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J.B.BODA GROUP

MEDIAN

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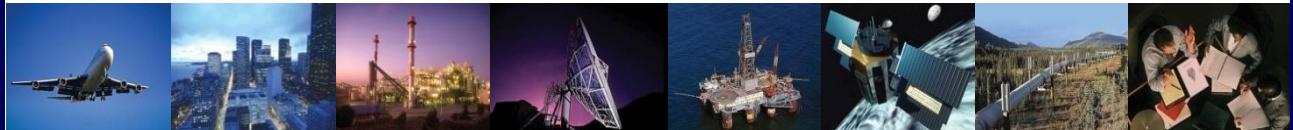
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ON “WRITE” SIDE

Valuation of Assets - IV

Sanjiv Shanbhag

(i) **Turnkey Projects:**

In practice, Insured also faces the problem on Turnkey Projects, where capitalised cost of the equipment item-wise is not available.

In such a situation, it is not possible to apply Index Method, when basic equipment cost is not known.

In a situation like this, following approaches are possible:-

- (1) On completion of the Project, work out the Estimated Replacement Cost at least for the major items with the help of the Project site team. Contractor for the Project may also be able to assist in this exercise.

For subsequent years, Index Method may be followed.

- (2) On completion of the Project, invite the quotations for the major items to be selected for the purpose of Operational Insurances. This may be done only once at the initial stage and for subsequent years, Index Method may be followed. However, care is to be taken that quotations are received for similar type and kind of equipment, otherwise cost may call for adjustment.
- (3) This task may be assigned to independent valuer, who may be having a Data Bank for price of similar equipments based upon their working on the other plants, where such data may be available.

Further, the price can also be interpolated based on prices available for similar equipments, but of different size and make. This may be approximate, but may reflect within narrow range of reality based on experience and data of valuer.

In an exercise like this, one has to be resourceful for getting the required details. Having once established the cost, future valuation can go by Index Method.

All the above Methods will give approximate valuation, but no better approach is available and one has to depend on the best of judgement and available information.





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In the above Method, the answer will be close to reality, when compared to actual quotation at time of claim and thus difference is minimised.

(ii) **Indigenous equipments with partly imported components:**

In such a situation, Insured suffers heavily at the time of claim, if proper precautions are not taken for adequacy of Sum Insured.

In this case, the first assumption is that Insured should be aware that some of the major equipments which are supplied by the local manufacturers or suppliers also contain certain imported components.

While purchasing the equipment, Insured has to atleast ascertain percentage of imported component in the equipment which he buys locally.

Once the cost is segregated approximately between imported and indigenous components, valuation can follow partly by local Index and partly by Index for imported machinery.

In normal course, Insured may escalate only as per RBI Index being local supply, but may go wrong when imported parts are quoted by manufacturers for repairs etc..

This approach brings adequacy of Sum Insured with the nearest approximation. Custom duty for parts may be substantially higher compared to custom duty for equipment as a whole.

Operational Policy only allows that percentage of custom duty, which is included in Sum Insured.

In order to overcome this problem, there is a provision for Additional Custom Duty cover, which Insured can avail, if desired.

MCE POLICY:-

In this case, adequacy of Sum Insured is to be determined under following situations:-

- (A) Turnkey Projects.
- (B) Projects partly handled departmentally in-house and partly by contracts.
- (C) Projects with partly old and partly new machinery.

In the above case, following approach may be adopted for adequacy of Sum Insured.





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(A) Turnkey Projects:

It is observed that when the consignments are received on item rate basis, there are no problems in settlement of the claim either under Marine or Erection cover.

However, care is to be taken particularly in respect of changes in Foreign Exchange Rate and Custom Duty during the period of initial shipment and replacement in the event of damage.

While declaring the Sum Insured as per contract, exchange rate and custom duty considered for arriving at the Sum Insured should be specified.

Further, sufficient escalation on judgement basis to be provided to take care of fluctuation in exchange rate, custom duty etc. during the Project Period.

Fluctuations of above nature are unpredictable and hence only best judgement can be used.

There are many instances where Projects are finalised on Turnkey Basis and consignments are received on weight basis.

In such cases, it is noticed that arbitrary price is indicated on weight basis and it has no relation with the real price. This is likely to happen as the contract price is firm and therefore for maximum recovery, earlier consignments may be priced higher than normal.

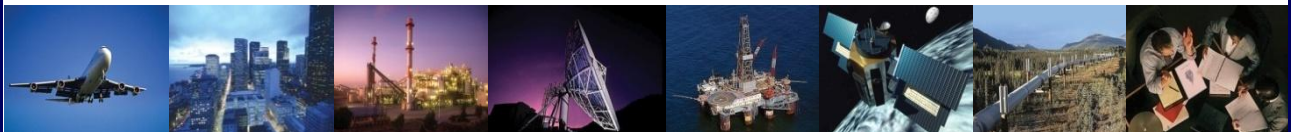
However, in the above cases, Insured and Insurer can agree on commencement of the Project on some break up of prices on weight basis and that is to be followed in the event of a claim under Marine or Erection cover.

This break up broadly covers the various equipments and their components, and rate on weight basis is fixed based upon nature of the equipment and its components.

In the absence of any other way of determining the price, this appears more practical and near to reality.

B) Projects partly handled departmentally in-house and partly by contracts:

Problem may be faced in arriving at adequacy of Sum Insured in case of Projects partly handled departmentally in-house and partly on contract basis.





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For part of the work handled on Contract basis, price is available from the Contracts.

For departmental in-house work, price is to be worked out based on Project Estimates, which may vary on completion. However, for the purpose of declaring Sum Insured, Project Estimate may be the basis.

In order that adequacy of Sum Insured could be established at the time of a claim, it may be necessary to keep the records of Project Working and Value arrived. It will also indicate assumptions taken into account for exchange rate, custom duty, escalation etc.. Further, the sum calculated and insured in the above manner should also tally with the Project costs that are declared by financial institutions etc..

In addition to above, escalation provision on judgement basis is to be provided for taking care of fluctuation in exchange rate, custom duty, escalations etc. during the period of initial procurement and replacement in the event of damage.

C) Projects with partly old and partly new machinery:

In such cases, Sum Insured is to be based on Market Value of the plant (Old and New) inclusive of freight, insurance, installation and modification costs etc. Further in case of imported equipments, exchange rate and custom duty taken into account for valuation has to be specified. Escalation is also to be provided on judgement basis, as Market Value of plant will vary based on escalation changes in exchange rate, custom duty etc..

In the event of a claim, one may have to work out approximately the Market Value of the plant as a whole based on the approximate cost of New Plant of same size and type. If Sum Insured is found to be adequate on Market Value basis, then the claim can be settled based on ratio of Market Value to be applied to the cost of Replacement Cost.

New equipment to be replaced in place of damaged one. When separate cost for second hand and new equipments is available, this exercise can be separately done as applicable in the event of a claim.

CAR POLICY:-

In this case, adequacy of Sum Insured is the Estimated Value of the Completed Contract. It is easy to indicate Sum Insured based on actual Contract Value, which is usually an item rate Contract.





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However, Insured has to be careful for the following considerations:

- 1) To increase or decrease the Sum Insured, when scope of work is increased or decreased or Project Cost has gone up for changes in price of material or labour.
- 2) To take care of Escalation during Construction Period.

If due to collapse or failure, work is to be repeated, it may attract Escalation which is to be taken care of.

Percentage of Escalation to be provided will depend on judgement for duration of Project.

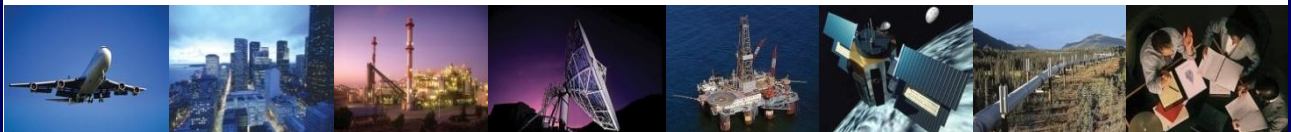
CONCLUSION:-

For the purpose of proper Insurance Management, adequacy of Sum Insured plays a vital role – particularly in the present context, when escalation, changes in exchange rate, custom duty etc. are major ones.

Best judgement based on definite facts seems to be the only solution.

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REINSURANCE

Allianz Re

Property and Casualty Reinsurance rates won't increase in January 2013, when the industry renews the majority of its annual contracts with clients, according to Allianz SE (ALV)'s reinsurance arm. Rates will probably be flat to a little down in January 2013.

ECGA inks MOU, Reinsurance Agreement

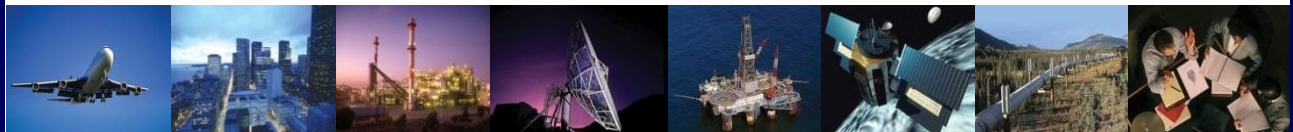
Export Credit Guarantee Agency (ECGA) of Oman has inked MOU with Export Import Bank of Malaysia, for the strengthening of mutual cooperation, covering the exchange of information, technical assistance, training and so on, between the two ECAs. A Facultative Reinsurance Agreement was also signed by the ECGA of Oman with the Arab Investment and Export Credit Guarantee Corporation (Dhaman). The reinsurance agreement operates on a facultative basis, as it will reinsure exports of Omani goods and services against the risks insured by ECGA of Oman and reinsured Dhaman. This agreement provides additional support for ECGA in covering selected exports for exports not covered under its existing Quota Share Reinsurance Treaty.

Munich Re

Yingli Green Energy Holding Company Limited, a leading solar energy company in China and one of the world's largest vertically integrated photovoltaic (PV) manufacturers, has announced a module performance warranty insurance agreement with one of Munich Re's speciality primary insurers.

In the event of an unexpectedly large performance specification, Munich Re indemnifies Yingli Green Energy for its performance warranty obligations. The Agreement covers the 10 years and the 25 years warranty on all multicrystalline Yingli Solar modules.

It guarantees that within 10 years multicrystalline Yingli Solar modules exhibit a power output of not less than 91.2 % of the nominal power output specified on the module's original product label. Furthermore, it covers multicrystalline modules within 25 years exhibiting a power output of not less than 80.7 % of the nominal power output as specified on its original product label.





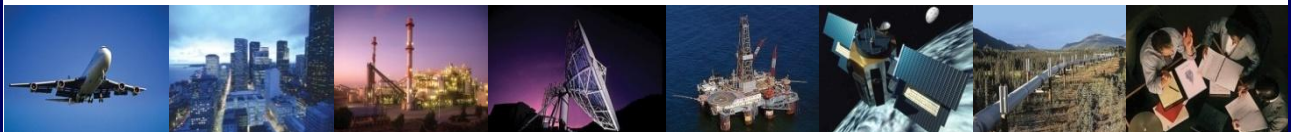
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Swiss Re

Life insurance premiums will rise 2 % in 2013 after not growing in 2012, while property and casualty premiums will rise 3 % in real terms, fueled by emerging markets, according to the Zurich-based reinsurer-Swiss Re.

US Reinsurers

The North American reinsurance sector posted a strong financial performance during the first three quarters of 2012, according to data recently released by the Washington – based Reinsurance Association of America.





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INTERNATIONAL

Asia : Ageing an opportunity

Longer life spans may drive up healthcare costs, but they also present a big opportunity for both the governments and the health insurance sector in the region, according to Swiss Re.

China

Fitch Ratings maintains a “Stable” outlook for China’s insurance sector over the next 12 to 24 months, but recent exits by overseas investors have stirred concerns about the sector’s profitability.

Ghana : Company marks 40th Anniversary

The Ghana Reinsurance Co. Ltd. (Ghana Re) has held its 40th Anniversary retreat in Accra, with a call on Ghanaians to insure their property to enable them recoup their losses. The aim of the retreat was to bring unity among partners in Ghana, to help address the grievances of clients and to examine the merits and demerits of phasing out the mandatory cessions becoming a norm in Africa.

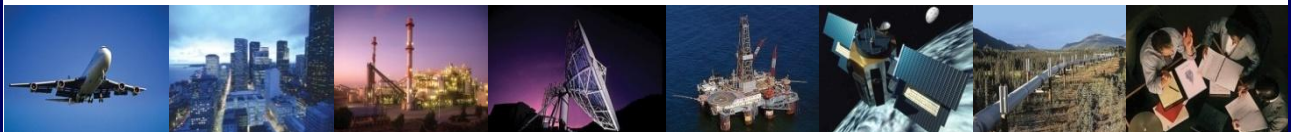
Ghana Re was formed through the initiative of the United Nations Conference on Trade and Development, which encouraged developing countries to form local and regional reinsurance companies with the view to create increased local capacity.

Middle East : JV Agreement

The global health benefits business unit of Cigna and Saudi Arabian Insurance Company B.S.C. (C) (SAICO) have announced that they have signed a joint – venture agreement to enhance their current partnership in developing their portfolio of health, wellness and insurance products targeted to regional and multi-national employers and organizations across the Middle East, expanding the 11 years business relationship between these two companies.

Nigeria

The Nigeria Deposit Insurance Corporation (NDIC) has stated that the International Monetary Fund (IMF) and the World Bank would be using the existence and capacity of Deposit Insurance as a measure of financial stability. This move by the IMF and the World Bank was to promote the importance of Deposit Insurance in the continent.





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With many African countries operating without a Deposit Insurance institution, the global financial institution had brought to fore the need and importance of Deposit Insurance.

South Korea : Stable life sector

The South Korean life sector's rating outlook for 2013 is stable on basis of continued demand for insurance policies, risk awareness, and increasing emphasis on prudent capital management, according to Fitch.

Vietnam : Health Insurance

At a recent meeting organized by the Ministry of Health and Vietnam Social Insurance (VSI) in HO Chi Minh City, to review three years of implementation of Medical Insurance Regulations, it was disclosed that almost 30 million people are still not covered by Health Insurance in Vietnam.

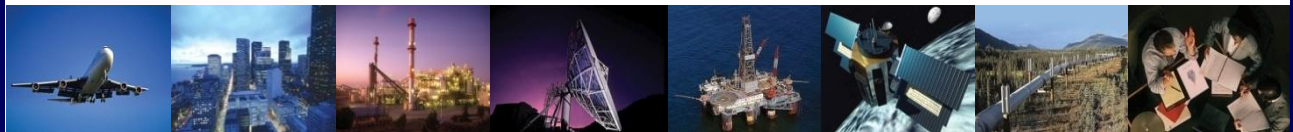
Insurance accounting practices

Swiss Re's latest Sigma research publication "Insurance accounting reform : a glass half empty or half full ?" takes a fresh look at the long – running debate over upgrading and harmonising insurance accounting practices. A key conclusion is that the proposed accounting reforms can contribute to more meaningful financial reporting in insurance. But they need to be complemented with additional metrics that communicate insurers' underlying economic value to their stakeholders.

Powerful quakes

Researchers have pinpointed the locations – like Indonesia's Sumatra Island – where the world's largest earthquakes are most likely to take place, with greater accuracy than ever before. "Subduction zones, where one plate slips under another, have long been known to harbour very powerful earthquakes, but our research suggests that regions where fracture zones on the seafloor meet subduction zones are at much higher risk", Dietmar Muller from University of Sydney has said.

The coasts of Southern Chile and Peru, Indonesia's Sumatra Island, and several regions along the eastern Eurasian coastline, are some of the regions prone to great earthquakes. The research has indicated that 87 % of the 15 largest (8.6 magnitude or higher) and half of the 50 largest (8.4 magnitude or higher) earthquakes of the past century are associated with areas of intersection between oceanic fracture zones and subduction zones.





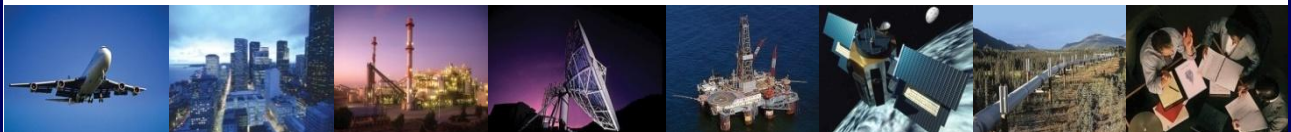
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Major factory fire in Bangladesh

A Bangladeshi garment factory that was producing clothes for Wal-Mart, Disney and other major Western companies had lost its fire safety certification in June 2012, five months before a major blaze in the facility killed 124 workers, according to Fire Brigade sources in Dhaka. The Tazreen factory had only permission to build a three-story facility, but it was expanded to eight storeys and ninth floor was being added at the time of the blaze. These scary facts about the deadliest garment factory fire in Bangladeshi history provide insight into the chaotic nature of safety enforcement at the country's more than 4,000 garment factories.

The damaged garment factory is responsible for 80% of Bangladesh's exports.

According to Fire Brigade sources, the factory did not have any fire exits for its 1,400 workers, many of whom became trapped by the blaze. Investigation has revealed that the death toll would have been far lower, if there had been even a single emergency exit. Fire extinguishers in the building were left unused, either because they did not function or workers did not know how to use them.





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NON – LIFE

Live with floods !

Flood is a natural phenomenon.

No one should even attempt to control it. The approach should be how best you live with floods.

India : Impact Statistics

- (i) Flood prone areas – 45 million hectares. Equivalent to 30 million cricket grounds of the size of Lords
- (ii) Annual damage INR 18.24 billion (USD 365 million)
- (iii) Lost of human lives 1,620 per year (Average between 1953 and 2009) 11,316 people lost their lives in 1977, the highest in a single year.
- (iv) Annual Damage to crops – INR 7 billion (USD 140 million)
- (v) Houses damaged – 1.2 million a year (Average between 1953 and 2009)
- (vi) Floods management cost – INR 500 billion (USD 10 billion) projected outlay for managing floods in 12th Plan as demanded by Water Resources Ministry, Government of India.
- (vii) Total amount spent on managing flood by Government of India between 2007-12. INR 100 billion (USD 2 billion). This amount does not include relief, rehabilitation and expenditure from kitty of State Governments.

India : Attempt Statistics

- (i) Flood forecasting – It gives an idea of level of water – flow and inflow of water in a river.
 - (a) 175 – Flood forecasting stations
 - (b) 140 – New flood forecasting stations likely in 12th Plan.





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- (c) 6000 – Average number of flood forecasts issued per year.
- (d) 98 % accuracy in flood forecasting, as claimed by Central Water Commission
- (e) 23 – Number of Key Expert Panels and Policy Documents on Flood Management.

India : The Schemes

- (i) Flood Proofing – It is a concept of raising villages above pre-determined flood level and connecting those to roads or high lands. It was applied to thousands of villages in UP in 1950s. Later it was experimented in West Bengal, Assam and Bihar.
- (ii) Living with Floods – It is based on the principle that no one can stop floods and one needs to learn to live with floods. Raised platforms fitted with amenities like drinking water, sanitation etc. were constructed across flood – prone States. Experimented between 1997 and 2002.
- (iii) Beyond Borders – China shares hydrological information on rivers Yaluzangbu (Brahmaputra) and Langquinzangbu (Sutlej) during monsoon. Five Indian flood forecasting stations get this data.

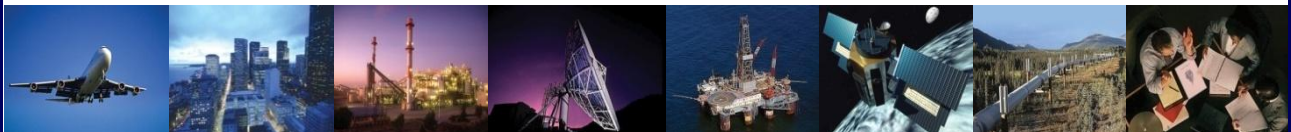
Source : The Economic Times Magazine

Insurance for deposits

Bank deposits of INR 38 trillion (USD 760 billion) accounting for 67% of the total deposits, do not have cover from the Deposit Insurance and Credit Guarantee Corporation (DICGC) as of September 2011. This is based on data from the Reserve Bank of India – the central bank of the country. The falling insurance cover is due to the rising proportion of high-value deposits. Bank depositors enjoy insurance cover on deposits upto INR 100,000 (USD 2,000). This means that if a bank goes belly up, each account will still recover upto INR 100,000 from the Corporation.

Health Insurance

As fraudulent practices erode the profits of health insurers, certain measures could help stem the rot. For the health insurance industry, the growing number of fraud cases at various stages has become a major concern and unless collective actions are taken, they may take serious proportions in the years to come. Increase in frauds indirectly drives up the premiums collected from insureds, as insurers ultimately recover the losses by increasing the premiums.





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Some of the common frauds by insureds relate to concealing pre-existing diseases or chronic ailments, manipulating pre-policy health check-up findings, duplicate and inflated bills, purchasing multiple policies, staged accidents and fake disability claims. There is absence of standard medical protocols, hospital-induced frauds – overcharging, inflated billing, unwarranted procedures, extended length of stay, fudging records and patient history and even billing for services – form a large portion of fraudulent claims.

Business and industry circles have highlighted the concern that insurance frauds are not defined under the Indian Insurance Act. Even other instruments with the Indian legal system such as the Indian Penal Code (IPC) or the Indian Contract Act, do not offer specific laws.

Payment of legal fees

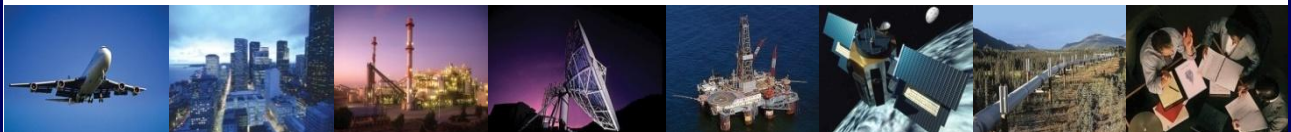
Bharti Walmart, which suspended its Chief Financial Officer and its entire legal team as part of a global probe into potential violation of anti-bribery laws in the US, had taken out a Directors' and Officers' Liability cover (D&O Policy) worth USD 5 million. The Policy partly protects the Company, its Directors and Officers for wrongful actions that cause financial harm and result in a lawsuit. If there is litigation in the case, thence the insurer will have to bear the legal expenses. Since Bharti Walmart had taken a pre-emptive step to suspend some executives, the chances of the claim are higher now. However, it is only after a legal suit is filed that the claim would arise. The D&O policies provide cover to the Company, its Directors and Officers against liability claims from third parties including shareholders, customers or employees.

Motor Vehicle Insurance

An executive going in the company car is entitled to compensation in a road accident only if the vehicle is insured under the Package Policy / Comprehensive Policy. The Supreme Court recently rejected the argument of an insurer that it was not liable to indemnify the managing director of a company, who was injured in an accident while riding the company car. The insurer contended that the Policy taken by the company did not cover the executive as he was not a "third party" under the Policy. If it is a Package Policy, the executive will be entitled to compensation from the insurer.

ESIC Act applicable to private institutes

The Employees State Insurance Corporation (ESIC) has clarified that it is mandatory for private technical and educational institutes to cover their employees under the ESIC Act.





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LIFE

Premium fall in 2013

Indian insurance regulator – Insurance Regulatory and Development Authority (IRDA) has hinted that the new mortality table for Indians is going to be notified in April 2013. Premium of new life insurance policies and term insurance plans will come down with the announcement of new mortality table, as life expectancy has gone up. The mortality table shows the rate of deaths occurring in a defined population during a selected time interval, or survival from birth to any given age. Statistics included in the mortality table show the probability of a person's death before next birthday, based on the age. The death rate data helps determine premiums paid by people, who have recently purchased life insurance. A mortality table is also known as a "life table", an "actuarial table" or a "morbidity table". Insurers charge mortality premium based on the mortality table and their risk assessment. Usually the mortality charge ranges from 0.5 % to 12 % of the policy premium, depending on age, gender and the policy chosen.

Life tables are usually constructed separately for men and women. Other characteristics can also be included to distinguish different risks, such as smoking status, occupation and socio-economic class. There are even actuarial tables that determine longevity in relation to weight. Presently, insurers are charging mortality premiums based on IRDA's data of 1994-96. The new mortality table is based on data collected during 2004-08. The average life expectancy in India has gone up in the interim, from 60 years in 1996 to 65 years in 2011.

High targets in industry

Thousand of "marketing" employees are leaving the private life insurance sector, as insurers feel the heat of sliding growth and rising costs with life premium collection dropping. An estimated atleast 10,000 people have quit the sector in the past two years. Staff hiring is now limited, since the boom that life insurance sector experienced from 2000 to 2010 is over.





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