



RISK ENGINEERING AND THE UMA: AN EFFECTIVE MECHANISM TO MITIGATE RISK

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One of the advantages of dealing with a UMA is that it is normally focused on a specific line of business and offers both specialised underwriting skills and risk management expertise. UMAs are, therefore, ideally positioned to provide specialist insurance solutions in niche insurance markets, providing a single point of access for underwriting, risk management and claims expertise.

The inclusion of a specialised risk engineering team within any UMA is an additional advantage. Risk engineers typically have experience in fire safety and approval of building plans. To balance a risk engineering team focused on the corporate market segment, the inclusion of engineers who have worked and consulted to chemical, petrochemical and mining companies is a significant advantage. This ranges from fire prevention to assisting with reliability and preventative maintenance plans to prevent machinery breakdowns.

The provision of risk management services to industrial and mining clients is gaining in importance both from a health and safety perspective as well as from a loss-prevention point of view. Shareholders and analysts alike display increasing concerns if quarterly and annual production targets are not met. Safety induced work stoppages and lost production owing to damaged process plant lead to volatile share prices and fluctuating company valuations. In the South African mining industry, the link between health and safety, effective risk management and consistent production results has probably never been more apparent than at present. Companies with successful risk management programmes

and effective health and safety initiatives will be rewarded by the market for sustainable results.

This presents a unique opportunity for companies that actively engage in risk management and include it as part of the brief to design and consulting engineers.

One of the concerns following the global recession of 2009 is that some companies have resorted to harsh cost reduction measures such as the retrenchment of experienced staff, curtailing of projects and even elimination of maintenance expenditure. Companies which have continued expansion on high-value projects and have invested in people and productive assets will present a lower risk profile and will be able to take advantage of the upswing in both the South African and the global economy.

Recently, some reinsurers that were previously domiciled in South Africa have shifted their operations offshore to streamline operations and contain costs. This means that centres of reinsurance expertise are not directly available to local insurers. It has been reported that five out of eight South African reinsurers have not been able to show an underwriting profit for 2009.

The dual effect on primary insurers and UMAs would be that reinsurance capacity for specific and referral risks would be more difficult to obtain and more costly. In the absence of a direct local relationship with reinsurers, the transaction would be subject to scrutiny by overseas reinsurers (or a review panel of reinsurers). This normally results in stricter terms and higher pricing, especially for mining risks following excessive mining industry losses in 2008.

The hurdle for risk acceptance by overseas-based reinsurers is generally greater. The response by the insured in implementing risk recommendations is key to securing reinsurance support, particularly for so-called special risks. Whilst a UMA may still find it difficult to obtain reinsurance support for a company with an inherent high-risk profile, it could well be accepted if the insured has implemented the required improvements as part of overall risk management.

This is especially true for corporate risks where underwriters look at specific accounts on an individual basis given the increase in frequency and severity of corporate losses in 2008 and 2009. Risk management in this sector in particular has deteriorated over the past several years. This trend needs to reverse to restore underwriting flexibility and a more favourable rating of corporate risks. Innovative product solutions are needed and can include the insured bearing a greater portion of the risk through a self-retention mechanism.

The adoption of an enterprise-wide risk management programme including business continuity plans (BCP) is essential to the long-term success of any company. Whilst certain loss scenarios are not foreseeable, the manner in which the company responds will be crucial to its continued success. Not many companies that have been hit by disaster have recovered without major inconvenience or disruption to their clients. There are few examples of BCPs being so successful that disruption is only a matter of hours following fire losses involving key installations. The good news is that UMAs can now add value to clients through risk transfer and risk engineering.