

# MSM Loss Management

**Specialists in  
loss management  
and quantum**



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## **MSM Newsletter**

Keep up to date with the latest MSM news, industry views and profiles from your Inbox or via our website [msmlm.biz](http://msmlm.biz).

## MSM Newsletter

MSM email newsletter for clients and industry members covering:

### **MSM training:**

Details on MSM training programs and content

### **MSM News:**

Keeping you up to date with MSM's independent services and initiatives

### **Current Industry Issues:**

Across the insurance, risk management, legal and construction industries

### **MSM profile:**

A brief profile of MSM consultants

## MSM Training Update

MSM have again been running Business Interruption Insurance training. In the last few months, MSM directors Greg Sutton, Colin Chinner and Peter Rink have welcomed the opportunity to again run the NIBA Intermediate and Advanced Business Interruption training in Sydney, Brisbane, Adelaide & Melbourne.



**SYDNEY**  
Greg Sutton



**MELBOURNE**  
Colin Chinner



**BRISBANE**  
Peter Rink

MSM are pleased to be able to provide updates in our newsletters of legislative developments. We have received the following article from Kennedy's Solicitors who last month opened a new office in Sydney. We wish them every success.

## New Insurance Code

A new code of practice covering the insurance industry was introduced on 18 July 2006. It aims to raise service standards, improve claims and complaints handling and to assist customers to gain a better understanding of how general insurance works.

The new code – the General Insurance Code of Practice - covers nearly all types of general insurance. It is substantially different to the previous code both in form and content and places a number of new obligations on insurers. The new obligations include:

- meeting set timetables for handling claims or responding to complaints;
- fast-tracking claims or making advance payments to customers in financial hardship;
- giving reasons for a decision not to provide cover and referring applicants to alternative insurers. If the applicant is unhappy with the decision the insurer must provide the applicant with information about complaints handling;
- accepting responsibility for the quality of workmanship and materials used by a repairer authorised by the insurer;
- establishing internal processes for responding to catastrophes and disasters;
- providing up-to-date and clear information to the community to assist it to understand how insurance works.

The Insurance Ombudsman Service monitors compliance with the Code and receives complaints about insurers. The Ombudsman may impose sanctions on insurers for breaching the Code. It also provides a dispute resolution service under which its determinations are now binding on insurers.

The Code applies on an opt-in basis: it applies only to insurers that have adopted it. The types of insurance not covered by the Code are reinsurance and those regulated by statute (such as workers' compensation and marine insurance).

The Code is available online at [www.codeofpractice.com.au](http://www.codeofpractice.com.au).

Should you require any more information about the Code please contact Sumiya Basha at Kennedys solicitors on [s.basha@kennedys-law.com.au](mailto:s.basha@kennedys-law.com.au). Please also refer to the Kennedys website at [www.kennedys-law.com.au](http://www.kennedys-law.com.au).

## Weekly Benefit Policies

One of the most frequently asked questions at our training sessions is about the merits of weekly benefit policies compared to the more traditional gross profit policies.

The difficulty in answering these questions is that there is a myriad of covers ranging from many and varied package policies to specialist BI covers.

So what are some of the problems we encounter with these covers:

- They often seem to encourage short indemnity periods; as low as 3-6 months on some – at a time when we are challenging people over 12 month periods being inadequate!
- The true cost can be hidden behind short indemnity periods and are often proportionately higher than traditional policies.
- Sub-limits are often lower and can be grouped together to create an overall limit that may be insufficient.
- Some terminology is often confusing – for example work out the difference in covers between increased costs, additional expenditure, extra costs, additional cost of working. Most importantly how does this relate to the wider and preferable cover of “additional increase cost of working”.
- Some do not offer the wider additional increased cost of working at all.
- Many have a waiting period – i.e. the first 2-3 days is not covered. Apart from the deduction when does a client start incurring costs to reduce the loss of turnover?
- Cover ceases with some policies when the client reaches 90% of last year’s turnover – yes, last year’s turnover not what they would have achieved.
- Despite being designed for SME’s some still have optional wages cover – a sure fire way of achieving some self-insurance.
- The weekly benefit is usually the maximum payable so if the business is seasonal, and the wording does not have a seasonality endorsement or the client does not elect to take it, and there is a claim in a peak season, the Insured will often be underpaid.
- Many need increased costs to be approved prior to the insured incurring them compared with the preferable cover of “necessarily and reasonably incurred”.

Other questions we hear:

- *Isn't it an agreed amount?* Not always, some still have an adjustments clause, which can be used to reduce the claim.
- *But some don't deduct savings?* Yes that's right, but does the client get all of their increased costs and expenses covered too?
- *Aren't the benefits paid weekly?* In theory yes, in practice rarely. In any event, the traditional policies allow regular progress payments and keep the Insured in funds.

Other issues – beware of the consequences of separating the material damage and business interruption covers. The best result for a client that suffers a significant loss is to minimise the disruption period and any adverse impact on customers. Often this needs the two policies working in conjunction with each other to achieve the best result. With no BI component the material damage insurer can take their time, for example, in investigating the cause of the loss, preparing the scope of works and preparing tenders, so crucial weeks or even months can be lost. The negative impact occurs outside the indemnity period leaving the client with an un-insured loss.

Is there a place for weekly covers? Yes, but in the main for very small businesses who are capable of relocating to alternative premises and do not suffer much of a loss of profit. So be careful to match the customer needs with, in a short time frame, appropriate material damage and business interruption covers.

Finally remember the old saying – **“if it seems too good to be true it usually is...”**

-Colin Chinner

## Compliance – Ivan's Ideas– Insurer Incentive Schemes

There is an old saying that long-term underwriters used to pass on to staff beginning their career in insurance that went along the lines – “Don't let the sweet smell of success in capturing premium income disguise the odour of the related risk of claims”. A similar approach could also be good advice for brokers involved in or contemplating Insurer Incentive Schemes – take a long-term view on both the income and the related risk.

Here's a synopsis of our humble and objective view on the Insurer Incentive Schemes that are becoming commonplace across the general insurance industry.

From the insurers' perspective such arrangements are clearly designed to change or maintain the behaviour (advice and recommendations) of the broker. Why else would someone pay good money if there was no outcome achieved?

We are of the view (as, it would appear, are ASIC) that without documented evidence to the contrary such payments are a clear Conflict of Interest. This Conflict issue lead to such payments being banned under the Insurance Agents and Brokers Act and is the reason that a number of suppliers in the Life and Financial Planning markets are discontinuing such arrangements. The challenge for most Licensees is to ensure that such arrangements:

1. Do not materially impair the advice and recommendations being provided by the firm;
2. Ensure meaningful disclosure of such payments when they are of a material nature.

Looking at the issue of "advice impairment" a prudent broker will typically put into place a number of steps to protect the quality of advice being provided which, apart from rejecting such payments, will include:

- Formal written advice to all advisory staff that the additional commissions potentially earned from such arrangements are to have no impact on the selection of an insurer to recommend to a client.
- Monitoring of overall portfolio share for the insurer to ensure that there is no material or significant increase in the placement of business with a particular insurer that cannot be explained by other factors such as product coverage and flexibility, pricing or other objective factors that could support such a shift in portfolio distribution,
- A random review of files where existing clients are transferred from one insurer to the "Incentive Providing" insurer to ensure that such transfers are clearly in the interests of the client in terms of the value for money offering of the two products.
- List the payment arrangement in the Conflict of Interest table and document the procedures adopted by the business to control such a conflict.

As regards disclosure we note an interesting phenomenon amongst our Licensee clients. There is a general reluctance to ensure disclosure of such arrangements and an even stronger resistance to making such disclosures timely and meaningful.

In our view an effective disclosure process will include:

- A general disclosure in the FSG that the business may enter into Profit Shares with insurers.

- A specific disclosure attached or included with all invoices/quotations where the insurer paying the incentive is being recommended or used.
- Specific disclosure in phone calls and meetings where the insurer paying the incentive is being recommended or used.
- Such disclosures to express the potential payments in a meaningful way e.g. "The maximum additional amount payable averages \$125.00 for each policy that we write" or "the maximum additional amount payable increases our average commission from this insurer from 15 % of the base premium to 17% of the base premium."
- We also believe that in most cases Licensees can easily calculate an expected payment by simply using prior year figures and extrapolating them forward. To rely on the volatility of the payment as a method of avoiding adequate disclosure fails to meet the expectations of both ASIC and the community at large.
- The disclosure should be based on the best possible outcome for the Licensee. That is assume maximum payments are involved. If the maximum payments payable under the arrangement are embarrassingly large then negotiate with the insurer to cap such payments.

In closing, the technological age makes it easy for ASIC to identify and investigate such Profit Share arrangements. We would therefore not be surprised if ASIC initiated such a review in the short to medium term.

We believe that the Insurer Incentive payments within the industry are high risk and require significant management review. Our advice to an AFS licensee is "Don't let the sweet smell of the additional commission disguise the odour of the conflict - without adequate controls in place".

## MSM CORPORATE PROFILE

MSM Loss Management (MSM) is Australia's premier provider of business interruption, litigation support, claims management and related support services.

Services include preparation of economic and consequential loss claims, **material damage claims (property, fidelity)**, business valuations, policy reviews business continuity planning. The practice has focused on **material damage and business interruption**, economic loss consulting, forensic accounting and litigation support as well as providing training and compliance services. The MSM team has gained technical and practical experience through years of involvement in thousands of claims and litigated matters, across a broad range of industries, including mining, construction, metals and energy, manufacturing, hospitality and logistics. MSM has a multi-disciplined, professional team which includes chartered accountants and CPAs with experience across a diverse range of industries and organisations.

### Claim Services – including Claim Preparation

- Management, preparation, review and settlement of **material damage**, business interruption, advanced loss of profits, fidelity, product recall/liability and related claims requiring the establishment of quantum.
- Advice on business interruption and **material damage** cover including rights and obligations, policy response and a review of the adequacy of the sums insured.
- Timely advice, allowing informed decisions on critical issues such as recovery actions and options affecting the treatment of payroll.
- Claims management and **commercial disputes**
- Identification and quantification of economic losses.

### Pre-Loss Consulting Services

The pre-loss consulting services include:

- Reviewing the adequacy of declared values, limits, sub-limits and indemnity periods.
- Establishing pre-loss procedures.
- Business continuity planning.

### Litigation Support

MSM undertakes assignments on behalf of major law firms, acts as expert witnesses, and provides expert opinion and advice in a broad range of matters across a variety of industries.



For more on MSM's services, visit our website at [www.msmlm.biz](http://www.msmlm.biz)

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respective clients.

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