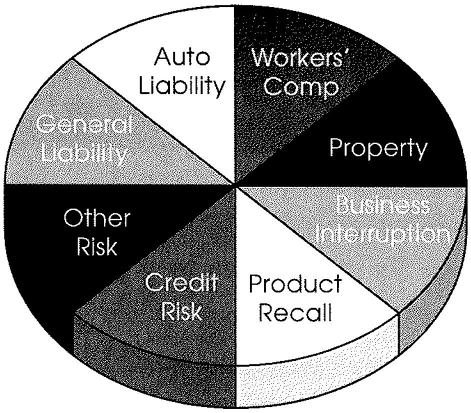
ROUTE TO:

THE RHA REVIEW

Vol. 4, No. 3, Second Quarter 1998

A publication of Robert Hughes Associates, Inc., an international litigation support, actuarial, risk management and insurance consulting company.



RISK MANAGEMENT GIVES NEW MEANING TO INTEGRATION

By Donald W. Bendure, CPCU, ARM

I recently attended a gathering of industry visionaries to try to comprehend what the risk management community has done with regard to its newest brainchild — Integrated Risk Management (IRM). What I learned was that the world in which many risk managers live has been redefined to include ALL aspects of business risk, not just fortuitous risk to property and persons. Credit risk, financial exchange risk, price commodity risk, and any other risk you can quantify that would affect the organization's income stream are now considered to be within the risk manager's purview. The new buzz phrase for risk managers is "risk mapping" and includes every department and aspect of the organization. IRM has evolved out of traditional risk management because of the realization that all risk affects financial performance and should have a common point of assessment and control. This conclusion puts the risk manager in the position of being a partner for new thinking across all disciplines of the business.

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IRM forces the largest shift in thinking for insurance companies since the package policy was developed in the early seventies. It is the largest opportunity for reinventing the risk management discipline since its birth. This concept is not new. It has been bandied about for at least three years as an intriguing concept but with few players from the insurance community expressing serious interest. Now it is clear that the concept has completed its gestation period and has been born. Several integrated risk deals were born last year, each with its own characteristic footprint. I expected to find that most, if not all, of the deals struck would involve programs worth millions in traditional premium. But surprisingly, one beautifully designed program involved an expiring total premium of well under $1,000,000. This program has proven that IRM is not just for the *Fortune* big boys.

So what's all the fuss about? Remember when basket aggregates were the rage? Insureds could include two or more lines of coverage in their aggregate retention, but they were generally limited to general liability, auto liability and workers' compensation. Now the IRM models incorporate basket occurrence limits *and* basket aggregates. To sweeten

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the pot just a little, let's envision including not only general liability, auto liability and workers' compensation, but also property, business interruption, product recall, credit risk and possibly other risks pertinent to the organization. Why would we want to include all of these lines in a single retention when the insurance market is as cheap as it is and insurance coverages are as available as ever?

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Organizations have come to realize that risk is risk, no matter what label is placed on it. All risk carries either realized cost or opportunity cost which is paid with the same dollars that come from the coffers of the company. Why are some companies willing to risk millions of dollars on business joint ventures yet routinely purchase liability deductibles at a fraction of the cost of the joint venture? Is it rational to have such dissimilar levels of risk tolerance for the organization as a whole? Once the risk manager has mapped the risk exposures and tolerance for the organization, he or she functions as the "chief risk officer" and coordinates the treatment of the overall risk at substantial cost savings to the organization.

But costs alone are not the motivating factors in developing an IRM model for the organization. Many insureds are realizing that this insurance market cannot remain as soft as it is for very long, and relationships need to be established with the insurance markets for the long term. With a closer relationship, the IRM can be designed over multiple years in order to stabilize the predictability of the model. The result of this effort is what is known as a MultiYear, MultiLine (MYML) product. It has the potential to provide lower cost of risk transfer, higher capacity, broader coverage, and simplified administration and also to create long-term partnerships with all vendors.

Would most insureds like to eliminate the annual mating dance between their insurance department and their broker, which takes weeks, sometimes months? Absolutely. Insurance coverage within an MYML program doesn't require collecting and remarketing the same data year after year. The time saved can be used to identify, measure and implement new areas of risk control rather than renewing insurance policies. It has been estimated that 30 percent or more of total risk management man-hours can be saved by eliminating the annual renewal process and converting to a multiyear program.

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Will everyone have an integrated risk management program? Probably not. IRM is a process, not just an insurance product. It has been said that IRM is a solution looking for a problem. Many of us will spend the next several years designing solutions to problems that will include IRM. But IRM involves a considerable commitment from upper management in time and resources for consensus building and a change from traditional risk management thinking. Interdepartmental processes must be understood within the context of both risk control and risk financing. The facilitator of this process must gain a considerable amount of buy-in from each of the departments within the company in order to have a clear understanding of the risk to the organization. In some cases, this buy-in involves relinquishing total control over the measurement, evaluation, and control of certain risk factors within the organization.

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Does integrated risk management have risks? Absolutely. If being highly visible or being considered an innovator carries organizational risk, then IRM may not be the ticket for some organizations. It can also strain existing broker relationships if there is not a perceived need on the broker's part. There are many areas for surprises, because any time something this new is attempted, there will be problems not previously considered. There must be a compelling reason to invest the time and effort necessary for a successful IRM program. Without clear objectives

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with a goal to satisfy specific needs, there will be no compelling reason to see the process through.

IRM is in the infancy stage, and currently there is no one policy language that can encompass the various coverages over long periods of time. Stapling forms together has been the *modus operandi* for many programs, with a master declarations page and integration wording to govern the various forms. How this master wording operates will be the deciding factor in how coverage operates and interacts with the various coverage parts. One of the shifts in thinking that must take place is the shift from "occurrence" thinking to "event" thinking, with all of its attendant potholes. We will now have to start developing precedents in "event" coverage. These may be slow in coming at first, but the momentum will pick up significantly with time.

So what's a company to do? An ever-increasing number of companies, both large and not so large, will be inquiring into the benefits and problems of integrated risk management sooner than later. Those of us involved with coverage issues would be well advised to learn as soon as possible what IRM can do and what it cannot do. There will be ample opportunity for those who want to innovate to participate in this movement over the next year. Already, major insurers and reinsurers are establishing departments to specialize in IRM. Whether under the guise of "new markets" or "global risk management," the goal is the same: to expand into the new generation of risk management and insurance.

Donald W. Bendure is an associate consultant with Robert Hughes Associates, Inc., who has extensive experience as an underwriting manager for umbrella and excess liability lines. He is also experienced in contract wording, product development, coverage enhancements and treaty issues.

FROM NEAR & FAR

Heavy rain and unseasonably cold weather caused a series of floods throughout the British Isles over the Easter holiday. Insured losses are expected to exceed $800 million. The East Midlands were hardest hit when the River Nene burst its banks in the city of Northampton.

Elton Bomer, insurance commissioner for the State of Texas, announced that he has expanded the mandatory 10 percent driver's education discount to include teenagers who are taught by their parents. The parents must follow a Texas Department of Public Safety-approved course.

Also in Texas, Bomer approved a change to standard homeowners' insurance that will allow certain insurance companies to sell cheaper policies that offer less protection for hail-damaged roofs in the Dallas/Fort Worth Metroplex. This change follows the decision by a number of insurers to stop writing homeowners' coverage in DFW and some surrounding counties. The high cost of constantly replacing or repairing hail-damaged roofs has driven the cost of homeowners' insurance to all-time highs.

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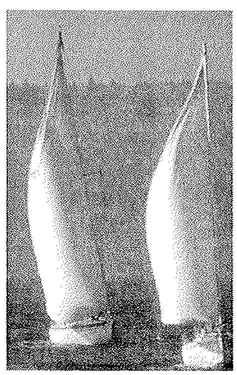
Retreating on Lake Texoma



On May 1–3, Robert Hughes Associates held its inaugural litigation support retreat/conference at the Tanglewood Resort Hotel & Conference Center on the banks of Lake Texoma in Pottsboro, Texas. All of RHA's testifying consultants and spouses were invited to attend, and most made it, including John Bogart from Palm Springs, California, and Dr. Tim Ryles from Newborn, Georgia. Unfortunately, Mike Jackson did not make it from London, and Dr. Joseph Launie did not make it from Santa Barbara, California.

The festivities kicked off on Friday, May 1, with a Mexican fiesta at Bob Hughes' house in Dallas. At first light on Saturday morning, the gathering moved from Dallas to Tanglewood, where the serious business of idea sharing began. Following a full day of discussions for the consultants and antiquing for the spouses, the group boarded Cap'n Buddy Greer's *Yacht 'O' Fun* for a two-hour cruise on Lake Texoma. An evening of fun continued with an Italian supper.

Not so bright and early on Sunday, Bob Hughes took a group aboard his boat, *Bon Temps,* for a relaxing sail around Lake Texoma. The landlubbers among us opted for the golf course, where our resident pro, Tom Wilkins, took all of our money.

A good time was had by all, and we hope to do it all again in the not-so-distant future. RHA

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Publisher .... Robert N. Hughes
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Assistant Editor .... Alice H. Oakley

The RHA Review is published quarterly by Robert Hughes Associates, Inc. — an independent international litigation support, actuarial, risk management and insurance consulting company based in Dallas, Texas, with offices in Houston, Texas, and London, England. The purpose of this publication is to offer insurance-related information and critical comment pertinent to the clients, friends and fellow professionals of Robert Hughes Associates, Inc. This publication is available free to interested parties. The information contained in this publication is intended to be general in nature; readers should obtain professional counsel before taking any action on the basis of this material.

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