insurance, but the type and amount of insurance cover purchased will vary according to the risk profile and risk appetite of the business. One business may decide to buy only a limited amount of insurance because it is willing to carry most of the risk itself, whilst another will choose to purchase considerable insurance. Such decisions form part of the overall process of risk management.

2.1 Reasons to buy insurance

Reasons for buying insurance can be grouped under three main headings:

- i. Satisfying Legal and Contractual Obligations
 - Mandatory, for example, liability for employees or for motor vehicles
 - Required for trade or professional reasons, for example, professional indemnity

- Demanded by customers or suppliers in a contract, for example, public liability
- ii. Providing Balance Sheet / Profit and Loss Protection
 - Protect the balance sheet if a major event occurs, for example, a fire or a flood
 - Relieve pressure on cash flow and reduce volatility in the event of a loss
 - Budget for losses, for example, vehicle accidents or stolen plant / machinery
 - iii. Providing Employee Benefit / Protection of Employee and Contractor Assets
 - Funding of an employment benefit, for example, Private Health insurance
 - Protection of personal assets, for example, Directors' and Officers' Liability
 - Protection of the business in the event of the death of a key member of staff

These categories are considered in more depth at **section 2.2** of this guide.

Insurance provides more than financial protection and can facilitate access to advice on risk management and expertise for handling claims, especially around new or emerging risks such as cyber. This can be particularly valuable to help businesses understand and mitigate their risks, thereby reducing the likelihood of a major loss and helping minimise disruption should a loss occur. Most businesses will consider insurance as one source of mitigation alongside wider risk prevention and risk management measures. The Airmic EXPLAINED guide *Risk and Managing Risk* provides more details on such measures.¹

¹ Airmic EXPLAINED Guide, Risk and Managing Risk. <https://www.airmic.com/technical/library/explained-risk-and-managing-risk>

2.2 The role of insurance in society and business

Insurance provides businesses with capital, which they pay a premium to access. A key feature is that payment of insurance capital is contingent on a specific set of circumstances applying. This is unlike other forms of business capital such as debt or equity, where once the set-up arrangements are completed, the money is available. The circumstances governing what will be paid, and when, are all set out as part of the insurance policy, often in complex detail. Businesses therefore need to be prepared to invest considerable resources to make sure that the insurance policy operates as expected to ensure that its access to this capital is reliable.

The concept of 'fair presentation of risk' is a critical part of the UK Insurance Act 2015. This legislation has been designed to promote fairer claims outcomes and to encourage professionalism on all sides of the insurance transaction. However, it does carry pitfalls for the unwary customer, in particular by introducing changes to the duties falling on the customer when arranging insurance. The Act is summarised in section 6 of this guide.

When considering the most catastrophic exposures, the quality of insurance is a key consideration. What is being purchased is a promise by the insurer to pay in future, so the conditions of that promise are important. This means that it is vital to get all of the details of the contract right, including meeting the organisation's own legal duties in putting risk information together and making a 'fair presentation of risk', which goes beyond merely answering insurer questions.

2.3 Different types of insurance cover

Insurance cover is available for a wide range of risks and perils faced by organisations. These are summarised below using the three categories set out at Section 2.1.

- Satisfying Legal and Contractual Obligations
- Providing Balance Sheet / Profit and Loss Protection
- Providing Employee Benefits and Protecting Employee and Contractor Assets

2.3.1 Satisfying Legal and Contractual Obligations

Organisations will need to purchase certain types of insurance policies because they are required by law, or because these are demanded by customers, business associates, banks or landlords. The most important examples of these insurance policies are:

Motor Insurance

By law, any vehicle used on the road or other public place must have Third-Party Motor insurance. This insurance offers protection for legal liability related to an accidental injury, death or third-party property damage caused by the insured vehicle if an employer, employees or other parties acting on behalf of an organisation use a vehicle in connection with the activities of the organisation. The following should be checked:

- That any personal vehicle owned by an employer used for business has insurance which covers business use
- That any vehicles owned by employees or vehicles owned by others used by employees or others acting on behalf of an organisation for business have insurance which covers business use
- That vehicles owned by an organisation are covered by appropriate insurance.

Employers' Liability

Employers' Liability (EL) insurance cover enables organisations to meet the cost of compensation claims (and the associated legal fees) from employees who are injured or become ill at work through the fault of the employer. Employees injured due to the negligence of their employer can seek compensation even after the business goes into liquidation or receivership. Sometimes EL

02 The purpose of insurance

insurance is referred to as Employers' Liability Compulsory Insurance. A growing number of EL insurers offer policies that provide rehabilitation options, so that those injured or sick can return to work sooner.

In the UK, there is a minimum limit of cover requirement of £5 million for EL insurance, and cover must be purchased from an insurer authorised by the Financial Conduct Authority (FCA).

Public Liability

Public Liability (PL) insurance covers any award of damages to a member of the public or other business because of death, injury or damage to their property caused by an organisation or the business activities of an organisation. As with EL cover, PL insurance also covers any related legal fees, costs and expenses. Special consideration must be given to homeworkers who are not employees. Product Liability insurance covers any physical item that is sold or given away. Products must be 'fit for purpose' and the organisation has a legal responsibility for any damage or injury that is caused by the products the organisation supplies. It is important to note that such liability cover does not normally extend to either:

- a) funding the cost of product recall (a separate cover extension); or
- b) a product simply failing to effectively perform its intended function (product efficacy).

If a product is directly sold, given away or otherwise supplied, and something goes wrong with it, claimants are likely to try to claim first from the organisation as the supplier, even if the organisation did not manufacture the product. Normally, such a claim can be passed on by the sued organisation to the upstream manufacturer, or 'subrogated' by the organisation's insurer if they have paid the organisation's claim but then seek to recover costs from the upstream party.

In the longer term, potential changes to UK product liability and product safety laws following the UK's

withdrawal from the EU will lead to changes for organisations bearing liability and regulatory responsibilities for unsafe products. Organisations need to ensure that they understand the obligations that they are likely to have to comply with.

Professional Indemnity

Professional Indemnity (PI) insurance protects an organisation against the payment of compensation to a client who alleges that the organisation has made mistakes or was negligent in the advice it provided. PI also covers the associated legal costs. PI insurance cover may be needed even if the advice given is incidental to the main business activities, including, for example, design work undertaken as part of preparing a quotation. Some sectors may have their own specialist PI policy wordings, for example, solicitors or construction firms.

For many organisations, dependency on technology has increased, and supply chains and distribution channels have changed.

Assets continue to be more intangible and reputation has become the primary business differentiator.

Risks are increasingly complex, connected, and change and emerge at an increasing pace of velocity.

Home is becoming the new workplace hub, where this is possible and desirable, as organisations are right sizing and optimising costs.

In this context, risks must be constantly assessed and insurance arrangements constantly reviewed to ensure they remain relevant.

2.3.2 Providing Balance Sheet / Profit and Loss Protection

Some events would be very serious for a business, either by hitting the balance sheet or impacting the profit and loss account more than the business is willing to tolerate. These events and associated insurance are likely to relate to the property, plant, machinery and other assets of the business.

Business Premises

Business Premises or Commercial Property insurance will cover rebuilding or repairing premises if they are damaged by events such as fire, explosion, malicious damage, storm, flood and damage caused by the impact of vehicles. If the business is a tenant of a premises, confirmation with the landlord should be sought to ascertain who is responsible for insuring the premises and its contents. Then the lease should be checked to ensure that it is consistent with the response. There may be additional specific insurance requirements placed on a business by the landlord in respect of the liability classes of insurance. In some 'civil code' overseas jurisdictions, tenants may have additional responsibilities to the landlord or neighbours in the event of damage caused to their buildings – and this should again be checked before determining the scope of appropriate insurance cover for each business.

Contents Insurance

Premises insurance covers the physical building, but separate insurance arrangements may be required for stock, machinery and contents. This cover can be arranged on the basis of replacement as new or on the basis of indemnity. Indemnity cover is cheaper, but in the event of a loss, the insurer will take wear and tear into consideration when settling the claim, and there may be ambiguity over whether new assets provide equivalent functionality to what was damaged or whether partially damaged assets are reusable. Such wording should be carefully reviewed against business needs (for example, in high-tech environments, where the costs of a reused IT asset failing may be high).

Depending on the type of building contract, there may be a need for fixtures and fittings to be

insured. It will need to be determined who these belong to and who is responsible for insuring them.

Business Interruption

Business Interruption (BI) insurance provides cover for loss of profits typically triggered by damage to physical assets used by but not necessarily owned by the insured, resulting from events including fire, storm and machinery breakdown. Most Business Interruption policies will also include increased cost of working to provide reimbursement for additional expenditure incurred by the insured in order to avoid or mitigate a reduction in turnover (or wider business disruption) following an insured event. Additional costs will need to be identified and any unusual items declared up front, whilst a business should also determine how long it might take to get back to business as usual in the event of a major loss.

Organisations will also need to think about whether all customers will return immediately when business operations are restored to pre-event levels, whether recovery promotions would be required, etc. Losses can seriously disrupt cash flow, and insurance arrangements will need to provide appropriate protection.

BI cover has evolved to additionally include other events that might give possibility to a loss of profit, including:

- Denial of access because of damage near the premises
- Loss of an attraction that draws customers to the premises
- Failure of power supplies or telecommunications to the premises
- Damage at suppliers' or customers' premises
- Supply chain disruption
- Notifiable disease
- A range of specialist non-damage business interruption (NDBI) triggers involving the loss of intangible assets such as intellectual property, reputational harm, trade disruption insurance, and others.

02 The purpose of insurance

'Covid BI': The FCA test case

The coronavirus pandemic has led to widespread disruption and business closures, resulting in substantial financial loss. Many customers have made claims for these losses under their BI insurance policies. There has been widespread concern about the lack of clarity and certainty for some customers making these claims, and the basis on which some firms are making decisions in relation to claims.

Most small and medium-sized enterprise (SME) policies are focused on property damage and only have basic cover for BI as a consequence of property damage. But some policies also cover business interruption from other causes, in particular infectious or notifiable diseases (disease clauses) and non-damage denial of access and public authority closures or restrictions (denial of access clauses). In some cases, insurers have accepted liability under these policies where such disruption arose due to Covid outbreaks and/or government restrictions. In other cases, insurers have disputed liability, leading to widespread concern about the lack of clarity and certainty.

The issues surrounding BI policies are complex and it was recognised that they had the potential to create ongoing uncertainty for both customers and firms. The FCA accordingly sought clarification from the High Court as part of a test case aimed at resolving the contractual uncertainty around the validity of many BI claims. The FCA advanced arguments on behalf of policyholders in the public interest. The test case was based on a representative sample of policy wordings.² The High Court's decision on the test case was subject to a leapfrog appeal to the Supreme Court.

The Supreme Court handed down its judgment on 15 January 2021, substantially allowing the FCA's appeals and dismissing the insurers' appeals. This means that many thousands of policyholders who have cover should now have their claims for coronavirus-related business interruption losses paid.

The judgment from the Supreme Court and High Court provides policyholders and insurers with clarity about whether customers have cover and can make a valid claim, and the amount due to policyholders.

The Financial Conduct Authority's (FCA) – Victory for policyholders, but a limited one

Whilst clearing up some of the disputes as to the validity and intentions of common Business Interruption wordings and extensions, and confirming cover under a number of common policy extensions, the test case is not quite the 'victory' to policyholders that many commentators first contended.

With only a small subset of Business Interruption policy extensions considered, the scope of the FCA test case was relatively narrow if compared to the totality of potentially relevant cover. Claims for interruptions to business's operations available under other policies – or even other sections of Business Interruption cover – were not considered. Claims outside the scope of the test case continue to escalate through the courts, with the settlement of these claims yet to be seen and many key points undecided.

Certainly, the judgment will bring sweeping changes to the way in which policies are constructed in the future (with most related cover now explicitly excluded as standard). However, for many policyholders, the judgment does not provide a straightforward means for judging their own Covid-19 Business Interruption claims and the battle is expected to rumble on multiple fronts for years to come.

² Herbert Smith Freehills & Financial Conduct Authority, Business interruption insurance test case: Representative sample of policy wordings, 9 June 2020. <https://www.fca.org.uk/publication/corporate/bi-insurance-test-case-representative-sample-of-policy-wordings-9-june.pdf>

Assets Protection

Depending on the nature, size and complexity of the business, it may decide to purchase specialist types of insurance, for example, for:

- Loss of cash cover for loss of money in transit or from business premises
- Goods in transit cover against damage to goods while being transported
- Credit cover against debtors unable to pay as a result of bankruptcy
- Crime loss of money or stock resulting from dishonesty / theft cover
- Engineering specialist cover for machinery, including computers
- Aviation cover relating to use or ownership of aircraft
- Marine cover relating to use or ownership of vessels

Although it is strictly speaking a liability class of insurance, it is a legal requirement for some types of machinery, such as lifting equipment, boilers and pressure vessels, to be inspected regularly. A specialist insurer will be able to tell a business if this applies to its plant and machinery, and can usually arrange for the necessary inspections to be undertaken.

Terrorism

Businesses in Great Britain can purchase terrorism cover for property and business interruption through the Pool Re scheme, which is backed by the UK Government. This terrorism cover can only be purchased as an extension of existing Property Damage/Business Interruption policies and not on a standalone basis.

Cyber

As of late 2021, the number of ransomware attacks worldwide increased 170% compared to 2020, with 39% of businesses having reported cyber security breaches or attacks in the last 12 months. These challenges have therefore created a significant escalation in demand for cyber insurance, as organisations try to protect themselves from exposures arising out of the risks and threats they are facing in the

digital age, which have been heightened for many organisations with the rapid rise in homeworking.

Most cyber policies cover both first-party and third-party losses. Cover for first-party losses usually includes cover for cybercrime investigations, data recovery, reputation management, notification costs and extortion payments. They may also cover business interruption where caused by a cyber incident. Cover for third-party losses usually includes damages and settlements, and defence costs for claims of a breach of General Data Protection Regulation (GDPR).

However, given the significant cyber exposures facing companies, as evidenced by the significant losses incurred by cyber insurers in recent years, the cost of cyber insurance has increased drastically since the onset of the pandemic. To that end, insurers are much more careful about the risks they are willing to write, with insureds increasingly required to have Multi-Factor Authentication, data segmentation and encryption, and network scans in place. In the current market, securing capacity at a viable cost is therefore highly dependent on the exposures of the insured, its risk management processes, and the extent to which the private insurance market can realistically assess aggregate exposures.

Contractors All Risk insurance (CAR) and Owner Controlled Insurance Programmes (OCIP)

Contractors All Risk (CAR) insurance is a form of insurance designed to cover work carried out by contractors whilst undertaking construction projects – either on an annualised or project-by-project basis. Common types of covers included in the policy are:

- Contract Works: Cover for damage or loss to fixed (i.e. buildings) and unfixed (i.e. on-site materials) assets during the course of construction
- Plant and Machinery: Cover for both own and hired-in plant, including theft, loss and damage
- Public Liability: Cover for damages or bodily injury to a third party as part of a construction project
- Employers' Liability: Cover for injury or illness sustained by employees of the insured during the course of a construction project.

02 The purpose of insurance

A contractor employed by an organisation is often required to have adequate insurance in place, via its own insurance arrangements – a Contractor Controlled Insurance Programme (CCIP). In contrast, an Owner Controlled Insurance Programme (OCIP), whilst still providing the covers available under a CAR policy, sees the Contractee arrange all-party cover for the project (covering all contractors under a single agreement). This allows for cost efficiencies – with contractors typically including insurance costs in bids – as well as greater control over the quality of coverage for construction projects.

2.3.3. Providing Employee Benefits and Protecting Employee Assets

Providing injury, illness or death-in-service insurance to staff is a valued benefit that can help a business to recruit and retain the right people, whilst protecting the business. Health insurance for employees will facilitate early intervention in any illness, which should help reduce absence and save money for the business.

Life and Health

Life and Health insurance can often be relatively low cost and highly attractive to employees as an employee benefit. Whilst the precise terminology used to describe the different types of Life and Health insurance may vary, the following options should be considered:

- **Life:** Pays out a lump sum/regular income on death of the life insured
- **Critical Illness:** Provides cover following diagnosis of a serious disease
- **Income Protection:** Pays regular income following illness or injury
- **Private Medical:** Covers the cost of private medical care
- **Permanent Health:** Provides benefits in the event of prolonged illness or disability
- **Personal Accident:** Pays fixed benefits in the event of death or loss of limb or sight
- **Travel:** Covers employees travelling and working aboard

Loss of a Key Person

If the business relies heavily on one or two members of staff, there could be serious consequences if they become ill or die. Small businesses in particular often depend on a key person for generating sales, managing a vital client or providing core expertise. Businesses can purchase Key Man insurance, which makes a payout in the event of his or her death. In any case, this type of cover may be required by the business's bank or financier. Critical Illness insurance would respond in the event of serious disease or illness.

Directors' and Officers' Liability

Directors and officers of organisations can be held responsible for a range of issues, including data protection, fraud, negligence, as well as health and safety. Directors' and Officers' Liability (D&O) insurance pays the cost of defending lawsuits and any compensation that may be awarded. There may be restrictions on the scope of D&O insurance cover that a business can purchase, because of the limitations and restrictions in the Companies Act and the exclusions found in many D&O policies. An insurance broker will be able to provide the business with more information.

Pension Trustee Liability

Pension fund trustees have a personal liability for breach of trust in connection with their role. Pension Trustees Liability insurance can provide cover for the trustees, pension scheme and sponsoring employer for damages, settlements, civil fines/penalties, defence costs and other expenses.

2.4. Alternative Risk Transfer

Alternative Risk Transfer is a section of the insurance market that provides methods and structures that allow organisations to purchase insurance coverage and transfer risk outside of the traditional commercial insurance market.

With the hard market felt sharply by many insureds,

and in pursuit of cost control and stability, insurance buyers have looked for alternative routes to managing or transferring risk beyond a traditional insurance policy of the types summarised above.

Captive

A captive is a dedicated insurance company that is set up, owned and controlled by the business it is insuring. The primary purpose of the captive is to insure the business's own risk, and this brings the benefit of enjoying underwriting profits in the event of good claims records, a greater degree of control over its insurances and potentially greater surety of claims approaches. Captives are commonly operated by larger businesses, with significant upfront capital, running costs and regulatory challenges to navigate. 'Rented' captives and similar structures can reduce some of these set-up costs and may be accessible to smaller companies with less resources.

Virtual Captive

A virtual captive is a multi-year insurance agreement that emulates the mechanics of a traditional captive; however, the insureds' self-financed, self-insured retention is held on an insurance company's balance sheet. The insured pays a premium to a capacity provider (a regulated insurance company) which – whilst also taking a commission from the premium – pools the insureds' premiums. In the event of a number of losses, the pooled premium is used up (with an agreed amount of conventional insurance provided from the capacity provider as back-up). In the event of a good claims record, the remaining pooled premium is returned to the insured at the end of the term.

A virtual captive thereby keeps the mechanics of a traditional captive, without the cost and complexity of setting one up. Nonetheless, as with a traditional captive, additional capital investment is likely to be

required in order to begin to adequately pool premiums.

Parametric Insurance

Parametric insurance covers the probability of a predefined event happening instead of indemnifying any actual loss incurred. The insurance cover is triggered if pre-defined event parameters are met or exceeded, with a contractually simple pre-agreed payout provided if the parameter threshold is reached or exceeded. For instance, using available weather records and loss data, an insurer may agree to provide a particular payment every time rainfall reaches a certain level in a 24-hour period.

Parametric insurance therefore provides the client with greater certainty with regards to claims payment. However, it currently remains more expensive than insurance covers available in the conventional markets and is generally used to cover risks for which clear, objective data is available.

Further information is provided in the Airmic white paper Parametric solutions: Overcoming the challenge.³

Structured Finance, Loss Portfolio Transfer and Other Alternative Risk Transfer (ART) instruments

The Alternative Risk Transfer (ART) market is complex and rapidly evolving, with a range of structures available (often on a bespoke basis) to help fund potential losses. These can vary from essentially just a cash flow smoothing mechanism to spread unpredictable costs over time (but where the organisation still pays its entire actual losses), to significant transfer of risk based on defined contractual parameters, to almost everything in between. Other tools exist for example to facilitate M&A activity, such as to package up and transfer historic liabilities to create a clean break with a division to be divested. Specialist advice is recommended if a business is interested in exploring such options.

³ <https://www.airmic.com/technical/library/white-paper-parametric-solutions>

03 Selecting an intermediary

The internet allows access to a wide range of intermediaries and insurers. In addition, depending on the business sector, a business's trade association may be able to assist with the identification of suitable insurance providers.

Even if the relevant trade association can help, businesses should consider appointing a professional insurance broker because they have specialist skills and can save time and money.

Businesses that are choosing a broker for the first time should think about asking business associates for recommendations. There are many brokers to choose from and some specialise in particular types of insurance and/or different types of industries.

The business should decide whether to use a large or small broker. Large brokers will deal with more insurance companies and should be able to negotiate a preferential premium based on the volume of business placed with a particular insurer. Also, large brokers may have more expertise if the business is a specialised type of business, although small brokers will often focus on niche activities or businesses. Businesses should always discuss and agree the level of service that they expect from their broker.

The broker is legally the business's agent and may keep a percentage of its premium (often referred to as brokerage), but may also receive additional commission from the insurers. It is the business's legal right to know how much the insurance broker or agent is earning on its account and how each component of this income arises, so that it can be confident there is no conflict of interest and that it is getting good value. If the broker does not volunteer this information, the business should ask for it and ensure it covers all types of commission/brokerage and any other fees from insurers. **[See the Glossary – Remuneration and Commissions]**

Their broker will be able to advise the business on the practical interpretation of the requirement for it to always act in good faith and how this relates to

insurance placement and claims. An insurance broker can undertake a range of services as outlined in **[See the Glossary – Insurance Broker Or Intermediary]**

If the broker makes a mistake and the business suffers a loss and fails to have a claim paid by an insurer, it will need to be sure that the broker will make good its mistake. The business is entitled to know that its interests are protected and its broker is adequately insured. So, it is worth the business asking the broker what Professional Indemnity (PI) or Errors and Omissions (E&O) insurance it has in place and reviewing the detail of its terms of engagement or Terms of Business Agreement (TOBA) to ensure that its service commitments meet the business's expectations and to check for capped or excluded liabilities.



When the business selects an insurance broker, it should make sure that the broker has the expertise it requires, by asking:

- What experience the broker has in the business's business sector to ensure that the broker understands the business's insurance needs
- What help and support the broker will provide when the business makes a claim
- Can the broker provide the specialist support the business requires, for example, risk surveys or risk management advice
- Can the broker demonstrate how it will help the business manage compliance with the Insurance Act 2015
- Can the broker demonstrate full transparency and clarity over its income and any potential conflicts of interest
- Can the broker provide appropriate references for the business to review

In order to properly consider the above, the business may want to consider running a tender to appoint a broker. Running a tender can demonstrate good procurement governance and encourages brokers to secure the most competitive results in order to win the business (which is particularly important given the challenges of a hard market). Because of the complex ways in which some brokers earn much of their revenue, via commissions and fees from insurers, different broking organisations will have particularly strong relationships with some insurers, which they can leverage to achieve more competitive terms, but this will require the business to have enough information to make an informed choice whilst ensuring a broad spread of bidding insurers.

There are two main types of tender commonly used in the market that the business may want to consider.

Conceptual Broker Tender: A selection of brokers respond to a Request for Proposal (RfP) with an overview of their services, areas of specialty and market connections. Proposals may include very



Running a tender to appoint a broker can demonstrate good procurement governance and encourages brokers to secure the most competitive results in order to win the business

rough premium indications, but these will not be backed by specific insurer quotes. A broker is subsequently selected based on variables including its costs, services offered and market reach – and the tender then goes out to insurers to place the business's risk.

This type of tender was particularly common in the soft market, where broker premium estimates were relatively accurate as insurers were eager to win business. However, in an evolving and more challenging hard market, the scope for later surprises is greater.

Written Lines Tender: Multiple brokers, usually two, are placed in competition with one another and are provided with exclusive access to their preferred markets, with the business secured by the broker who secures the best terms (while the insurance buyer judging the balance between price and cover).

The process ensures that insurers are only approached by one broker, allows brokers to utilise their strongest relationships and enables the insurance buyer to appoint the broker based on their insurance priorities – typically deciding on (i) cover quality and (ii) cost. This form of tender can be particularly worth considering in a hard market to maximise the level of competition.

Whilst a broker tender ensures increased competition – driving brokers to secure the best possible terms to secure the business – tendering brokers too often is ill advised, with benefits also to be found in developing relationships with brokers and insurers over time as they build an understanding of the business's risk and are incentivised by a longer-term partnership.

04 Choosing an insurer

Most buyers of insurance regard cost and suitability of cover as important criteria when choosing their insurer; however, price and policy cover should not be the only considerations.

The most important service purchased from an insurance company is the full and prompt payment of the claim when a loss occurs, so securing certainty around claims response should also be a prime consideration.

Several other factors are relevant to a business's choice of insurance company. In the first instance, the overall reputation of the insurance company is important, both in general and in relation to the business's specific business sector.

In addition, the business should include the following in its evaluation:

- Financial strength and credit rating of the insurance company
- Does the insurance underwriter understand the business
- Areas of specialism relevant to the business
- Level of service support and range of advice available
- International capability if the business has overseas operations
- Ability to explain coverage so that the business is clear how the policy responds to a loss
- Scope of claims service so the business knows what the broker will do, and what it need from the business, when a claim occurs
- Flexibility on coverage terms

The financial strength of the insurance company is vitally important. The insurance broker is likely to have solvency criteria for insurance companies that must be fulfilled before placing business with them. However, the business should check that this is the case. In the UK, the insurance market divides into commercial insurance companies, mutual insurers and the Lloyd's market:

- Commercial insurance companies offer a very wide range of insurance covers
- Mutual insurers are usually specific to a particular business sector
- The Lloyd's market tends to concentrate on more specialised or unusual risks

Ancillary services made available by insurers should also be considered ahead of renewal, in particular around emerging or changing areas of risk. Many insurers are looking to build long-term strategic relationships with their insureds and may offer additional services such as discounted risk engineering work, or enhanced claims response services to support clients who may not have suffered a similar loss before. This will usually include legal support but can be particularly varied in the case of cyber insurance, with providers offering an array of additional services including staff training, crisis response helplines, IT forensic support and IT infrastructure advice. These additional services should be considered ahead of renewal and the choice of insurance provider.

The FCA regulates all insurers in the UK. For some types of cover, the business can opt for an insurer based in the European Economic Area or Switzerland, provided it is regulated in its own country. However, for Employers' Liability and Third-Party Motor insurance, the business must use an FCA-regulated insurer.

If the business is small and has a complaint about its insurance broker or insurance company, then the Financial Services Ombudsman Scheme may be able to assist. If one of the business's insurers fails to pay a claim because of insolvency, it should notify the Financial Services Compensation Scheme (FSCS), which is the statutory fund of last resort for customers of authorised financial services businesses in the UK.

Policy Standardisation

Securing robust coverage in the current market is even more of a challenge given the industry trend towards increasingly standardised policy wordings. On one level this is a sensible practice, allowing for clarity, the spread of best practice and underwriting efficiency, provided technically skilled underwriters and brokers can then amend the policy wording to reflect specific client needs. However, too often generic policies are not being adapted, even where underwriters agree that a bespoke solution is needed, leaving policy wording ambiguous and with significant gaps in coverage. This enables too much uncertainty to affect claims. Risk needs to be carefully analysed and explained, with policies being duly negotiated to fit.

4.1. The Hard Market

Insurance is a famously cyclical market, with long periods of low rates punctuated by massive cost increases. The insurance market is currently the most challenging it has been for 20 years, following a period of hardening that began in 2019 and was severely accelerated by Covid-19, as evidenced by a reduction in capacity, a reduced appetite for risk and significant but uneven spikes in premium.

- In the financial lines market, significant reductions in capacity (including the withdrawal of AXA XL from the London market financial lines business) have led to rocketing premiums and coverage restrictions.
- In the property market, with global warming and other considerations leading to increases in the severity and frequency of losses in recent years, few have escaped underwriters' new pricing models, guidelines or internal strategies with regards to capacity deployment.
- In the cyber market, following high loss ratios for the 2019-20 year owing to increases in the frequency and severity of ransomware claims, exacerbated by the advent of homeworking, significant pricing increases and reductions in cover have become the norm.

Most obviously, hard markets are defined by rising premiums. These are quite different to the sort of variation the business might see in most other markets and can go through triple-digit swings within a 12-month period.

Beyond this, the business should expect coverage to be reduced through (often very subtle) changes to its policy wordings. These changes aren't always flagged by insurers and brokers, so this is something that all insurance buyers should bear in mind when reviewing the small print.

Finally, hard markets create a harsher environment for claims, which take longer to resolve or negotiate, and are more likely to be disputed. Mactavish customer research shows that – excluding small or attritional losses – 45% of large and complex commercial claims are disputed by insurers, they take an average period of three years to resolve and the typical settlement value is 60% of the original claim. And those are the statistics for a pre-hard market claims environment.

05 Insurance Buying Process

An insurance policy is a legal contract between the buyer and the insurer, arranged with the support and advice of the insurance broker.

This section outlines the nature of the insurance contract and summarises the relevant information required by the insurer on the risks to be covered. Additionally, it includes information on the broker contract. Finally, it considers the responsibilities of buyer, insurer, broker and other potential service providers.

5.1 Outlining The Buying Process

The insurance buying process will vary depending on the circumstances of the business. However, there are seven key elements in the insurance buying cycle, which fit around the placement or renewal of a business's insurances.

The elements are focused on pre-placement preparation for arranging insurance, activities during the placement process and actions after placement

Table 1 The Insurance Buying Cycle

Pre-placement:
1 Define risks and insurance requirements
2 Select or confirm a broker and its responsibilities
3 Build relevant risk information – to disclose to insurers and determine insurance coverage requirements
During placement:
4 Market the risk to insurers
5 Negotiate and agree insurance policy terms
Post-placement:
6 Manage compliance with insurance policy conditions
7 Handle claims

to ensure that the insurance responds effectively if required.

5.2 Understanding Insurance Contracts

An insurance policy is a contract made up of a number of elements. The policy does not exist in isolation and its reliability is affected by:

- the risk information disclosed by the customer when arranging it; and
- the contractual duties assumed by the broker as part of placement.

The following elements are all pertinent to a contract of insurance. (Key terms are further explained in the glossary)

- The insurance policy or contract:
 - Policy document or wording, which sets out the full terms and conditions
 - 'Policy Schedule' summarising key terms and showing the limits, deductibles or excesses, and the structure of cover. This may be a separate document or it may be attached to the policy
 - 'Broking Slip' is often used by brokers for insurers to physically or electronically agree to provide the insurance cover. This will detail broker commissions and administrative aspects, but may also contain additional policy terms
 - 'Insurance Cover Certificate' – an evidence of cover provided for certain classes of business insurance, in particular, where required for regulatory or legal purposes
 - 'Summary of Insurance' – produced by some insurers as a simplified document showing cover, terms and conditions; however, this is normally not a legally binding document.
- Risk information supplied by the insurance buyer is likely to consist of one or more of the following:
 - Submission documents – bespoke, client-specific

Buying Insurance in a Hard Market

Given the current challenges in a hard market, with higher and more variable pricing, less capacity and narrower cover, steps should be followed to deliver the best outcome:



Take control of the process: The business should take a lead in driving its broker to work harder for it, and should have a clear view of its broker's marketing strategy and expectations. The business should hold regular update sessions keep everyone accountable.



Start earlier: In a hard market, renewal planning should commence at least four to five months ahead of renewal to ensure that conversations with insurers get underway, additional information requests are responded to and options can be found in the event of unwelcome surprises.



Stand out from the crowd: Underwriters need to understand why the business's risk is attractive. To do this, they need to understand the business and its approach to risk management. The business should go beyond the minimum pro forma responses and think about how it can make the business stand out – both to 'sell' its risk and also to ensure it has complied with its legal duty of fair presentation of risk.



Be willing to change your insurers and broker: In a market this challenging, businesses need to have options, including a willingness to switch their insurance partners if better and more cost-effective cover is available. Considering different types of tender [see section 3] can increase competition and deliver the best possible outcome.



Seek independent advice: Insurance policies are increasingly complex and require technical expertise if they are to be interpreted properly. If the business's insurance buyer is a non-specialist, it can be impossible to know if they really are getting the best available cover.

documents setting out key risk information for insurers (typically used for larger and more complex clients or classes of insurance)

- Proposal forms – standardised Q&A-based forms containing essential risk information for the class of business concerned (typically used for smaller businesses and specific classes of business such as Professional Indemnity insurance or Directors' and Officers' Liability insurance)
- 'Statements of Fact' – used more commonly by insurers for smaller business clients; this is normally an insurer-produced document setting

out assumptions regarding business activity. This should be reviewed carefully by the insurance buyer to ensure accuracy.

The broker contract is likely to consist of one or more of the following:

- Terms of Business Agreement (TOBA) – the core terms and conditions of broker service provision
- Service Level Agreement (SLA) – where required, it specifies service expectations and any client-specific fee structures or key

05 Insurance Buying Process

performance indicators

- Letter of Engagement – where required, it sets out a client-specific summary of key terms, in particular, any issues which vary from the standard TOBA position (such as a specific limit of liability or the term of the broker's appointment).

The insurance buyer should ensure that they fully understand the nature of their contract with the broker so that the engagement with the broker and insurers in the buying process produces the desired outcome – a fully effective insurance cover which will respond properly to insured losses.

5.2.1 Contracting Standards

Given the challenges facing insurance buyers, especially in a hard market, it is important that insurance buyers are able to review the contracting standards of their insurance documents, as much of the devil is in the detail. Below are a few examples of things to consider:

- Exclusions: Are there exclusions for operational activities that the insurance buyer would intend the insurance to cover, and how broadly are these exclusions framed? This can depend on specific carve-backs for some types of loss, or big changes in effect can come down to minor wording differences such as “indirectly caused by” or “in connection with”
- Notification and Claims Handling Obligations: Are there any demanding notification or claims handling obligations? For instance, what events and whose knowledge will trigger the policy requirements and how onerous are the time frames (e.g. “immediately” or “as soon as reasonably practicable”?)
- Other Insurance: How fair is the policy if cover overlaps with other policies? Has the intended order of response been agreed?
- Innocent Non-Disclosure: Is there a clause governing the effect of a breach of the duty of fair presentation of risk, and how does it change the default position of the Insurance Act 2015? Are disclosure obligations extended throughout

the term of the policy?

- Warranties and Conditions Precedent: Are there any Warranties or Conditions Precedent in the policy (see glossary), or ‘sweep-up’ clauses giving greater legal status to every single policy obligation, and are there any clauses seeking to limit remedies in the case of breach?

5.2.2. Broker Terms of Business Agreement (TOBAs)

As well as considering the contracting standards of an insurance contract, it is also worth the business paying attention to the Terms of Business Agreement it has arranged with its broker. Again, a few of the areas to consider include:

- Wording checks: Are there any clauses assigning the business with sole responsibility to check that policies are correct, or are there any clauses outlining the brokers' responsibility?
- Fair presentation of risk: Does the broker have any specific duties to:
 - a) advise the business on required disclosure;
 - or
 - b) manage its own material knowledge (since its knowledge effectively counts as your own)?
- Remuneration transparency: Does the TOBA detail a wide range of potential sources of broker remuneration from insurers? [**see the Glossary – Commission**] Does the TOBA require proactive disclosure of the amounts of such remuneration applying to the business's placement?
- Liability: What is the broker's financial limit of liability? Are there outright exclusions for certain types of liability which could be problematic in the event of a problematic claim on a policy placed by the broker?



06 Insurance Act 2015

6.1 Insurance Act and Interpretation

The Insurance Act 2015 remains the most fundamental change to the law of England and Wales, Scotland and Northern Ireland governing commercial insurance and reinsurance since the Marine Insurance Act 1906.

The Act, which came into effect on 12 August 2016, aims to address the imbalance between insurer and insured rights. It made significant changes to several areas, including:

- The duty of disclosure required by insureds and the remedies available to the insurer in the event of material non-disclosure and misrepresentation
- The interpretation of warranties and terms not relevant to the loss

- The abolition of Basis of Contract clauses
- Following further amendment to the Insurance Act brought in by the Enterprise Act 2016, there is also a new right for insureds to claim damages in the event of unreasonable late payment of insurance claims by insurers.

Overall, the new legal framework is significantly more favourable to organisations buying insurance than the old law, with the remedies available to insurers now far more proportionate. However, in reframing the obligations of both buyer and seller of insurance, it is contingent on organisations to ensure their own compliance or else they risk being unable to benefit from the enhancements intended by the Act. The example shown in the box on the first Insurance Act judgment demonstrates the ongoing need to take care when compiling and presenting risk information.

The First Insurance Act Judgment

The first high-profile Insurance Act judgment was handed down on 8 October 2021 – a Queen's Bench ruling on a coverage dispute between a property development joint venture, Berkshire Assets Limited, and its insurer, AXA Insurance UK PLC.

The dispute arose over coverage for an incident on a multimillion-pound residential complex which Berkshire was developing, where an escape of water had resulted in physical damage and business interruption losses.

The judgment upheld the insurer's decision to avoid the claim because of Berkshire's failure at renewal to disclose the fact that criminal charges had been lodged against one of its directors by the Malaysian Government.

The decision to avoid the claim was upheld despite the fact that the charges arose through the director's involvement in another entity unrelated to Berkshire and that all charges against the director were subsequently dropped.

The court held that the criminal charges were in any case material information and also agreed that AXA would not have underwritten the risk had the criminal charge been disclosed – allowing it to avoid the policy. One factor that swayed the court was an AXA practice note providing guidance to underwriters that it was outside of the AXA underwriting strategy to write risks in circumstances where there were criminal allegations lodged.

The case demonstrates the important effects of the Act on professionalism in insurance placements, both on the part of the underwriters, who must show their workings on why they have accepted a risk or where they would draw the line and decline (which is where the practice note proved crucial), and on the part of insurance buyers, who must do their due diligence in complying with the duty of fair presentation of risk, especially reasonable search, and who would do well to be able to demonstrate this in the event of a dispute.

6.2 Managing duty of fair presentation of risk

In managing the duty of fair presentation of risk, there are five main areas insurance buyers should be aware of.

Further information is provided in the Airmic EXPLAINED Guide *Making the most of the Insurance Act 2015*.⁴

Issue	Comment	Points to consider
Senior management knowledge	<p>There is an absolute requirement to disclose the knowledge of senior management.</p> <p>However, the Act does not specifically define who falls into this category.</p>	<p>Consider who might be included in senior management for the business, and seek to agree a definition directly with insurers.</p> <p>The business will need to make sure that the individuals within that defined group disclose material information within their unique knowledge of the insured risk.</p>
Insurance team's knowledge	<p>Similarly, the Act requires the business to disclose the knowledge of those responsible for placing insurance.</p> <p>This is not limited to the organisation itself and, in particular, includes its broker's knowledge.</p>	<p>Ensure that the broker team is keeping records of information gained from their interactions with different parts of the business and any responses to insurer queries. Consider working this into the broker's contract.</p>
Reasonable search	<p>This will require adequate enquiries to be conducted to identify information that would be important to insurers.</p> <p>These searches are expected to seek out information that could be material for insurers, from business units, relevant third parties involved with the business or anyone insured by the policy.</p>	<p>Consider whether any key business units or functions may have material information about the risk.</p>
Information needs to be clear and accessible	<p>Presenting information clearly for insurers, including highlighting unusual activities or concerns about the risk, and avoiding data dumping.</p>	<p>Use commentary and guidance to help underwriters navigate the material, and use contents pages and indexes to keep it accessible.</p> <p>Include specific sections on unusual or higher-risk areas.</p> <p>Use specific signposts to other potentially useful documents that insurers may request (and be as specific as possible by using page references, etc.).</p>
Putting the insurer on notice	<p>Insurers also have a duty to make reasonable enquiries based on the risk information presented to them and waive their right to information that would have arisen from such enquiries if they fail to do so.</p>	<p>Where information is not readily available, consider identifying 'known unknowns' to insurers as specifically and clearly as possible. This allows the business to focus down on areas of importance to the insurers based on their follow-up queries.</p>

⁴ https://www.airmic.com/system/files/technical-documents/Airmic%20EXPLAINED%20Guides_Insurance%20Act.pdf

6.3 Impact of Warranties Explained

A warranty is a term in an insurance contract that must be strictly complied with by the insured. Prior to the Act, a breach of a warranty would discharge the insurer from any liability under the policy, even if the breach was unrelated to a claim. Under the Act, the effect of a breach of warranty is to suspend liability, which is potentially a less severe situation for the insured.

See the Airmic Guide *Warranties in Insurance Policies: A practical guide to warranties in insurance policies*, for a full explanation of this.⁵



It is contingent on organisations to ensure their own compliance, or else they risk being unable to benefit from the enhancements intended by the Insurance Act 2015.

6.4 Abolition of Basis Clauses Explained

A basis clause is a declaration contained in either a proposal form (if submitted) or an insurance policy that certain representations made by the insured (including answers given in a proposal form and any other information supplied) are true and accurate. This declaration is, by operation of the basis clause, incorporated into the policy as a warranty given by the insured. Such clauses have been considered to be unduly onerous and unfair as it can be very difficult for an insured to comply with the strict terms of such a warranty.

Basis clauses are prohibited by the Act. See the Airmic Guide *Basis Clauses: A practical guide to basis clauses in insurance contracts* for a full explanation of basis clauses.⁶

⁵ <https://www.airmic.com/technical/library/warranties-insurance-policies>

⁶ <https://www.airmic.com/technical/library/basis-clauses>

Scenario analysis is an exercise of considering potential risk events or occurrences and asking the questions: ‘What might happen, how might this impact our business, what could we do?’

Scenario analysis is an important part in any insurance buyer's toolkit and supports most stages of the buying process outlined in the previous section.

From the insurance programme perspective, the primary objective is to establish how the insurance policies would respond to a specific type of loss. This creates certainty as to coverage or identifies weaknesses or gaps for further attention. This is particularly useful where there are, for example, unusual cost components anticipated as part of a claim or exposures that fall into grey areas between types of insurance.

Scenario analysis is therefore most critical for stages 1 and 3, and 5 and 6 of the Buying Cycle outlined earlier, but it also has implications for the whole process.

As outlined below, the process requires participation from senior and operational management and other colleagues who may not previously have considered insurance in an in-depth way. There is an inherent opportunity to raise the profile of insurance within a business, bringing key issues and challenges (e.g. fair presentation of risk, condition compliance, etc.) to the consciousness of key stakeholders. This in turn can feed into success in other aspects of the placement process, including:

- Maximising compliance with the duty of fair presentation of risk by unearthing special or unusual facts and particular concerns about the risk. These are explicitly considered to be material information under the Insurance Act 2015
- Expanding understanding and reporting of areas where robust risk management strategies are already in place in addition to insurance, as this is also valuable information to feed back to underwriters, who may then be inclined to favourably reassess their view of the exposure

- Raising awareness of key weaknesses in current risk mitigations, especially where these could put the organisation out of compliance with the risk management obligations under its insurance policies.

It is recommended to approach scenario planning in two phases:

Phase one: Establish a framework to prioritise risks and scenarios

Not all risks have the same potential impact on the business. Scenario analysis should be applied to the scenarios associated with risks that could be seriously damaging to the business if the insurance cover failed to respond. Initially, therefore, the insurance buyer should conduct an analysis to establish the level of financial disruption that could not be tolerated. This may be a smaller sum than first envisaged.

The key benefits of such objective financial analysis are twofold:

1. It enables the insurance buyer to position insurance alongside other sources of finance, focusing on its value to the business, rather than seeing insurance as a commodity.
2. It brings clarity as to which policies will be included in the exercise, i.e. those that are relevant to the risk and could incur a loss above a defined level.

Phase two: Conduct scenario analysis for the most material risks.

Once it has been decided where to focus, the next step is to determine the most critical exposures and conduct workshops, with all relevant personnel, to make sure that the insurance policy is structured appropriately and wordings are tailored to any particular circumstances. The main objectives are:

07 Scenario Analysis

- Clarifying what cover is required
- Building internal understanding of the scope of the insurance cover
- Clarifying what business information is material to a fair presentation of the risk
- Stress-testing policies in advance of an actual loss, identifying any limitations or gaps
- Considering what steps are required post loss to ensure full and rapid claims payment

It is important to recognise that this is a business-specific exercise. The broker and insurer can offer valuable support, in particular to work through how policies will respond to a given situation, but fundamentally, the scenario workshop is an internal insurance buyer responsibility. Personnel involved will vary from business to business and could include:

- Internal personnel: divisional operational management, senior technical and commercial personnel closest to unusual or new activities, internal 'owners' of relevant risk areas (such as health and safety, product quality, security or those tasked with business resilience/continuity planning, etc.)
- External personnel: brokers, underwriters, insurer claims staff, loss adjusters, risk surveyors.

Once convened, making the best use of the mix of knowledge and expertise is critical, and usually requires a very structured forum. Areas for attention include:

1. Setting a clear agenda: Focus on defined risks and business critical risk scenarios as agreed in advance
2. Clarifying required outputs: Deciding on which scenarios to focus on and documenting the wider business impacts and costs, as well as the corresponding analysis of policy response
3. Noting any unusual or notable material information arising that is likely to be key to any future risk disclosure

4. Follow-through: Required operational or insurance policy changes must be put into practice. In particular, formal amendments should be made to the insurance contract and reliance should not be placed on letters of understanding or similar correspondence that are not an integral part of the insurance contract.

Scenario analysis is a valuable way to help a business understand its risk exposures, supports strategic planning and brings benefits far beyond the operation of the insurance programme.

It is worth noting that, before Covid-19 emerged, many businesses' risk registers mentioned pandemics, but the low likelihood factor meant that this risk was typically overshadowed, ultimately leaving many businesses underprepared.

Developing loss scenarios also provides a forum for open discussions across business units and functions, with individuals who may not normally be involved in formal risk reporting processes. The process also promotes the modelling of risk impacts, both operationally and financially. This offers the potential to refocus attention away from more generic macro risks and commercial challenges, which sometimes dominate corporate risk registers, and to identify new or emerging areas of higher risk, and to prioritise risk mitigation strategies accordingly, whilst maximising the role of insurance protection against these risks.

Other benefits of scenario planning are outlined on page 42 the Airmic EXPLAINED Guide *Risk and Managing Risk*.⁷ For more detailed guidance on scenario analysis, refer to the separate Airmic Guide *Scenario Analysis: A practical system* for Airmic members.⁸

⁷ <https://www.airmic.com/technical/library/explained-risk-and-managing-risk>

⁸ <https://www.airmic.com/sites/default/files/technical-documents/Scenario-Analysis.pdf>

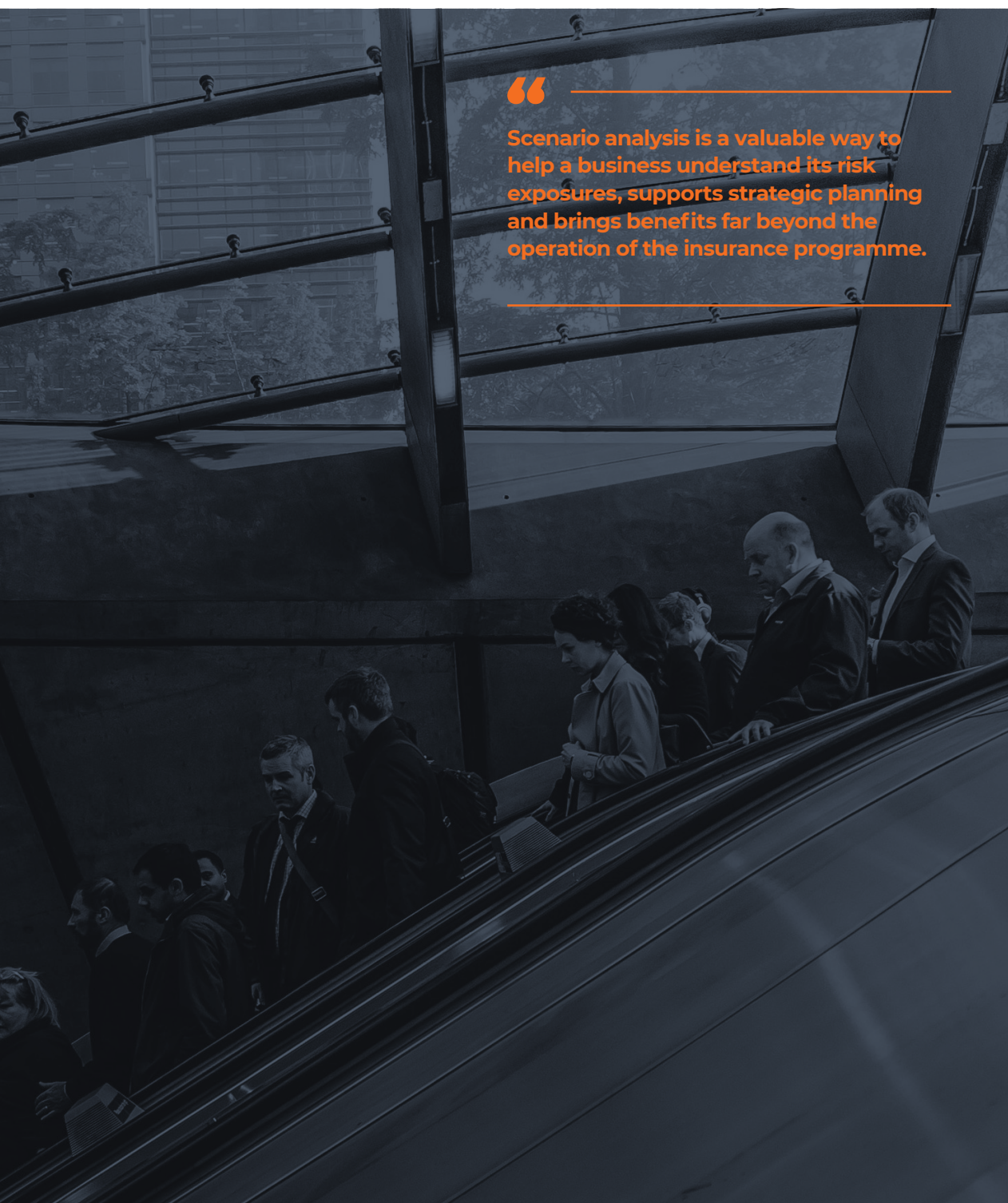


07

SCENARIO ANALYSIS



Scenario analysis is a valuable way to help a business understand its risk exposures, supports strategic planning and brings benefits far beyond the operation of the insurance programme.



08 Getting Claims Paid

The value of insurance is ultimately proven when a claim is paid, and obviously the faster and simpler this process is the better for the insured organisations.

Much of the groundwork for a smooth, fair settlement lies in the approach taken to disclosure and policy placement, long before a loss even occurs. As noted in the research statistics above, too often for large and complex claims, this process is delayed and is then subject to dispute or uncertainty, and this is becoming more common in the hard market. But there is much a business can do to avoid this outcome.

8.1 Pre-Loss Priorities Explained

Getting the contract right at placement will limit the scope for future surprises. By far the leading cause of insurance claim disputes is uncertainty over whether the events are in fact covered by the policy. As such, the single most important pre-emptive steps to avoid displeasing claim surprises simple reflect the buying advice in section 5 above:

- Ensuring detailed, clear disclosure of the business's risks, in particular, any unusual features or scenarios
- Reviewing policy detail to ensure these are covered and that extensions, sublimits, exclusions, etc. are all appropriate
- Making sure the organisation is aware of its own obligations around operationally managing its risks, advising insurers of material changes, notifying claims promptly, handling claims and obtaining insurer consent, etc.

Specialist advice can help create clarity in this area and negotiate necessary amendments, but this is definitely an area where prevention is infinitely better than cure.

8.2 Claims Resolution

The early phases following a claim is the most common time that businesses make errors that later undermine claim recovery, so pre-planning and knowledge of best practice is invaluable to help ensure everyone knows what to do, what information is needed and how to engage with insurers to avoid the common situation where cover is undermined by actions following a loss.

First, re-checking the detail of policy notification provisions is essential since this can vary widely between policies in terms of the triggers requiring notification, the information and timelines required, or what degree of insurer consent or engagement is required. And all of this comes at a time when circumstances are fraught and everybody's focus is rightly on minimising disruption and getting back to normal operation as quickly as possible. Even innocuous measures such as removing destroyed equipment or acknowledging a third-party claim letter without the insurer's specific consent can breach policy conditions.

Second, consider what immediate advice is required: are there external claimants or scope for regulatory investigation where urgent legal support is essential? Is the claim likely to prove contentious over time – either in terms of disputed or ambiguous areas of cover or just through size or complexity. If so, early advice can be essential to avoid missteps, to present information clearly and to avoid a dispute from ever arising.

Third, complex insurance claims can be, well, complex – and, if so, then policies may also provide specific funding for things such as 'claim preparation' work (evidencing and quantifying the loss) or legal defence costs – which the business should make use of where needed. The business's broker may be able to help explain what its insurers require and any

uncertainties over cover, especially as they may place many similar policies with the same insurers. However, in complex cases, there is often a strong case for using specialist advisors to ensure the business is prepared to engage with its insurers, which will quickly appoint their own coverage lawyers, loss adjustors, forensic accountants and technical experts to look at whether the loss is covered and how much they should pay. This isn't only limited to where a claim is formally disputed or repudiated, there can be material and complex debate over cover entitlement, loss measurement, what kinds of alternative reinstatement are reasonable, which advisers can be used, what business response measures are allowed, how costs are allocated between policies or sections, etc. – the list is almost endless.

For policyholders, this can be a stressful and challenging time to ensure they have access to dedicated, independent and unconflicted advice in these areas, so that all parties can pull together to pursue a fair resolution quickly and support the business getting back to normal. Specialist claims resolution experts focus on supporting this process, identifying and managing the best legal and technical input required, and engaging with the client and its broker to drive resolution.

8.3 Learning from Losses

Claims are sometimes painful but can be a good learning opportunity to avoid the same pain happening again or to remove future grey areas. Some key things to consider after any major or difficult insurance claim include:

- If the incident has led to risk improvements, what is the best way to explain this to the insurers and get their buy-in, so that they don't overestimate the risk (or cost) of recurrence or later recommend a different approach?
 - If the policy was unclear or ambiguous, how can it be negotiated with more clarity (either concerning what is covered or what the requirements are when handling the claim or responding to loss)?
 - What new things have been learned about the business that are material and should be disclosed as part of a fair presentation of risk?
 - Are there expected loss response measures that it would be important for insurers to fund next time but that may not be standard, e.g. goodwill payments or incentives, specialist legal advice, etc.?
-
- What are the risk management learnings to avoid a similar loss from occurring in the future?

09 How Insurance Supports Risk Management

This section summarises how insurance forms an important part of the risk management programme for businesses and demonstrates where insurance, and insurance-related actions, influence and support the risk management process.

9.1 What is Risk Management?

All organisations face many risks, some of which will be well known and understood. Indeed, risk-taking is fundamental to the success of any organisation. The leaders of an organisation must decide the extent to which risk needs to be sought, accepted, addressed or avoided, and their approach to this will determine how risks are managed across their organisation.

The concept of risk management has been of increasing relevance and importance in recent years and has attracted much attention across the whole of society. Risk management is the identification, assessment and prioritisation of risks followed by co-ordinated and economic application of resources to maximise the realisation of opportunity or address the impact and/or likelihood of adverse events (see the Airmic publication 'A Brief Guide to Risk Management').

9.2 ISO 31000 Risk Management Standard

Table 2 identifies each element of the ISO 31000 risk management standard, summarises the risk management actions expected, and illustrates how insurance and the insurance process bring tangible value at every stage.

Insurance is an important risk management tool that allows businesses to minimise the impact of an adverse event by transferring the risk to another party, the insurance company. However, as shown above, this is only one of the risk management benefits of insurance. Insurers, brokers and other service providers bring considerable value through the expertise of specialists and the pooling of risk and claims information.

9.3 Insurance Conditions and Risk Management

As noted in table 2 above, insurance adds value to each step of the risk management process. This is positive when managed well but can descend into a vicious cycle if handled poorly. Most insurance policies will contain risk management conditions, but failure to identify these requirements and actively monitor compliance can lead to them being breached inadvertently. In some cases, condition breach is only identified after a loss has occurred – at a time when it is already too late. This leads to a situation where not only could the risk have been better managed by complying with the policy conditions, but the insurer is then also entitled to some potentially punitive remedies when it comes to settling the resultant insurance claim.

On the flip side, active management of policy condition compliance can enhance a business's risk management systems. Often risk engineering reports, especially where occurring bi-annually or more frequently, will focus on major capex and other snapshot issues at a site. By comparison, risk management conditions in insurance policy wordings often focus on everyday behaviours or maintenance aspects, which are much harder for a risk engineer to identify during a fleeting visit.

Failing to monitor insurance condition compliance can be a missed opportunity to enhance risk management processes. A proactive business can use its insurance policy conditions to actively inform and enhance its risk management standards. Monitoring these standards – be it via more frequent third-party auditing, or by developing the systems in-house to actively identify and correct non-compliance – can drive a culture of risk control and mitigation, before the worst occurs.

Table 2 The risk management process

Element of Risk Process	Summary of Action	Insurance Value Added
Establish context	Consider internal and external landscape, business objectives, risk criteria	Advice and information available from insurance service providers – drawn from their client databases
Risk identification	Consider outcomes from all significant risk sources	Information and reports on internal and external risks from risk specialists employed by service providers
Risk analysis	Quantitative or qualitative analysis using risk criteria	Use of insurance industry data to inform risk impact and likelihood considerations
Risk evaluation	Construct risk profile of key risks to prioritise importance and time to address	Validate by lessons learned from past losses by reference to claims databases
Risk treatment	Options to change controls that avoid, seek, modify, share or retain risk	Risk transfer to insurers using insurance contracts Claims expertise supports business response to and recovery from major losses
Monitor and review	Ensure risk actions and outputs meet requirements	Site audits to validate effectiveness of controls. Training on risk issues
Communication	Consultation on the whole risk process or for specified risks	Information on new and developing risks Risk mapping, e.g. for flood or earthquake

An insurance buying glossary

The insurance industry uses quite a number of technical terms, usually for reasons of precise meaning. Here is a list of the most important insurance terms. More comprehensive lists of insurance terms and definitions can be found at:

www.abi.org.uk/data-and-resources/tools-and-resources/glossary/

www.lloyds.com/help/glossary-and-acronyms

Terms and Principles

Aggregation

The manner in which different losses are grouped together under one limit of indemnity, and usually one deductible. A wide aggregation position will mean multiple claims are subject to only one limit, whereas a narrow clause may mean that the insured has access to multiple limits but may have to pay multiple deductibles.

Average

A clause in insurance policies whereby, in the event of under-insurance, the claim paid out by the insurer is restricted to the same proportion of the loss as the sum insured under the policy bears to the total value of the insured item.

Claim or Loss

Injury or loss to the insured arising so as to cause liability to the insurer under a policy it has issued. Loss is another name for a claim.

Clear And Accessible Disclosure

An explicit requirement included in the Insurance Act 2015 (as part of the 'duty of fair presentation of risk') stipulating that risk information presented to insurers at renewal should be "clear and accessible" – including appropriate structuring and signposting of key risk information and avoiding data dumping large quantities of unstructured information.

Claims Made versus Claims Occurring Policy

A 'claims made' policy covers claims that are made and reported during the policy period, regardless of when a claim occurred. A 'claims occurring' policy covers claims for events that occur during the policy period, regardless of when a claim is made. This is an important difference for liability policies where new claims can relate to historic events and care must be taken when changing basis.

Co-insurance

An arrangement where an insurance policy is backed by more than one insurer. In the event of a claim, insurers will

split the claim payment based upon their pre-agreed share of the policy indemnity. Usually, one insurer will be nominated as lead and they will actively handle the claim.

Commission

Money paid to a third party, typically brokers, for matching customers with insurance providers as an alternative, or in addition, to client fees. Some brokers derive a variety of revenue streams from insurers and may only disclose the generic types as opposed to specific amounts applying to the business's risk placement:

- Client fee: paid by the client as a flat service fee or including add-ons for optional services such as claims handling or risk engineering
- Commission: may be charged as an alternative to a client fee, or in some circumstances, in addition. Levied as a percentage of the premium and paid by the insurer. If applying in addition to a fee, it may sometimes be rebated to the client.
- Insurance Services Brokerage (ISB): a standard additional levy paid by many insurers to many brokers for unspecified administrative services in connection with the client's specific placement, usually as a percentage of the premium, usually between 3.5% and 5%, although it is sometimes more
- Reinsurance commission: if an insurer passes part of the risk on a client-specific 'facultative' basis, the broker may earn further commission on that placement, as a percentage of premium
- Investment income: brokers may hold client money on account before passing it on to the insurer, making investment income on those funds based on the volume of premium
- Scheme/facility or work transfer fees: service fees sometimes applying to all business placed by a broker with a given insurer in a pre-arranged facility, typically paid by the insurers as a percentage of the total value of client premiums in the facility
- Information or advisory service fees: payments sometimes made by insurers to brokers for aggregated client information, wording advice, R&D or strategic

advice. Negotiated on a case-by-case basis but often as a 'broad' percentage of premium across the portfolio either for the current or previous year

- Profit share or profit commission: an additional payment sometimes agreed between insurers and brokers based on the financial performance of the portfolio of clients held with that insurer. Structure varies but income will typically be linked to both premium volume and underwriting profitability. This means that the payments to brokers increase if premiums rise and claims payments are kept low.
- Referral payments: fee or commission payments may be received from third-party service providers recommended by some brokers, including lenders and premium finance companies whose services may be needed if premiums rise steeply.

Condition Precedent

A condition precedent is a harsh contractual term which, if breached, may entitle an insurer to reject a claim (regardless of whether prejudice is suffered) or may mean that cover never attaches.

Contribution

Contribution is a principle that specifies that when insurance is purchased from a number of insurers to cover the same event, and that event occurs, the organisation against whom the claim is notified is entitled to collect a proportionate amount of money from the other involved insurer/insurers. If the insured recovers from all the policies, they must refund payments in excess of the actual loss sustained. Contribution preserves the principle of indemnity. However, covers to protect life and accidents are not typically contracts of indemnity, and this principle does not apply to these covers.

Contract Certainty

Describes a situation where the terms and conditions of an insurance contract are fully agreed and finalised before the inception date of the contract. It has been the subject of a major FSA/FCA initiative since 2004 to improve industry practices around policy issuance.

Coverage

The scope and extent of protection afforded by an insurance policy. This may be defined in multiple ways such as specifying perils, defining the necessary circumstances of

insured loss, locations covered, individuals insured, elements of cost for which indemnity is provided and/or specified policy benefits, etc.

Deductible, Excess, Retention

Deductible is the amount that a loss must exceed before a claim is payable. Only the amount above the deductible can be claimed. Excess is the amount of the claim to be paid by the insured and it can be either voluntary to obtain premium benefit or imposed by the insurer. Retention is the amount of any loss that would otherwise be payable under an insurance, but which the insured has agreed to bear before the insurer becomes liable to make any payment under that contract.

Double insurance

Double insurance denotes overlapping insurance of the same subject matter with two different organisations or with the same organisation under two different policies. This is possible in the case of indemnity contracts such as fire, marine and property insurance. Policy terms such as 'Other Insurance' clauses determine how the two covers interact and should be checked to ensure compatibility. The insured can never recover more than their actual loss and cannot claim the whole amount from both the insurers/policies.

Exclusion

A provision in a policy that excludes the insurer's liability in certain circumstances or for specified types of loss.

Fair Presentation of Risk

The disclosure duty introduced under the Insurance Act 2015, updating the previous duty of disclosure. A fair presentation of risk is one that discloses – in a clear and accessible way – every material circumstance known or which ought to be known and would be revealed through a reasonable search, or that gives the insurer sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purpose of revealing those material circumstances.

Hard Market

A hard market occurs when premiums increase and cover scope reduces. Historic hard market cycles have been market responses to insured catastrophes, years of declining prices and low interest rates that depressed

insurer investment income. Those hard markets were typically confined to specific types of insurance and had limited geographic impact. More recent hard markets have seen double-digit and triple-digit rate increases in most types of business, reduced capacity in key types of insurance and withdrawal by underwriters from some sectors.

Indemnity

The principle of indemnity under a general insurance policy provides for the policyholder to be placed in the same financial position after a loss as they enjoyed before the loss. This is at the heart of most general insurance policies and is designed to ensure that the policyholder is not placed in an improved position following a claim as this might otherwise lead to fraudulent claims. However, should the cost of replacement be more expensive than the original cost of what has been claimed, this need not breach the principle.

Indemnity Period

The period, beginning with the occurrence of damage, where indemnity is provided under the policy. Under a Business Interruption policy, this is usually an estimate of the time expected to be needed to restore the business to its pre-loss trading level. Underestimating this period can severely restrict claims payouts.

Insurable Interest

The purpose of insurance is to return to the same financial position after a loss as existed before the loss occurred. Insurable interest is an essential requirement for issuing an insurance policy that makes the entity or event legal, valid and protected against intentionally harmful acts. Generally, the business needs to have a financial interest in the assets or revenues to be protected in order to take out insurance against them. In some cases, this may not be obvious, for example:

- The terms of a loan or a leasing agreement on a car will probably make the owner responsible for the upkeep of the vehicle. It may be a condition that the owner insures it and, as such, in these circumstances, the owner has a clear insurable interest in the property.
- The owner may have asked for a temporary car to be loaned to them by a garage while their own car is being repaired or serviced. The insurer will agree to do so on the basis that the garage will hold the owner responsible for any loss or damage that occurs whilst the car is in the garage's possession.
- Home insurance policies may cover property owned by visitors and guests of insured persons.

In summary, if a business stands to lose financially from loss or damage to property, then it has an insurable interest in it.

Insurance Governance

Describes an emerging field of policyholder activity focused on ensuring the reliability of insurance. Insurance governance involves a coherent approach to overseeing all aspects of insurance placement: risk analysis, disclosure and fair presentation of risk, insurance contract analysis, placement conduct and broker management, policy compliance monitoring, etc.

Insurance Policy

The insured pays a premium to the insurer as a consideration for a contract of insurance or policy. The policy should be issued before the inception (start) date of the insurance cover. It is a document detailing the terms and conditions of an insurance contract and provides evidence of insurance. There is usually a schedule attached to the policy document containing information specific to the risk and noting active sections of cover, and it may also attach 'slips' summarising key terms for the participating insurer to sign on to and/or certificates to demonstrate the existence of cover. It is important to obtain all elements of the policy documentation that exist.

Limit of Indemnity

Indemnity is the principle whereby the insurer seeks to place the insured in the same financial position after a loss as the organisation occupied immediately beforehand. The limit of indemnity is the maximum amount an insurer will pay under a policy in respect of all accumulated claims arising within a specified period of insurance. It is also referred to as the sum insured or the maximum amount payable.

Limits of indemnity can be on an 'aggregate' basis, i.e. the maximum amount an insurer will pay for all claims during the policy period, or on an 'Any One Claim' basis, i.e. the maximum amount an insurer will pay for each and every claim during the policy period.

Loss Minimisation

The insured should always take all necessary steps to avoid losses and damages to insured property. It is its obligation to minimise the losses to insured property in case of any uncertainties such as blast or fire outbreak. The insured should not be negligible or act irresponsibly towards the property just because it is insured for losses, but must act to protect property and avoid losses in the same way as if these were not insured (subject to obtaining insurer consent where required).

Notification

The process of informing an insurance company that the insured has had a loss and that it intends the insurer to indemnify it. Particular attention should be paid to notification conditions within a policy, with claims payment sometimes contingent upon compliance. Notification of circumstances that may, or are likely to, lead to future loss may also require notification and such terms should be reviewed carefully to ensure compliance.

Proximate cause

Insurance policies provide cover for loss or damage as a result of one or more of the perils listed in the policy. Determining the cause of loss or damage is a fundamental step in considering a claim. In the majority of claims, the cause is obvious, but when more than one cause is identified and not all causes are insured, it can be a complex process to determine whether cover under the policy operates. The policy holder must determine that an insured peril has caused the loss or damage and it is then for the insurer to determine the operation of any exclusion if it wishes to deny policy cover.

This situation is slightly different for 'All Risks' policies, where the policyholder need only demonstrate that damage has occurred to what is insured during the period of insurance. If an insurer wishes to apply an exclusion, it must then prove that the cause was one of the excluded events. The legal context around causation can be complex and fact-specific, and this is a common area of claim dispute.

Reasonable Search

An element of the duty of fair presentation of risk (introduced by the Insurance Act 2015) that requires appropriate enquiries to be conducted to seek out material risk information for presentation to insurers at renewal. These enquiries are expected to be appropriate for the business's specific business and could also extend to outsourced service providers, individual beneficiaries of the cover and/or across its broker's organisation.

Reservation of Rights

An insurer's notification to an insured that coverage for a claim may not apply. This notification allows an insurer to investigate and/or progress a claim without waiving its right to later deny coverage.

Risk management

The identification, measurement and economic control of risks that threaten the assets and earnings of a business or other enterprise. A risk is defined as the peril insured against or an individual exposure

Statement of Fact

Operating as part of the business's insured disclosure and historically more typical in the SME insurance market, this is a series of assumed facts about the business. If such a document is issued, it is important to check this for accuracy or it may affect a future claim.

Subrogation

Subrogation is a remedy to an insurer for an insurance claim that has been paid. The subrogation right is generally specified in the policy and may contain clauses that provide the right to the insurance company to start the process of recovering the payment of the claim from the party that caused the damages to the insured party. In such situations, the insurer represents the interests of the insured. There may be negotiable limitations to subrogation rights available in the policy, for example, to avoid insurers pursuing rights waived by the insured under contract or where otherwise detrimental to the insured's business. Subrogation does not apply to non-indemnity contracts and when payments are paid on an 'ex-gratia' basis (a payment made voluntarily rather than because of an obligation under contract) or in situations where the policyholder receives gifts or charitable donations following its loss.

Time Based Deductible/Waiting Period

A form of deductible, sometimes used in Business Interruption and other policies where loss severity is time-dependent, establishing that an insurer is not liable for losses suffered during a specified period immediately following a loss.

Third-Party Liability

Liability of the insured to persons who are not parties to the contract of insurance and are not employees of the insured. The third party is the person claiming against an insured. In insurance terminology, the first party is the insurer and the second party is the insured. This is similar to the term 'General Liability' used in the US and some other insurance markets.

Utmost Good Faith

Insurance contracts are agreements made in the utmost good faith, sometimes called by the Latin name, *uberrima fides*, which implies a standard of honesty greater than that usually required in most ordinary commercial contracts. Utmost good faith is a principle used in insurance contracts that legally obliges all parties to reveal to the others all important information. A breach in the duty of good faith by the customer would historically have enabled an insurer to avoid an insurance policy. Whilst this specific remedy no longer applies following the

introduction of the Insurance Act 2015, the principle of good faith is still required as part of the new duty of making a fair presentation of risk and can also apply to the insured's conduct during a claim. A policy is voidable if utmost good faith is not observed by both parties.

Warranty

A contractual term in which the insured promises that, for liability to attach, it will avoid a particular activity(ies) during the policy period. If the warranty is breached, regardless of materiality, the insurer can avoid all liability under the policy from the date of the breach.

Insurance Stakeholders and Roles

Insurance Broker or Intermediary

An insurance broker is a specialist with professional skills in handling insurance business. An insurance intermediary acts as the agent of his client but is normally remunerated by a commission (brokerage) from the insurer.

The extent of a broker's responsibility will vary depending on the division of responsibilities between the insured, the broker and any additional service providers. This should be reflected in the terms of the broker's mandate and TOBA/SLA. Key responsibilities common to most brokers' mandates include:

- Advice on which insurances to buy, including the specifics of the different types of policy available, their suitability for the client's business, and benchmarking of limits and premiums against broadly similar businesses
- Support in compiling, checking and presenting risk information to insurers
- Negotiating terms with insurers, generating competition for the client's risk and acting as the main contact point for insurers during placement
- Executing insurance policies – by completing the placement and ensuring all insurance documentation is issued, and handling the client's premium payments to insurers
- Providing transparency over remuneration – covering the fee paid by the client and any commissions also earned from insurers
- Manage and disclose conflicts of interest arising through the broker's role as an intermediary and as an auxiliary service provider to insurers
- Maintenance and retention of records relating to the placement
- Maintaining appropriate PI/Errors & Omissions insurance to cover its activity

Additional areas, which can be a broker's responsibility include:

- Claims notification and handling – although Third Party Administrators (TPA) and insurers may be involved to varying degrees, depending on the type of claim
- Higher levels of disclosure support – compiling risk information for insurers directly from the client's business and/or taking a higher degree of responsibility for its adequacy
- Support with international insurance placements – such as ensuring their regulatory and tax compliance and assisting with the issuance of local policies as part of an international programme
- Add-on services – for example, captive management, risk engineering or survey programmes, business interruption or supply chain risk analysis, etc.

Insured

The insured is the person/organisation buying the insurance and who benefits from cover.

Insurance Buyer

The insurance buyer is the individual or team at the insured's organisation responsible for purchasing the insured's insurance. Responsibilities include:

1. Setting and agreeing insurance requirements based on business needs and priorities and legal requirements
2. Engaging with the organisation's broker – either confirming an existing broker's mandate for the renewal process or when appointing a new broker, agreeing the distribution of duties between the organisation and the broker.
3. Analysing the risks to the organisation's business and communicating coverage requirements and disclosure to the insurers – relying on the support of the broker to the extent the organisation has decided but remembering that the core legal duty to make a fair presentation of risk to the insurers ultimately rests with the insurance buyer. This obligation repeats at every renewal of the insurance policy (including within a multi-year Long Term Agreement)
4. Managing the placement process, giving instructions to the broker, ensuring effective oversight and engaging the insurers in discussions directly where practicable
5. Ensuring that policy terms are suitable for the business (using specialist legal advice where appropriate), confirming the placement and paying the relevant premiums
6. Once policies are in place, ensuring compliance with policy risk management conditions, notification requirements and requirements to disclose material changes to the risk to the insurers.

7. In the event of a claim, managing the notification and handling of the claim – using additional service providers and the broker for support where appropriate (for further details, see section 8).

Insurer

The insurer is an insurance company or Lloyd's underwriter who, in return for a payment (a premium), agrees to make good any loss or damage suffered by the insured as a result of an insured event. Responsibilities include:

- Understanding and underwriting the organisation's risk based on the risk information provided (and asking questions naturally arising from that information)
- In relation to the Insurance Act 2015 specifically, notifying the organisation and/or its broker of policy conditions that differ from the new legal regime if they could prove disadvantageous
- Issuing complete policy wording documentation in a timely fashion
- Informing the organisation or its broker of changes to policy terms
- Maintaining capital adequacy and reserving appropriately against potential losses, to ensure that valid claims can be paid
- Investigating and processing claims in line with policy conditions and any claims agreements in place between the insured, the insurer and other third parties
- Paying valid claims fairly and in a reasonable timeframe (since 2017, this is an automatic implied term of every insurance contract)
- Providing add-on services, for example, risk management or risk engineering advice, or claims handling process support.

Loss Adjuster

Independent qualified loss adjusters are used by insurers to carry out detailed investigations of complex and large losses. Although the insurers invariably pay the adjuster's fees and this may include variable remuneration based on total claims cost across a portfolio of claims with an insurer, and that the insured may not be entitled to review all of their recommendations to insurers, the loss adjuster is technically an impartial professional person. The suggested settlement should be within the terms of the policy and equitable to the insured and insurer.

Loss Assessor

In Motor insurance, the loss assessor is an engineer. In other classes of insurance, the loss assessor is a person who acts for the claimant in negotiating the claim. It is usually

only necessary to appoint a loss assessor when the loss adjuster recommendation is unacceptable to the insured. Loss assessors will help secure payments, fill out paperwork, and meet and negotiate with the insurance company's loss adjusters, and often earn a fee based on a percentage of the amount claimed.

Managing General Agent (MGA)

A Managing General Agent is a third party or broker who is vested with underwriting authority from an insurer within defined parameters, and thereby allowed to perform functions ordinarily handled by insurers such as binding coverage, underwriting and pricing, and settling claims.

Risk Engineer

A third party, broker or insurer team who surveys an insured's sites and/or operations, in order to assess an insured's risks and risk management, and provides improvement recommendations and site gradings as an input to the underwriting process.

Senior Management

A specific category of individual included in the Insurance Act 2015's definition of the duty of fair presentation of risk. The Act stipulates that material information known by these individuals must be included in risk presentations to insurers. Senior management is defined as those having a significant role in decisions about how a business is to be organised or managed. There may be value in a business seeking to define this for its own business as clearly as possible.

Third Party Administrator

A firm which provides administrative support services in the areas of claims administration, risk information, loss control, employee benefits programmes, etc. TPAs may be appointed in this capacity by either a policyholder or by an insurance company.

Underwriter

An insurance underwriter is a professional who evaluates and analyses the risks involved in insuring people and assets. Insurance underwriters establish pricing for accepted insurable risks.

A syndicate is a group of underwriters on the Lloyd's insurance market, consisting of active underwriters who arrange the business and non-working underwriters (also referred to as 'names') who stand surety for insurance claims that may arise.

Additional Service Providers

Many businesses supplement the support of their broker and insurer in specific areas with the services of additional specialist providers. The mix of support and providers depends on the priorities of the business, with significant variation across businesses. Below are descriptions of some of the areas commonly delivered by other service providers, with some providers working across several areas identified:

- Claims handling/Claims Resolution services – provided by Third Party Administrators, or specific divisions of brokers to handle the administration of high-volume claims. Separately, broader claims resolution services are available for larger and more complex claims which can involve advising on resolution strategy and managing the overall process of resolution with related third parties (lawyers, accountants, loss adjusters, technical experts, etc.)
- Loss control surveyors or risk engineers – conduct site visits to review risk exposures and risk management practices and controls to benefit all interested parties and provide recommendations to reduce risk. Some organisations prefer to 'owner control' this work as opposed to relying on insurers to arrange it
- Loss adjusters (insurer appointed) or loss assessors (appointed and remunerated by the insured) – investigate claims and advise on settlements, sometimes in situations where claims are disputed or an insured company prefers to have independent advice to stress test the work of adjusters appointed by the insurers
- Forensic accountants – can be insurer or insured-appointed, but tend to work to quantify and evidence losses suffered, with a particular focus on Business Interruption (and again some organisations may prefer to appoint their own specialists rather than rely on accountants appointed by the insurers)
- Property valuers – valuations on buildings, plant and equipment for inclusion in risk information presented to the insurers
- Disclosure specialists – providing specialist advice on the suitability of a business's disclosures and assisting in the compilation of risk submissions, etc.
- Legal advisers – advice ranging from pre-contractual support advising on policy terms through to litigation support in the event of a disputed loss
- Risk analysis or risk modelling specialists – assist with setting policy cover limits, both by investigating exposures and loss scenarios or through actuarial analysis of the insured's own and/or wider industry experience

- Policy wording expertise – from a variety of specialists analysing the detail of policy wording to ensure terms are optimum for the business, with the most comprehensive support including legal review and drafting of revised policy terms.

Alternative Structures and Insurance Markets

Alternative Risk Transfer

A catch-all term for various methods and structures that allow companies to purchase insurance coverage and transfer risk outside of the traditional commercial insurance market, including captives, virtual captives, and the use of capital market funding to spread or part-fund the cost of insurable events.

Captive

An insurance company that is owned and controlled by the business it is insuring. The primary purpose of the captive is to insure this business's risk. The business benefits from the captive's underwriting profits and may have a greater degree of control over its insurance. Captives are commonly operated by larger businesses.

Lloyd's of London

The policyholder can be businesses, organisations, other insurers and individuals from around the world looking to mitigate the impact of potential risks. The local broker is the first contact for a policyholder. They work in the local market where the policyholder is based. They assess the policyholder's needs and decide if it's suitable for the Lloyd's market. The Lloyd's broker works on the policyholder's behalf, negotiating with underwriters to create a tailored policy to insure the risk. The underwriter works with other specialist underwriters and the Lloyd's broker to draw up the policy. Each underwriter will decide on the price and terms they are willing to take. Underwriters group together to form a syndicate to write insurance at Lloyd's. Each syndicate is given a number by Lloyd's to identify it. The managing agents are a company set up to manage one or more syndicates. Managing agents are responsible for employing the underwriters. The Corporation of Lloyd's oversees and supports the Lloyd's market, ensuring it operates efficiently and retains its reputation.

Loss Portfolio Transfer/Adverse Development Cover

An insurance-backed product to reduce or remove cost uncertainty within, e.g. a basket of known litigation or claims where future actual costs are covered by the third party in return for a fixed-cost premium. This can, for example, be used to create certainty around historic liabilities to support M&A activity to buy/sell a business or division.

Finite Reinsurance / Structured Finance

A long-term funding structure agreed with capital markets partner(s) to smooth costs of given events over time to reduce uncertainty. Such deals can vary widely in terms of how much risk is transferred as opposed to simply providing a smoothing mechanism, with the organisation itself paying the actual costs.

Parametric Insurance

Parametric insurance covers the probability of a predefined event happening, instead of indemnifying actual losses incurred. The insurance cover is triggered if predefined event parameters are met or exceeded, with a pre-agreed payout provided if the parameter threshold is reached or exceeded. For example, having reviewed weather data, an insurer might agree to pay a defined amount to an insured in the event of a pre-defined amount of rain falling, regardless of whether any damage to the insured's property takes place. Whilst typically available only for clearly measurable, objective triggers, such policies have the advantage of being relatively simple and subject to few conditions.

Reinsurance

Insurance that is purchased by an insurance company, whereby the primary insurer lays off or 'cedes' part of its risk in return for a premium. It relates either to an individual risk exposure ('facultative' reinsurance) or to an insurer's portfolio of risks ('treaty' reinsurance).

Virtual Captive

A virtual captive is a multi-year insurance agreement that emulates the mechanics of a traditional captive; however, the insureds' self-financed, self-insured retention is held on an insurance company's balance sheet. A virtual captive thereby keeps the mechanics of a traditional captive, without the cost and regulatory complexity of setting one up.

Wholesale/Retail/Specialty Insurance

These terms relate to parts of the insurance market. 'Specialty' insurance may mean slightly different things to different firms but provides cover for unusual or difficult insurance needs and for higher risk accounts (and may include insurance such as Directors' & Officer's or Cyber Liability). 'Retail' insurance is the normal model whereby a organisation buys insurance (through a broker) from a licensed insurer, usually in the same territory as the organisation's headquarters. 'Wholesale' insurance brokers provide a specialist role as a further middleman between a retail broker and wider carriers which could be based overseas or not be licensed to write direct retail business in

the territory concerned. This model is sometimes used for high-risk areas where many insurers' risk appetites are limited, such as pharmaceutical product liability or environmental risks.

Insurance Policies and Covers:**Additional Increased Cost Of Working (AICOW)**

A common extension to Business Interruption policies, AICOW cover typically allows the insured to incur further reasonable additional expenditure (beyond what would be covered by ICOW alone) in order to continue operations or, more broadly, to limit disruption to the business and including measures which may be uneconomic (i.e. costing more than they directly save) to support reasonable wider business objectives.

All Risks

Term used to describe insurance against loss of or damage to property arising from any fortuitous cause except those that are specifically excluded from the policy.

Business Interruption

Cover for loss of revenue/profits typically triggered by damage to physical assets used by but not necessarily owned by the insured, resulting from events including fire, storm or machinery breakdown.

Contractors All Risk Insurance

A form of insurance designed to cover work carried out by contractors whilst undertaking construction projects, including cover for contract works, plant and machinery, public liability and employers' liability. This can be bought on an annualised or project-by-project basis.

Cyber Insurance

A form of cover designed to protect the insured from threats relating to its electronic exposures, such as data breaches or malicious cyber hacks on its computer systems. Most policies cover both first-party and third-party losses. Cover for first-party losses usually includes cover for cybercrime investigations, data recovery, reputation management, notification costs and extortion payments. Cover for third-party losses usually includes damages and settlements, and defence costs for claims of a GDPR breach.

Difference In Conditions/Difference In Limits (DIC/DIL)

Difference in Limits (DIL) insurance provides cover in excess of other, usually local policies, which the insured has purchased and which may have lower limits. Where

Difference in Conditions cover (DIC) applies, this would also mean that the cover will come into effect where the underlying policy would not provide cover due to application of narrower policy terms and conditions.

Directors' and Officers' Liability Insurance

Directors' and officers' liability insurance covers the cost of compensation claims made against a business's directors and key managers (officers) for alleged wrongful acts. Directors' and Officers' insurance typically comprises three separate agreements, called Side A, Side B and Side C.

Side A covers claims against directors and officers not indemnified by the organisation. Side B provides reimbursement for indemnifying directors and officers. Side C provides coverage for securities claims – claims which often allege breaches of disclosure or fiduciary duties, or misleading conduct that results in a loss of market value of the organisation's shares.

Employers' Liability Insurance

Insurance by employers in respect of their liability to employees for injury or disease arising out of and in the course of their employment. With some exemptions, this insurance is compulsory in Great Britain and can only be provided by an authorised insurer regulated by the FSA.

Increased Cost Of Working (ICOW)

Under a Business Interruption policy, some additional cover is provided for expenditure incurred by the insured in order to prevent a reduction in turnover following an insured event. This would normally need to be 'economic', i.e. to cost less than it saves.

Key Person Insurance

Cover that pays out expenses in the event of the death or critical illness of an individual upon whom a business relies heavily.

Permanent Health Insurance

Term used to describe contracts of insurance providing continuing benefits in the event of prolonged illness or disability.

Personal Accident and Sickness Insurance

Insurance for fixed benefits in the event of death or loss of limbs or sight by accident and/or disablement by accident sickness. Accident and sickness may be insured together or separately.

Pension Trustee Liability

A form of insurance that provides cover and expenses for pension fund trustees' personal liabilities for breach of trust in connection with their role.

Product Liability Insurance

These policies cover the insured's legal liability for bodily injury to persons, or loss of or damage to property caused by defects in goods (including containers) sold, supplied (including as gifts), erected, installed, repaired, treated, manufactured and/or tested by the insured.

Professional Indemnity (PI) Insurance

This policy protects a professional person or organisation against legal liability towards third parties for injury, loss or damage arising from that party's own professional negligence or the negligence of their employees. For many modern businesses, the line between 'products' and 'services' is increasingly blurred, and therefore more and more businesses (beyond traditional advisory firms such as lawyers or architects) may need PI cover.

Property Damage Insurance

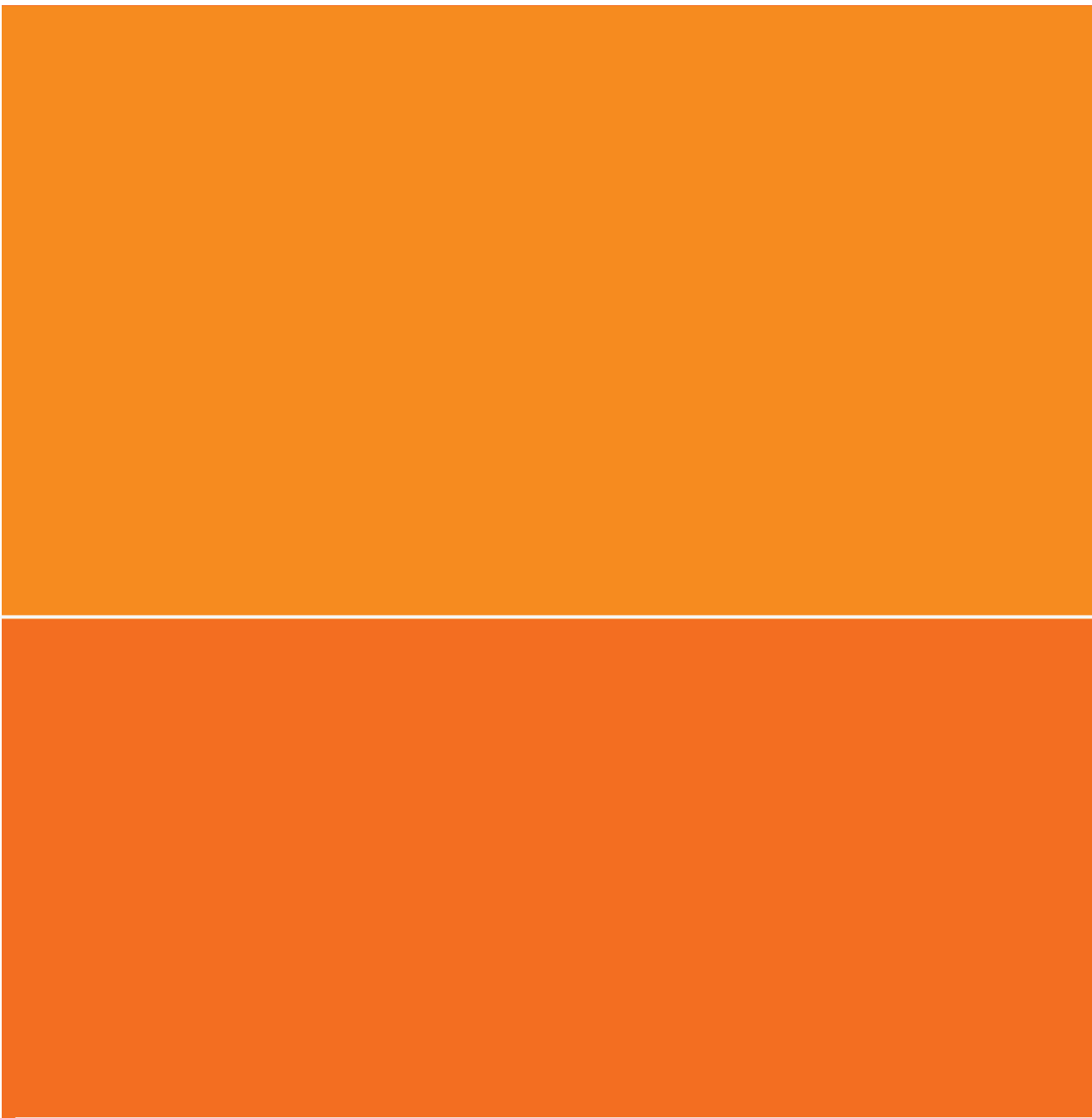
This policy provides cover for accidental loss, or destruction of, or damage to insured property and necessary costs of reinstatement.

Public Liability Insurance

These policies cover the insured's legal liability for death, injury or damage to a member of the public or other business. It is typically combined with Product Liability cover into a single policy

Terrorism Insurance

These policies cover loss, destruction of or damage to insured property resulting from a terrorist incident. Cover is purchased through the Pool Re scheme, which is backed by the UK Government.



This guide is part of the EXPLAINED series of Airmic Guides:
www.airmic.com/technical/library

airmic

EXPLAINED

GUIDES

Airmic
Marlow House
1a Lloyd's Avenue
London
EC3N 3AA

Tel: +44 207 680 3088
Fax: +44 207 702 3752
Email: enquiries@airmic.com
Web: www.airmic.com

Mactavish
22a St James square
London
SW1Y 4JH

Tel: +44 207 046 7956
Email: mail@mactavishgroup.com
Web: www.mactavishgroup.com

