MARSH

ISSUE 2, 2013

ASIA DIRECTORS' SERIES

AN IN-DEPTH LOOK AT MANAGING SPECIALTY INSURANCE CLAIMS

LEADERSHIP, KNOWLEDGE, SOLUTIONS...WORLDWIDE.

MARSH & McLENNAN COMPANIES

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PUBLISHER’S NOTE

Welcome to Marsh’s second Asia Directors’ Series publication for 2013.

The ripple effects from a major event are amplified today more than ever before, as interconnected supply chains create greater levels of business dependencies and financial exposures. In Asia-Pacific, we have seen many examples where major events have created debilitating knock-on effects, including the Japan earthquake and subsequent tsunami in 2011 and the Thailand floods in 2012. Further afield, civil unrest in the Middle East and North Africa is also causing businesses with interests in those areas to look at risk management and resiliency plans for their assets and investments.

Navigating the claims process once an event happens can be daunting and complex. For this reason, we have dedicated this issue of the Asia Directors’ Series to providing insights and guidance when managing specialty insurance claims. Specifically, we take an in-depth look at three areas that can be particularly complex, including:

- Business interruption.
- Trade credit.
- Political risk.

In our experience, these classes of insurance in particular can present numerous challenges for businesses when trying to recover from a loss.

As a company executive, your number one priority is to get your business and cash flow back to pre-event conditions. We hope that this publication demystifies the claims process and provides you with practical knowledge to manage a claims process with confidence. If you have any questions, Marsh’s dedicated claims professionals across the region and around the world stand ready to help with your specific needs.

Martin South
CEO, Asia-Pacific


Strategy
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ance
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BUSINESS INTERRUPTION CLAIMS:

BOUNCING BACK FROM A MAJOR DISRUPTION

Asia's innovative supply chain strategies are boosting capacity, cost competitiveness, and speed to market, creating a lean, fast moving, and constantly evolving flow of global trade. This means businesses are becoming more reliant than ever on the interdependence of multiple supply chains, increasing their vulnerability to the impact of a disruptive event.

As disruption becomes an assumed operating reality, C-suite executives are paying greater attention to their ability to bounce back quickly in the face of the next big event.

Calculating the cost of business interruption and assigning appropriate insurance is a vital step in managing the risk. Yet, equally important and often overlooked is a complementary post-loss strategy to manage and expedite claims. Without this, recovery may be unnecessarily delayed.

DISRUPTION CAN DESTROY

Fires, storms, floods, machinery breakdowns, power outages, and product recalls are just some of the events that have the capacity to severely interrupt an organisation's ability to trade, putting it at risk of significant financial loss and potential failure.

It is common for businesses to insure their assets to help reduce the financial hardship of repairs or replacement if damage should occur. However, it is sometimes overlooked that those same assets produce income that, if not insured, can cause crippling losses and additional costs after a disruptive event.

Protection against this loss, in the form of business interruption insurance, can mean the difference between post-loss recovery and significant long-term financial hardship and, in worst cases, closure.

INSURE AGAINST THE INTERRUPTION

Business interruption insurance is designed to put a business back in the same position it would have been had the damage caused by an insured event not taken place.

It typically covers the profits that would have been earned as well as the operating expenses and other costs still being incurred by the business while out of action. Properly arranged, policies also cover the extra expenses for moving to, and operating from, a temporary location and reimbursement for reasonable expenses that allow the business to continue operation while property is being repaired.

Depending on the nature and complexity of a business, some also find significant value in *contingent business interruption insurance*, which reimburses lost profits and ongoing costs resulting from an interruption of business at the premises of a customer or supplier, or *supply chain insurance* products.

A BUSINESS'S RESPONSE CAN AFFECT INSURANCE RECOVERY

The way an organisation responds to a major loss may critically impact the success of a business interruption insurance claim.

Every hour spent on managing or resolving a claim issue or contesting a dispute is an hour that could otherwise be spent on managing the immediate continuity of the business, recovery, or communicating with clients and other stakeholders.

At a time when the business interruption has reduced sales and increased costs, a slow progress payment or understated settlement will only further reduce vital cash flow.

To ensure the most efficient claim response, key factors that businesses should consider are outlined below.

GET YOUR COVER AND APPROACH RIGHT, UP FRONT

As with all insurance products, initial analysis and calculation of a business's particular circumstances will determine the optimal insurance solution, including the level and scope of coverage.

The aim at this stage is to avoid insufficient coverage (underinsurance), wasted premiums, or redundant capacity and determine those actions that would minimise losses should a disruptive event occur. Careful supply chain mapping is important to ensure clarity around which suppliers are named in the policy or otherwise, and how they are ranked. By quantifying the business impact of potential actions, a business can also firm up its decision-making process – including its approach to the claims lodgement process – for when the need arises.

This process can be complex depending on the nature and size of an organisation. Independent advice from an insurance broker with business interruption specialists can often give confidence that the calculation and approach is the most appropriate for a business. Marsh's Forensic Accounting and Claims Services team has extensive experience in this area and can work with a business to undertake a pre-loss review. *Read more about this in the break-out box.*

WHO WILL LOOK AFTER YOUR INTERESTS?

When a business interruption claim is made, the insurer will arrange a team of specialists to analyse the claim, with members of the team selected to match the size and complexity of the business and the claim. Headed by a loss adjuster, the team is likely to include other experts such as engineers, forensic accountants and, potentially, legal advisors. Analysis will include a review of any related issues, including the business's premises, production, sales and marketing, advertising, and accounting.

Many business owners are not aware that they, too, will be obliged to prepare and present their claim to the insurer and be ready to support their business's respective position. To do so, it can be valuable for the insured business to appoint its own team of specialists, including a forensic accountant and claims specialist, to ensure its position is most effectively presented.

A forensic accountant can expedite the claims process by bringing experience in reviewing production and sales and the more technical aspects of accounting, as well as the ability to translate the policyholder's operating results and other financial records to conform to its business interruption insurance policy coverage. Correctly arranged, the policy will cover reasonable expenses in doing this.

Appointing specialists will also allow the business to concentrate on recovery and rebuilding, rather than tying up senior resources on documenting and negotiating claims with third parties, including insurers.

PREPARING THE CLAIM

Although the process can often be complex, careful engineering and project management of a claim can help to swiftly secure cash flow and aid post-loss recovery.

The process involves preserving and recovering evidence and investigating all aspects of the loss, including discussing operations and markets with various parts of the business to measure economic damages and support the claim. It is important to present the most relevant data and evidence in a way that will mount the strongest argument. It is equally important to omit information that may either confuse or not directly support the claim. An insurance broker with a recognised specialist claims team can advise on the most appropriate way to present a claim to achieve the most effective response.

IMMEDIATE WORKING CAPITAL DURING THE CLAIM PROCESS

If there is a pressing need, most insurers will respond to a well-documented case to provide policyholders with an advance payment to cover the immediate costs necessary to allow the business to continue operation while the recovery and claim process is underway.

QUANTIFYING THE IMPACT FOLLOWING A LOSS EVENT

Calculating the quantum of an interruption to business basically involves projecting what the income and ongoing costs expectations would have been had an event not occurred. These projections can be calculated in many different ways and often require an intricate process involving a detailed understanding of a business, including production flow and capacity, the market for affected products, and both financial and management accounting. An essential additional element is a detailed understanding of the policy and the rights and obligations of the insured so that early decisions can be made.

The key elements in determining the estimated quantum of the loss are:

- **Estimated duration:** The time over which the loss will be measured. This is often referred to as the Indemnity Period. The calculation takes into consideration the time that the direct physical damage occurred and an estimate of the time it will take to repair, rebuild, or replace the damaged property and to resume normal business operations. The calculation of this time may not be immediately obvious and can involve detailed analysis and subsequent discussion with an insurer's appointed specialist.

- **Estimated sales:** The projected sales that would have occurred throughout the duration of the interruption, taking into consideration the impact of recently signed contracts, the competitive environment, changes in the business's operating capacity, and seasonal or long-term sales trends.

- **Estimated expenses:** The projected expenses and costs, segregated into fixed, variable and a combination of both. Fixed costs, which may vary between businesses even in the same industry, are considered as continuing costs, and may include marketing, power, maintenance costs, rent, and other contractual obligations. Variable costs are the non-continuing expenses which generally fluctuate depending on the volume of goods manufactured or services delivered, such as raw materials, shipping, and bad debts.

Once these factors are determined, in a simple scenario, the business interruption loss is the difference between the expected revenue and expenses, and the actual revenue and expenses during the period the business is impacted by the loss.

As the calculation comprises many components, some of which are objective while others are more subjective, differences can arise between the estimations of the insured and the insurer. These will need to be discussed, analysed, and various views supported and, finally, negotiated. An independent, pre-loss review can be a valuable way to reduce the likelihood of these differences from arising.

TIME IS OF THE ESSENCE

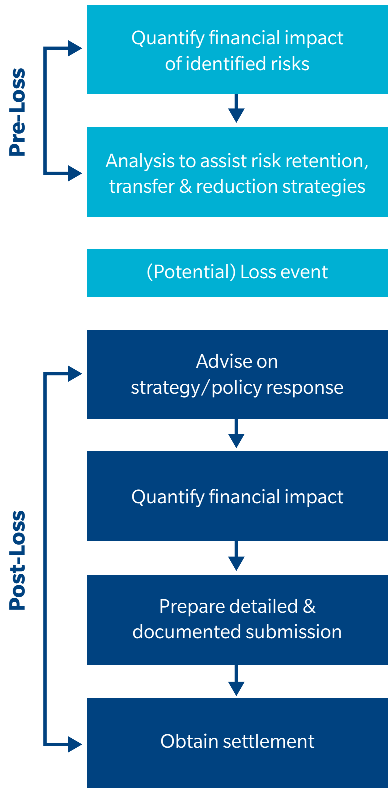
A claim should be prepared and lodged as soon as possible following the loss. Delays in lodgement can affect the claim process as evidence may need to be regathered and analysed depending on the time that has lapsed.

REVIEW YOUR STRATEGY TODAY

Properly structured business interruption coverage can provide the critical working capital needed for a business to survive a major disruption. It can be the difference between a business being able to rebuild and recover and maintain relationships with its suppliers and customers, or being severely impacted and, at worst, shutting down completely.

While it is important to ensure that the most appropriate level of cover is established, it is equally important for businesses to have a post-loss claims strategy supported by independent experts to ensure the most effective response from a business interruption policy. This will allow a business to concentrate on recovery and rebuilding, rather than negotiating paperwork with insurers.

MAJOR STEPS TO ENSURE EFFECTIVE BUSINESS INTERRUPTION INSURANCE RECOVERY



PRE-EVENT PREPARATION PAYS

Determining the insurable value for loss of income can be a difficult and intricate process. A pre-loss review, which can be conducted by Marsh's Forensic Accounting and Claims Services (FACS) team, can help a business to understand and assess business interruption risks and identify appropriate levels of coverage, support the insurance placement process, and maximise financial stability.

Various options may be available to support the funding of such a review which can be discussed with, and negotiated by, the FACS team.

During the review, scenarios developed by a risk engineer will be analysed to understand the possible outcomes of various disruptions, including the financial implications, and assess the effectiveness of mitigation measures across a business's entire supply chain.

Through a combination of management and financial accounting and risk management techniques, the drivers of a business's performance will be analysed to ensure a deep understanding of its fixed and variable costs to inform the business interruption calculation.

Undertaking a pre-loss review can help to better prepare a business for unforeseen incidents and to even gain competitive advantage should the unexpected occur, while also avoiding unnecessary premiums.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69.24
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1494.88
PAYMENT DUE
ANNUAL
PERCENTAGE
RATE
PAST DUE

TRADE CREDIT CLAIMS:

GETTING PAID WHEN YOUR CUSTOMERS WON'T PAY

The outlook for Asia's vast legions of suppliers is optimistic, with economic growth and higher volumes of intra-Asian trade in the coming year predicted by many economists.

However, operating in an increasingly competitive supply environment, the fight for market share has seen many suppliers accepting credit risk from a wider variety of customers, both international and intra-regional. For many of these businesses, establishing robust credit risk governance procedures and adequate insurance solutions to avoid the risk of buyer default is quickly becoming a priority.

As part of their approach, companies throughout Asia are increasingly turning to trade credit insurance. To get the most out of a trade credit insurance policy, it is important to have a deep understanding of the policy triggers.

MORE THAN SIMPLY INSURANCE PROTECTION

A trading partner's payments – and the terms on which they transact – are critical for a supplier's cash flow. Trade credit insurance is available to help protect suppliers in the event that a trading partner does not pay for the goods or services they've received. Yet trade credit insurance offers much more than a simple risk transfer mechanism. It can also be an instrumental aspect of a company's business development strategy:

Supports business expansion: Having trade credit insurance gives businesses confidence to extend more credit to creditworthy customers while reducing the risk of non-payment, thereby promoting safe sales expansion.

Avoids letters of credit: Insured suppliers can offer unsecured payment terms without taking on increased risk, so buyers can avoid the need for costly letters of credit or bank guarantees.

Favourable financing terms: Insured businesses have better chances of bank financing through increased borrowing capacity.

Balance sheet protection: A sudden accumulation of debts that disrupts the financial structure of your company can be avoided. Credit insurance may replace loss provisions.

Access to credit experts: Trade credit insurance provides access to professional credit analysts who can provide a second opinion for the company's credit risk management framework.

WHAT IS AND IS NOT PROTECTED?

Trade credit insurers offer standard policies, or they may customise a policy to suit an organisation depending on the trade to be insured or the particular needs of the business. A trade credit insurer will always carefully investigate an organisation's circumstances to ensure the most appropriate solution is offered.

The policy terms and approaches of the major trade credit insurers vary. Securing the right policy terms and understanding what is included and excluded from the cover are essential to ensure the policy will respond well when it is needed. Specialist, impartial advice can be sought from an insurance broker.

In general terms, trade credit risk insurance protects against losses related to a buyer's failure to pay owing to financial difficulties or bankruptcy. It covers payments related to trade in goods or services between companies (not individuals) and can cover up to 90% of the loss.

Foreign exchange transfer risk is generally covered, providing protection against a buyer's inability to make payment in the contracted currency due to the imposition of local currency controls. Some political risks, such as import/export license cancellation or embargo, can be included. It can also protect against domestic insolvencies or mitigate the risk of a client failing to pay.

Trade credit policies can be structured on a single- or multiple-buyer basis, covering domestic sales, foreign sales, or all sales combined. Most insure short-term trade receivables (usually regarded as a maximum of 180 days although longer terms may be agreed) and are structured on a multiple-buyer format, insuring a broad spectrum of risk.

Credit insurers will cover not only manufacturers but traders, financing banks, factors and service providers such as advertising agents, travel agents, consultants, and engineers. In addition, loans directly linked to the supply of goods may be covered. Policies do not cover financial obligations unrelated to trade, loans with no underlying related trade contract (for example mortgages), commercial disputes or contract default by the insured, or the insured's failure to obtain the appropriate import, export, or foreign exchange authorisation.

It is important to understand and be comfortable with any exclusions in the policy. These will vary from insurer to insurer. Typical factors that are excluded from cover are disputes, illegal contracts, and failure to comply with a country's import and export regulations. An insurance broker may challenge or negotiate exclusions on behalf of the policyholder as necessary.

UNDERSTANDING TRADE CREDIT POLICY TRIGGERS

While securing the right cover is important, equally critical is an intimate understanding of the insurer's compliance requirements and the steps to be taken if a claim is filed. While all legitimate claims will be paid, an organisation's failure to comply with the terms of the policy may compromise a claim.

A "LIVING" DOCUMENT – KEEP YOUR INSURER INFORMED

A credit insurance policy is a "living" document. It should evolve to reflect the major changes in the insured organisation's business, as they happen. For example, an organisation's policy should be updated if:

- Turnover significantly increases by attracting more buyers, selling more products, or distributing in more countries.
- Agreements with distributors are cancelled.
- Different contractual terms are introduced for deliveries or payments.
- Changes to the business model are introduced, such as new manufacturing processes, alternative delivery patterns, or more aggressive sales techniques.
- Major changes in the global and regional economies are experienced.

It is important to keep the insurer as fully informed as possible to enable a prompt decision to be made at the appropriate time when a claim is made.

In addition, an insured must regularly report sales to the insurer within the time specified in the policy (usually 15 days after the end of each quarter).

PRUDENCE REMAINS NECESSARY

Trade credit insurance does not replace the need for the insured to act prudently and have firmly embedded credit risk governance processes. An insurer will expect an organisation to take all reasonable steps to avoid or minimise loss and to act in accordance with the policy.

Acting to minimise losses also benefits the policy conditions for future renewals and coverage on marginal buyers.

AVOID EXCEEDING CREDIT LIMITS

The insured should fix a credit limit on every buyer. The smaller limits can be set by the insured using internal credit management procedures, while larger limits will be underwritten by the credit insurer. The insurer will usually set limits based on available financial information but will also work in conjunction with the client's credit management team. The credit limit is the maximum insured credit line for a specific buyer, and the policyholders can trade on an insured basis within the approved credit limit. The amount of the limit depends on the creditworthiness of the respective customer. It is the insured's responsibility to comply with credit limit requirements such as obtaining valid guarantees of payment.

If the insured organisation's trade with a customer exceeds the credit limit, it is important to notify the insurer and obtain an increased limit.

WHEN TO NOTIFY INSURERS

When credit insurance is initially negotiated, the insurer will set the maximum credit terms within which the insured can work. These will usually reflect normal trading terms of the business. In addition, the insured has the freedom to extend the due date, within an agreed period and without seeking approval from the insurer. This would typically be no more than 60 days past the due date.

If payment is not received within the agreed timeframe (or by the extended due date) it is essential to notify the insurer immediately. Failure to do so may prejudice a claim. The insured must follow up the overdue account and keep the insured informed. While the account remains overdue, further deliveries will not be covered.

TIMING IS CRITICAL

There is an unequivocal requirement to notify the insurer as soon as circumstances are known which may result in a claim.

If a customer has made payments but is known to be facing financial difficulties, or if any other reason arises which might cause non payment, the insurer must be notified within the timeframe specified. The timeframe varies from policy to policy and in some cases may be very short. Failure to notify may compromise the claim.

MAKE EVERY EFFORT TO COLLECT DEBTS

There may be several reasons payment is not received from a customer. For example, in some countries or industries there may be a tradition of delaying payment.

If a buyer is late in paying, an established collection procedure should be used. Most companies have internal guidelines to manage late payments. However, if these procedures prove ineffective, it may be helpful to employ a professional collection agent. Most trade credit insurance companies either offer debt collection services or have partnered with specialist collection firms and will typically contribute towards collection costs.

SUPPORTING THE CLAIM

Claims must be submitted within the time limit specified in the policy. When making a claim, supporting evidence will be required, including:

- A summary of the circumstances giving rise to the loss, including the contract with the buyer and invoices.
- Evidence of dispatch, for example the carrier's receipt.
- Correspondence relating to the debt and attempts to recover it.
- Details of any security held.
- Historical statements of account.
- Evidence of insolvency including registration of debt.

To ensure a smooth claims process, a policyholder should clarify all evidence that will be required under the policy and ensure that the organisation's internal systems are set up to provide it if necessary.

CONCLUSION

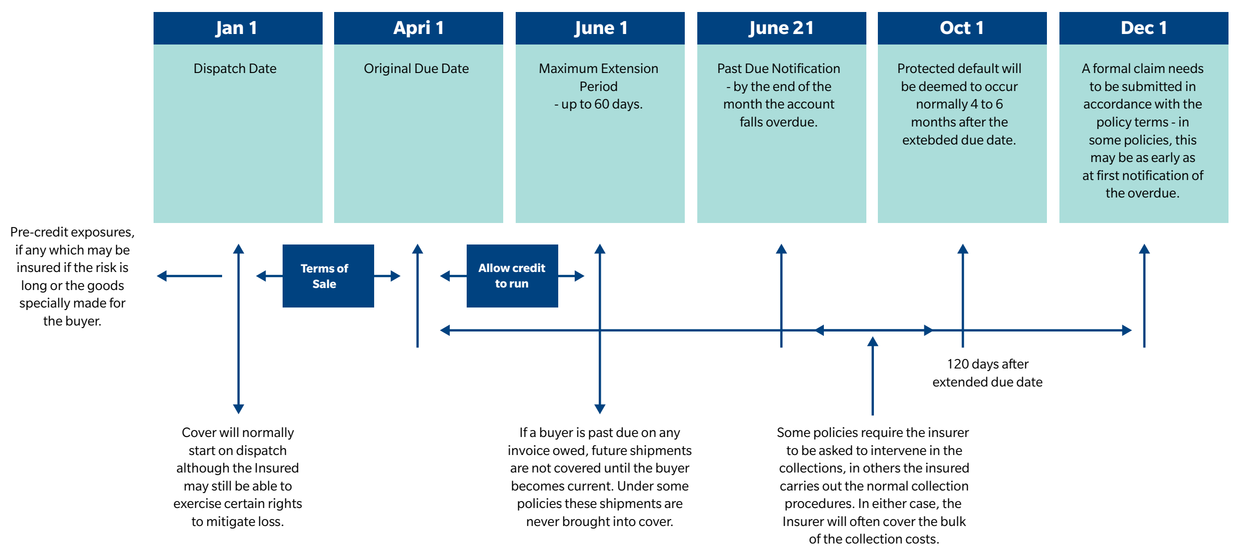
An investment in trade credit insurance is a valuable part of a supplier's overall risk management approach and can deliver many other benefits to support business growth.

Variations exist between the policy terms and approach of all major credit insurers and policies can be tailored to ensure they respond most appropriately to particular trades or circumstances. Insurance brokers can provide specialist advice to help businesses choose the most effective trade credit insurance solution.

In recruiting expert external advice, businesses can redirect their resources towards growing sales and achieving operational efficiencies, instead of worrying about the potential for default and chasing overdue debts.

Through effective risk management, today's global suppliers can benefit from the enormous rewards of being part of the great Asian manufacturing engine.

TYPICAL CLAIMS PROCESS



POLITICAL RISK CLAIMS:

PREPARATION IS KEY TO PROTECTING YOUR GLOBAL INVESTMENTS

Political risk is the top concern for corporate investors, according to the World Investment and Political Risk Report[1] by the World Bank's Multilateral Investment Guarantee Agency (MIGA). This concern is well founded – research from Marsh and Maplecroft has found that nearly one-in-five countries experienced escalating political violence at the start of 2013.

In response, the take-up of specialised insurance to mitigate this risk is rising, including for businesses based in Asia.

Navigating the political risk insurance sphere can be complex. Claims and claim determinations are custom-crafted, not standardised, and can be factually complicated. A keen understanding of the claim process, particularly from an underwriter's perspective, can help a business secure the best policy response at claim time.

THE RISKS ARE REAL

Politically inspired events can unfold, often without warning, and have serious implications for businesses. Acts of war, terrorism, and military coups are extreme examples of political risk, but civil unrest spurred by government elections can have equally negative consequences for trading conditions as businesses suspend or abandon operations.

A number of current geopolitical trends in particular continue to underpin the risk globally. The introduction of austerity measures to tackle the economically crippling effect of the global financial crisis has incited violent demonstrations across many countries, threatened cash flows, and complicated exit strategies for lenders and investors. Meanwhile, persistent regime instability is creating uncertain investment conditions in parts of the Middle East, Africa, South America, and Asia.

In addition, a widespread swing to more socialist politics in many parts of the world is seeing the rise of "resource nationalism", with people's interests taking priority over corporations in the ownership of strategically important natural assets. This shift impacts the investment environment and, in more radical cases, can manifest in expropriation of assets by governments.

[1] 2011 World Investment and Political Risk": Report by Multilateral Investment Guarantee Agency <http://www.miga.org/resources/index.cfm?aid=3227>

If these risks are not adequately managed, the effect can mean costly, unproductive delays at best, or operational abandonment at worst.

THE RISE OF POLITICAL RISK INSURANCE

Political risk insurance has become increasingly vital as a risk management instrument for businesses investing or operating in politically unstable countries, particularly emerging markets. By covering possible losses resulting from expropriation, currency inconvertibility, and political violence, political risk insurance can reduce value erosion caused by sudden disruptions, allowing more focus to be placed on measures to increase profit potential.

It can also unlock access to financing as it gives lenders, whether in the public or private sector, assurance that the impact of political uncertainties for a project or investment has been mitigated. This potentially improves the amount, interest, and tenor of loans received. In fact, most banks will demand political risk insurance coverage on assets they are financing in emerging markets, where this risk is a significant challenge for foreign investors.

The political risk insurance market has grown worldwide. According to the World Bank's Multilateral Investment Guarantee Agency's (MIGA) 2011 World Investment and Political Risk report, foreign investments covered by political risk insurance grew from 5-8% a decade ago, to 13-15% in 2011[2]. Members of the Berne Union, the world's leading association of export credit and investment insurers, collectively issued more than US$93 billion worth of political risk cover in 2012, up 20% from 2011.

Political risk insurance policies typically offer the following types of coverage:

- Transfer Restriction: It protects a lender against a borrower's and/or a lender's inability to convert local currency proceeds into foreign exchange, or from transferring the foreign exchange out of the developing member country, to service the guaranteed debt.
- Expropriation: It protects a lender against expropriatory measures, including nationalisation, deprivation, and confiscation, which prevent a borrower from servicing guaranteed debt. The guarantee also protects a lender in the event of an inability to service debt arising from a series of measures that constitute a "creeping expropriation".
- Political Violence: It protects a lender against a borrower's inability to service guaranteed debt as a result of physical damage to a project's assets, or an interruption in a borrower's business activities, as a result of war, revolution, insurrection, terrorism, or other politically motivated acts.
- Contract Disputes: It protects a lender against a default by a borrower of a guaranteed loan as a result of a frustration of an arbitral process (Denial of Justice) and/or the inability to enforce an award against relevant governmental parties to a project agreement (Arbitration Award Default).

SETTING UP FOR CLAIM SUCCESS

Just as the outcome of political events can be difficult to predict, so too can the political risk insurance market be difficult to navigate. Claims and claim determinations are custom-crafted, not standardised, and can be complicated. Businesses should consider the following key areas to secure the best response from their political risk insurance policy.

DISCLOSE MORE, RATHER THAN LESS

Due to the large quantum of risk capital extended by underwriters of political risk insurance policies, these underwriters should be viewed as genuine partners to the insured party, in the same way as an equity investor.

This entails transparently disclosing every material fact that a prudent underwriter would reasonably expect to know in forming a decision about whether to take on a risk and at what price. The insured's duty of disclosure

[2]2011 World Investment and Political Risk": Report by Multilateral Investment Guarantee Agency <http://www.miga.org/resources/index.cfm?aid=3227>

does not end when a policy is placed. If material changes occur to the circumstances of an insured business during the life of the policy, the validity of the policy may be undermined. For example, during a recession it is common for a business to renegotiate an underlying contract with a trading partner or to reschedule payments. If an underwriter is not advised of these changing circumstances, any potential claim will be at risk.

If in any doubt as to what should be disclosed to an insurer, it is advisable to err on the side of caution and disclose more rather than less. Better still; ask the insurer whether a change in circumstances is material. If time allows, set up regular (monthly or quarterly) disclosure meetings.

Another common question for businesses is who exactly is bound by the disclosure duty, particularly in large organisations with many employees operating in multiple jurisdictions. In these circumstances it is often advisable to seek to negotiate an agreement with the underwriter to limit the duty of disclosure to a defined group of people within the organisation or specifically defined categories of information.

COMPREHENSION, COMFORT, AND COMPLIANCE ARE CRUCIAL

What a policy does and does not cover, along with other terms and conditions, will vary from insurer to insurer. It is important to understand, be comfortable with, and comply with all policy wordings.

A policy that covers strikes, riots, and civil commotion, for example, may not cover confiscation, war, or civil war. Another policy that covers war and civil war may not cover expropriation or the imposition of currency exchange controls. Indeed, some exclusions may arise for situations in which a subjective judgment may be required, such as corrupt dealings in which the validity of adverse government actions can be disputed. Similarly, it is often overlooked that most governments are at liberty to expropriate an organisation’s assets so long as the organisation is fairly compensated under international law. The issue then is how to determine fair value.

In addition, businesses should be aware that waiting periods may also be involved before claim payments are made under confiscation, expropriation, nationalisation, contract frustration, and currency inconvertibility covers. This may be due to the insurer’s view that the restrictions caused to the insured may be only temporary.

It should not be overlooked that all political risk policies are confidential. Disclosure to third parties without the prior consent of the underwriters will breach the contract and jeopardise a claim.

An organisation’s failure to fully recognise or comply with the terms of the policy may compromise the way they expect a policy to respond when a claim is made.

WHEN TO NOTIFY INSURERS

A business must notify an insurer promptly if circumstances arise under which a claim will be made or, indeed, if anything should occur which has the potential to lead to a claim. As a plan of action is developed to manage the circumstances, the underwriter should be consulted on the plan and consent must be received by the underwriter before the plan is carried out.

SUPPORTING THE CLAIM

When making a claim, many business owners are not fully prepared to meet their obligation to present their claim to the insurer and support their business’s respective position. Often the evidence required to support the legitimacy of a claim is underestimated and confusion surrounds the role of the loss adjusters appointed by insurers to investigate claims.

The burden of proof is always on the insured. It is critical to understand that the manner of claim presentation is often crucial for the timeliness of a claim determination. It is important to take the time to complete claims documentation as fully as possible, as this significantly speeds up the claims process and generally reduces the number of queries raised by insurers. All documentation, including reports and other physical evidence, needs to be preserved for use in the subsequent recovery action.

Often it can be useful to agree with the insurer when establishing the policy to evidence which will be required in the event of a claim and to annexe this list of supporting requirements to the policy. A broker with specialist experience in the field will also be available to support the claims lodgement and management process.

If a claim is rejected by an insurer, the policyholder may have recourse to the dispute resolution procedures in the policy. In such cases, most policies provide for international arbitration.

AFTER THE CLAIM IS PAID

Once a claim has been paid, the process is not over. The insurer will assume its right to seek reimbursement from the party that has caused the loss (often the host government) and the insured party has a duty to assist the underwriter in these efforts, sometimes over months or years, until recovery is achieved. This process is known as subrogation. Subrogation is where an entity (the insurance company) assumes the legal rights of another person (the insured) for whom the first entity has paid money on their behalf and will take legal action against the entity that caused the loss.

It is essential, early on in the claims investigation process, to consider the prospects of subrogation, as this may affect the way in which the claim is handled.

TYPICAL FREQUENCY OF CLAIMS BY POLICY TYPE

FREQUENCY	POLICY TYPE
↑	Trade Credit
	Structured Trade Credit
	Trade Disruption Insurance
	Lenders' Contract Repudiation
	Contract Repudiation
	Contract Frustration
	Lenders' Political Risk
	Equity Political Risk
	Wrongful Calling of Bonds

KEEPING YOUR INSURER ACCOUNTABLE

Your insurer is a genuine partner in this process and as such it is important to ensure you are partnering with an insurer that best meets your requirements.

Businesses are well advised to review the major credit ratings assigned by international ratings agencies to their chosen insurer and to consider having a rating clause written into the policy. If the insurer experiences a credit rating downgrade, the insured will have the right to cancel the policy without penalty.

CONCLUSION

Political and trade credit risk analysis has become an integral part of investment due diligence and planning, due to the possibility of continuing political, legal, and regulatory uncertainty in foreign ownership restrictions, capital controls, and partnership terms.

Political and structured trade credit insurance is vital to the risk management armoury and, in most cases, mandatory to secure finance.

While the political risk insurance sphere may seem complex, a keen understanding of the processes will enable a business to be prepared to support a claim smoothly through the process, allowing it to continue to trade regardless of the politically led events it may encounter.

While trade credit losses happen with regular frequency, losses which are covered by political risk insurance occur only sporadically and are difficult to predict.

EXAMPLES OF POLITICAL RISK INSURANCE CLAIMS

ENERGY COMPANY – INDONESIA

When the state-owned utility defaulted on its payment obligations, the insured initiated proceedings against the government of Indonesia under the guarantee issued by the Ministry of Finance. The arbitration tribunal found in favour of the insured.

Result: Following the government's failure to pay this award, the insured filed claims with OPIC and private market insurers and received full payment under the policies of $290 million.

MINING – SOLOMON ISLANDS

Mining was suspended and staff evacuated after political unrest broke out in June 2000. However, even after a cease-fire in October 2000, the mine remained occupied by hundreds of supporters of the Isatabu Freedom Movement. The conflict appeared to be based on resentment between the local islanders and management of the mine who came from another island.

Result: The claim was approved and paid up to the full policy limit of Au$70 million.

TECHNOLOGY – VENEZUELA

Due to worsening of the economic crisis, the state-owned Venezuelan oil company expropriated the insured's ownership interest in their joint venture without any compensation. The insured filed a claim with OPIC.

Result: OPIC agreed that the government's actions against the insured were discriminatory and arbitrary and paid compensation of $6 million.

OIL & GAS – ECUADOR

The expropriation of the investment of a US oil company with significant assets in Ecuador resulted in a cessation of operations. The central government offered compensation in line with bilateral agreements, but significantly less than the net investment value of the operation.

Result: The market agreed to pay the difference between the compensation provided by the Ministry of Finance of Ecuador and the net investment value of the operation.

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