Exercising the choice...

Chris McGloin became Vice President, Risk Management & Insurance at Invensys at the beginning of 2006. Prior to that he had spent over 30 years in the insurance industry at Royal Insurance, Sedgwick and Aon. He has recently been appointed to the council of the Association of Insurers & Risk Managers (AIRMIC). This combination of experience makes him well placed to opine on the key aspect of the reform programme – how will the changes that London is implementing allow the market to better meet the needs of its clients?

Invensys, a FTSE 100 company, is a global technology and controls business focussing on industrial automation, rail transportation and controls. It employs 25,000 people and has facilities in more than 60 countries.

When agreeing to contribute this article, the essential question I was asked to tackle was: "what do clients look for from the London insurance market; and how far off providing that level of service is the market as it currently stands?" Not a straightforward assignment as I am sure you will recognise. In order to understand where the answers to this question might come from, I think it is worth taking a couple of steps back up the chain. The starting point is: what leads a company like Invensys to purchase insurance in the first place?

At Invensys we fully subscribe to the belief that effective corporate risk management is at the core of an efficient operation. So key to our organisation is the ability to analyse the full range of risks posed to our business. Armed with that knowledge we then have to decide how best we can address those risks. To my mind there are two fundamental options. Either we accept the risk and seek to minimise it through good management and absorb any residual element; or we seek to transfer it in some way.

The vital component that helps you reach the right decision in this process is good information. Invensys understands its main areas of operation – engineering and technology. This puts us well placed to be able to deal with risks in these areas internally. Our knowledge of our primary operational risk allows us to minimise the potential for realisation through such things as tight terms with our customers. It also allows us to have a good concept of which risks we can simply carry ourselves. Out of this process comes a collection of risks that we think we cannot manage ourselves. Typically this is where we have insufficient knowledge of the likelihood of the risk crystallizing and our suffering a loss; or where the potential loss is sufficiently significant that we could not easily make adequate provision for it internally. These are the risks that we are prepared to pay money to transfer.

So the primary benefits we are seeking to gain from an insurance transaction are better knowledge and support than we have in house to address the risk; and/or access to sufficient capital to underwrite it. Mostly we look therefore to cover catastrophe risks on property and casualty exposures. On top of this, in our line of business, we do have statutory obligations to provide certain types of cover – Invensys is active in more than 100 territories and we need proof of certain insurances to be able to trade in many of these.

Having made the decision to purchase insurance, we gravitate towards London. Invensys is a UK plc; my background means that I know the environment in London and feel I can get the deals I need. Above all, we understand the law that underpins most London market deals and feel comfortable with that. Even before the impact of the credit crunch on certain carriers, I had not felt comfortable that alternative approaches using the capital markets were of sufficient maturity to breed confidence. In my mind therefore there is still a strong market demand for conventional insurance products.

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Looked at on one level then, you could say that London is delivering its customers' needs. But delve a little deeper and I think a different story begins to emerge. When buying insurance I think most clients expect a number of fundamentals:

- The ability to present the data that informs the underwriting process in a standard way (and preferably electronically) with confidence that the underwriters' expectations have been met;
- A document (the insurance contract) that the insured can understand and that clearly meets the requirements of any of the territories that they operate in;
- For business to be settled in a clear way; and
- Clarity on the ability and willingness to pay claims with a transparent process to deal with them.

At the moment, from where I stand, I am not sure how well the market is meeting these needs. I judge that any reasonably sophisticated client is capable of providing all the information an insurer needs to assess a risk in any format required by any insurer. Certainly this is true of Invensys. The problem we face is that insurers find it difficult to decide what it is that they want. Information requirements and formats vary from company to company; and from year to year. I accept that the development of the slip standard and the increasing take up of electronic placing are beginning to address this issue, but I would urge you all to make sure that this process is not allowed to falter. The end result should be better information, better coverage, improved prices and happier insurers – and insureds!

I have noticed that the contract certainty exercise has had a significant effect on the market. It is now at least a question of when rather than whether you will receive your insurance documents. But I would urge the market not to focus solely on production at the expense of quality. One only has to look at some of the media stories around NHS targets (remember Tony Blair being confronted on Question Time about GP appointments) to see the dangers of concentrating too much on one aspect of a process. Don't undermine the genuine progress made by the market by falling in to this trap.

I found the accounting and settlement process opaque when I worked in the industry. It is twice as bad now I am a buyer. Customers like to know where their money is going and how it gets there. If an industry is not moving the money around in a simple, efficient manner, you wonder where else it is allowing unnecessary complication to the process. The removal of paper submissions from the London market is commendable up to a point – the move to exchanging structured data will be a further improvement. Even then, I think we clients will be entitled to ask "what took you so long?"

The fundamental point for any client when purchasing insurance is that money is being paid in return for a promise to pay for losses. How the market delivers on that promise is the single most important aspect of the service you offer to your customers. My experience is that I can have up to a dozen different parties involved in the reporting process for my claim before it even starts. It is difficult to understand what each party adds to the process apart from complexity or delay. Why should the interests of the reinsurer or someone further down that chain matter to me? I want support to help me manage the incident and my money in compensation for a valid event.

So, at the least, anything that makes information available to all these people simultaneously must be a good thing. I am encouraged therefore by news of the electronic claims file. But I believe fervently that the thinking needs to go beyond this. The London market needs to develop a claims model that genuinely puts the interests of the client over those of other parties if it is to remain an attractive place to purchase cover.

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I also believe there is a need to extend this client centric thinking into more than just the claims arena. One of the things that really frustrates me as a risk manager is the annual renewal cycle. I would far rather purchase a five year contract, say, where the longevity of the relationship would deliver better value and where I could be less concerned about price fluctuation. Long term deals like this would also allow the insurer to change approach and rather than spending 90% of its time focussed on the transaction, it could spend 90% of its time focussed on business development and service quality. Concentration of resources on the tasks that can add most value is at the heart of a modern service model.

But, you might say, for all this, many buyers still choose to bring their business to London. That is true. But to a degree that is only for want of a viable alternative. In 10 years time will that still be the case? I am not sure. I see developments in Shanghai and in the Middle East either of which could provide an alternative market of choice. I am not sure there is too much mileage in London believing custom will always come because there is nowhere else to go.

I applaud the effort made thus far to improve the efficiency of the London market. Importantly the Market Reform Group is working with AIRMIC and other client groups to understand their position. But whilst progress has already been significant, please do not think that from a client perspective it is anywhere near sufficient. It is not just my colleagues in Airmic and the risk management industry that you need to listen to. Your target audience is also the top management from major companies across different industries who have had to work very hard to improve their own business models. Some of these look at the insurance industry and doubt whether you have the will to bring about the improvements needed. Given my background, I am keen they are proved wrong.

I think the challenge for London is not just to get better at what it does already, but to completely reappraise the offering to clients to provide a product more geared to client need and less driven by internal practice and reinsurance cycles. I have seen it quoted that the frictional cost of placing business is 35% of premium. That means that, at present, insurers can only commit 65% of the industry's income to paying claims – the key factor that all clients value above all. That must affect insurers' attitude to claims management. There is an enormous opportunity here. Suppose you could deliver a market where that transactional cost began to bear comparison with that in other wholesale financial markets. Imagine if insurers could commit, say, 90% of industry income to paying claims. That allows for an entirely different business model – and one that could redefine your relationship with the end customer for the better.