

INSIGHTS

FEBRUARY 2023



SELF-DRIVING REVOLUTION

How Autonomous Vehicles
Are Revolutionising Insurance

CAPTURING THE ABSTRACT

Tangible Solutions for
Intangible Risks

LEARNING FROM TRAGEDY

Role of Insurers in Disaster
Risk Management

D&O IN THE CROSSHAIRS

Understanding the Growing
Threats & Risks

Editor's Note



Although the true extent of the disaster is still unfolding, the earthquakes that hit Turkey and Syria in the early hours of February 6 and the subsequent aftershocks, are already regarded as one of the deadliest natural disasters in decades. Even though disasters are natural in origin, the severity of the impact is often exacerbated by human actions or inactions, such as poor urban planning, inadequate infrastructure, or insufficient disaster preparedness.

The February issue of INSIGHTS highlights the critical role that insurers play in disaster risk management by providing financial protection against potential losses. In this context, captives can be a valuable tool for managing and financing intangible risks of natural disasters such as earthquakes. Beyond financial protection, insurers' role in disaster risk management includes offering post-disaster support services, partnering with governments and stakeholders to develop and implement disaster risk reduction programmes, and contributing to building resilience in communities.

While it is heartbreaking to see the scale of the devastation, the loss of lives, and sufferings in Turkey and Syria; it is heartening at the same time to witness people and organisations from around the world coming together to offer relief efforts and contributions. It's important to note that ongoing relief efforts are essential beyond the immediate aftermath of the earthquake as recovery can take months or years, and continued support is vital for affected communities to rebuild and recover.

Annie Undikai
Annie Undikai
Managing Editor

IN THIS ISSUE



02 EDITOR'S NOTE

04 SELF-DRIVING REVOLUTION

Autonomous vehicles are poised to bring about a radical transformation in the transportation industry, and the insurance sector will not be left untouched by these technological advancements.

08 CAPTURING THE ABSTRACT: TANGIBLE SOLUTIONS FOR INTANGIBLE RISKS

Discover how captives can be the answer to managing and mitigating intangible risks, and understand why they are becoming increasingly critical tools for businesses in today's intricate and uncertain business landscape.

13 LEARNING FROM TRAGEDY: ROLE OF INSURERS IN DISASTER RISK MANAGEMENT

The earthquakes in Turkey highlight the importance of disaster preparedness, risk management, and the critical role of the insurance industry in mitigating catastrophe risks.

16 D&O IN THE CROSSHAIRS: UNDERSTANDING THE GROWING THREATS & RISKS

This article highlights the growing concern over D&O liability for corporate boards and their members, as well as key risk trends and drivers that could lead to potential lawsuits.





SELF-DRIVING REVOLUTION

How Autonomous Vehicles Are
Revolutionising Insurance



The emergence of autonomous vehicles is poised to disrupt the transportation industry as we know it. Self-driving cars, controlled by artificial intelligence and operating with minimal human supervision, have the potential to revolutionise how we travel: making them safer, more efficient, and more environmentally friendly.

Even though it remains unclear when fully autonomous vehicles will completely replace traditional driving, the necessary groundwork has already been made. Many of the key features that enable autonomous driving, such as front and rear crash prevention systems, ultrasound sensors, blind-spot detection, and locking-out controls, have already been integrated into commercially available cars.

The emergence and advancement of autonomous vehicles are already transforming our driving experience and this is happening even before fully autonomous vehicles become the norm.

While fully autonomous vehicles are still in the early stages of development, they are already making an impact on the insurance industry. The shift from human-driven vehicles to self-driving cars raises critical questions about liability, risk assessment, and claims management. This calls for a need to examine how autonomous vehicles are changing the face of insurance and the implications of this technology on the industry and society as a whole.

Liability and Risk Assessment

One of the most significant changes that autonomous vehicles bring to the insurance industry is in the area of liability and risk assessment. Traditionally, auto insurance policies have been based on the driver's behaviour and driving history. However, with self-driving cars, liability shifts from the driver to the manufacturer or technology provider.

In the event of an accident involving an autonomous vehicle, the question of liability will be determined by who or what caused the accident. Was it a flaw in the software or hardware, or was it a human error in the design or installation of the technology? These questions were raised after a Tesla Model S collided with a stationary fire truck in the US where the driver alleged that his car was on autopilot mode during the incident. Following this, Tesla confirmed that its autopilot feature is not intended to operate without human oversight. This occurrence emphasises the need for much clearer liability guidelines in autonomous vehicle accidents.

This liability shift implies that insurers need to adapt their policies and risk assessment models to account for new and emerging risks associated with autonomous vehicles. For instance, insurers will need to assess the safety features and performance of the technology as well as the software that powers autonomous vehicles. Additionally, insurers will need to evaluate the risks associated with cyberattacks and data breaches, which are increasingly becoming the norm with advancement in technology.



In the event of an accident involving an autonomous vehicle, the question of liability will be determined by who or what caused the accident.

Claims Management

The claims process for autonomous vehicles is likely to be different from that of human-driven cars. In the event accidents involving human-driven car occur, the insurance company will typically investigate the circumstances surrounding the accident, such as the driver's actions, road conditions, and any other relevant factors. With autonomous vehicles, however, the focus of the investigation will be on the technology and software that powers the car.

Additionally, data generated by autonomous vehicles can provide insurers with a wealth of information that can facilitate them in the investigation and handling of claims. The sensors and cameras integrated into these vehicles record detailed information related to accidents; including vehicle speed, the distance between the vehicles involved, and pre-accident actions. With this data, insurers can determine liability and process claims more efficiently.

Product Innovation

The emergence of autonomous vehicles also creates opportunities for insurers to innovate and develop new insurance products. For example, as liability shifts from the driver to the manufacturer or technology provider, there may be a need for product liability insurance to cover any defects or malfunctions in the technology or software that powers autonomous vehicles.

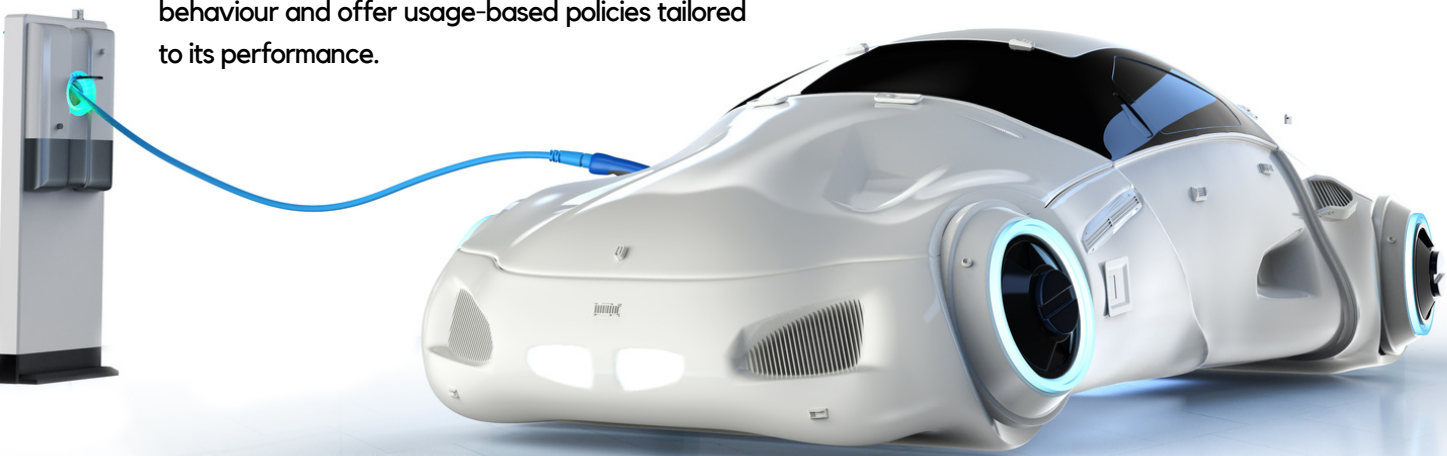
Insurers can develop usage-based insurance products that incorporate the driving patterns of autonomous vehicles. These insurance policies provide a customised insurance experience in which drivers are charged premiums based on their driving habits, such as the distance they cover and their driving speed. With autonomous vehicles, insurers can track the vehicle's driving behaviour and offer usage-based policies tailored to its performance.

The Future of Insurance

The rise of autonomous vehicles is set to have a profound impact on the insurance sector. Insurers must prepare to adapt their policies, risk assessment models, and claims processes to keep pace with this new technology.

As autonomous vehicles become widespread, insurers will have to develop new products and services to meet the changing needs of their customers and ensure that they can continue to provide coverage in an ever-evolving transportation landscape. While the full impact of autonomous vehicles on insurance is yet to be realised, one thing is clear: the insurance industry is on the brink of a major transformation that will shape the future of mobility.

With autonomous vehicles, insurers can track the vehicle's driving behaviour and offer usage-based policies tailored to its performance.



CAPTURING THE ABSTRACT:

TANGIBLE SOLUTIONS FOR INTANGIBLE RISKS

Intangible risks have become an increasingly prevalent threat to companies, and captives can be an effective way to manage and mitigate these risks.

As businesses become increasingly digitised and interconnected, the risks they face are also changing. Intangible risks such as climate change, brand reputation and intellectual property disputes have become a growing concern for companies worldwide. These risks are not easily quantifiable or predictable and can result in significant financial losses and damage to a company's reputation. In response, many businesses are turning to captive insurance as an effective way to manage and mitigate these intangible risks.

Captives offer a unique opportunity for businesses to take control of their risk management strategy and tailor coverage to their specific needs. In this article, we will explore how captives can provide a solution for managing and mitigating intangible risks and why they are becoming essential tools for businesses in today's complex and uncertain business environment.



Intangible assets are rapidly becoming the dominant source of economic value for global companies, with investments in these assets steadily increasing.



Intangible Risk A Tangible Threat

Intangible risks refer to risks that cannot be easily quantified or measured, such as reputational risk, cyber risk, or intellectual property risk. These risks have become increasingly important in today's business landscape as the global economy has shifted from industrial-based to service and knowledge-based.

The global pandemic and current economic environment have amplified the reliance on digital technologies and exposed pre-existing vulnerabilities in an interconnected global economy. These have led to a marked shift in risk perceptions as non-physical loss scenarios have moved from theoretical to the real world.

Intangible assets are rapidly becoming the dominant source of economic value for global companies, with investments in these assets steadily increasing. Analysis by Howden indicates that intangibles now account for nearly 70% of the total business value of the world's largest 50 corporations, amounting to about US\$11 trillion¹. Just like physical assets, they need to be protected.

Managing intangible risks is complex due to difficulties in evaluating and quantifying their potential impact, which is often subjective and based on assumptions about future income. This makes identifying, managing, and mitigating intangible risks crucial because they can substantially impact a company's financial performance, operations, and reputation. Captives can address many of the challenges that traditional market face when looking at intangible risks.

¹<https://www.raconteur.net/sponsored/building-resilience-what-are-the-top-five-operational-risks-for-financial-services-firms/>

The Intangible Risks of Climate Change

Climate change is a prime example of an intangible risk. The risks associated with climate change are not immediately apparent or tangible, yet they can have significant economic, social, and environmental consequences. Climate change can cause extreme weather events, such as floods, droughts, and heat waves, which can lead to property damage, crop failures, and loss of life. Climate change can also lead to changes in the availability of resources, such as water and food, which can have far-reaching consequences for communities and economies.

One advantage of captives is that they can be tailored to the specific needs of a business. This means that captives can be designed to provide coverage for risks associated with climate change, such as property damage from extreme weather events, business interruption from flooding or other climate-related events, and liability for climate-related damage. Businesses that are vulnerable to climate-related risks can benefit from the use of captives as a way to manage these risks and contribute to the fight against climate change.

A key litigation challenge faced by captives in the context of climate change is greenwashing. Greenwashing refers to the practice of making false or misleading claims about a company's environmental credentials. Captive owners need to ensure that their coverage is effective in protecting the parent company against potential legal action related to greenwashing claims.

Intellectual Property

IP infringement Poses Significant Risk

Intellectual property (IP) risks have become a growing concern for companies across various industries. These risks arise from the potential infringement of IP rights, such as patents, trademarks, and copyrights, which can lead to costly litigation, reputational damage, and loss of revenue.

IP infringement is a top concern for many companies, but the lack of insurance results in a significant coverage gap with an average potential loss exceeding \$1 billion.² Insurers have struggled to keep pace with the rapidly evolving nature of IP assets, the challenges associated with valuing them, and the lack of historical loss data.

Even though commercial insurance provides coverage for various risks, it has its limitations in responding to sudden shifts and changes, as well as in providing coverage for the many covert risks that businesses encounter during their regular operations. This is where captives

²<https://riskandinsurance.com/intellectual-property-insurance/-are-the-top-five-operational-risks-for-financial-services-firms/>

can be advantageous, as they can function as a reserve of funds that the parent company can draw on in the event of a crisis or in the theft of valuable intellectual property.

Insuring Brand and Reputation

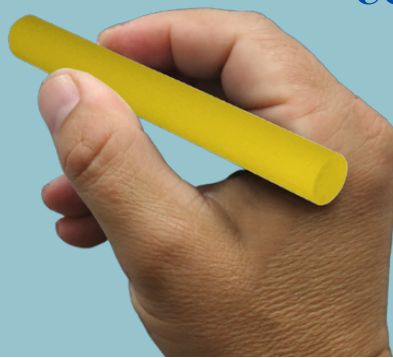
In today's global and interconnected world, the impact of a negative event on a business's reputation can be catastrophic. The era of the digital age has enabled information to be shared instantaneously and with a broader reach than ever before. Reputational damage from a cyber attack, industrial accident, or PR blunder can quickly spread due to the speed and outreach of digital communication channels.

Social media platforms, news websites, blogs, and other online sources can quickly amplify negative news and commentary, potentially reaching millions of people within hours. This can result in significant harm to a company's brand reputation and could lead to lost revenue, decreased customer trust and loyalty, and even legal and regulatory consequences. In some cases, the reputational damage can be irreversible.

Speed is crucial in managing intangible risks. If left unchecked, it can result in significant damage, particularly when the company's reputation is at risk. Warren Buffett famously said, "It takes 20 years to build a reputation and five minutes to ruin it." Captives can provide coverage that enables the company to immediately deploy crisis management experts to limit the magnitude and duration of the damages when something triggers a wave of negative publicity. This capability allows the company to effectively cap the extent and scale of damages that may incur.

While responding promptly and appropriately is crucial, insuring brand and reputation risks is challenging due to their intangible nature. In this regard, captives provide an alternative insurance option that can address the intangible nature of these risks.

Reputational damage from a cyber attack, industrial accident, or PR blunder can quickly spread due to the speed and outreach of digital communication channels.



Captives play a crucial role in managing reputational risk by an "arms-length" risk management practice that safeguards the reputation of the parent company. As captives operate independently from the parent company, with their board of directors, management team, and risk management practices, this separation ensures that decisions related to reputational risk are made objectively and without undue influence from the parent company.

Cyber Risk on the Radar

Cyber risk is one of the fastest-growing intangible risks and has become a significant concern for companies in recent years. Data breaches, cyber-attacks, and other cyber incidents can cause substantial financial losses, reputational damage, and legal liabilities. To mitigate these risks, companies are turning to captives for cyber risk insurance.

One of the main advantages is that captives can offer more comprehensive coverage than traditional insurance policies. Captives can be tailored to cover specific cyber risks including data breaches, cyber-attacks, and other cyber events. Hence, businesses are able to adapt their insurance coverage to their unique needs and risks.

Captives can serve as a "risk incubator" for cyber threats, using the information obtained to improve the understanding of the exposure and make informed decisions on risk management and financing.³ This assumption is, however, based on the occurrence of claims. If claims do not happen, there may be limited opportunities to learn. Nevertheless, retaining the risk can help businesses focus more on managing cyber risk.

Getting a Grip on Intangible Risks


In addition to insurance coverage, captives can be utilised to finance intangible risks. For example, a captive can be used to fund the costs associated with a legal dispute or a data breach, which would enable companies to manage their cash flow effectively and mitigate the financial impact of intangible risks.

Overall, captives can be valuable tools for managing and financing intangible risks. By providing customised insurance coverage and financing solutions, captives can help companies better manage their exposure to these risks and protect their bottom line.

Captives play a crucial role in managing reputational risk by an "arms-length" risk management practice that safeguards the reputation of the parent company.

³ Aon. (2020). Global Risk Management Survey Report. Retrieved from <https://www.aon.com/getmedia/f37a754b-411c-4e45-a16e-8a18ab6e600f/Aon-Global-Risk-Management-Survey-Report-2020.aspx>

LEARNING FROM TRAGEDY: ROLE OF INSURERS IN DISASTER RISK MANAGEMENT



The southeastern region of Turkey was left in ruins by a sequence of powerful tremors and aftershocks that occurred after two major earthquakes on February 6, resulting in a death toll of over 43,000. The severity and extent of the damage have shocked the world, with tragic impacts on the affected communities. The earthquakes have affected and displaced 13 million people and caused extensive damage to buildings and infrastructure across ten provinces in Turkey.

As the dust settled on the rubble of Turkish cities, we examine the role of insurers in managing and mitigating catastrophe risks. The role of insurance in disaster risk management is multifaceted. Insurance companies provide critical support in identifying risks, promoting risk reduction measures, providing resources for emergency response efforts, and supporting post-disaster recovery efforts.

Insurance plays a critical role in promoting disaster resilience. It provides financial protection to insureds, preventing negative economic hardship after a disaster by providing a mechanism for individuals and businesses to transfer the risk of potential losses to insurers. This transfer of risk allows them to protect themselves from financial losses associated with disasters.

In the aftermath of a disaster, insurance has a vital role in helping communities recover. While insurance cannot prevent disasters from occurring, it can help reduce the financial burden that comes with recovery efforts. By providing financial support for recovery efforts, insurance companies can help accelerate the recovery process, reducing the economic and social impacts of disasters. Moreover, insurance can help promote risk reduction measures before a disaster occurs by offering financial incentives to encourage individuals and businesses to take necessary precautions.

In Turkey, the government set up the Turkish Catastrophe Insurance Pool (TCIP) designed to provide coverage for damages caused by natural disasters, such as earthquakes, floods,

and landslides. TCIP was established in 2000 after a major earthquake in Turkey resulted in significant financial losses and highlighted the need for a comprehensive insurance system for natural disasters. The pool is funded through contributions from insurers and it operates as a reinsurance facility that can absorb a portion of the losses incurred by insurers in the event of a catastrophic event.

According to government officials, the TCIP has disbursed approximately TRY520m (\$27.6m) in compensation payments to policyholders whose homes were destroyed in the recent earthquakes. Official estimates indicate that about 1.13 million TCIP policies are in force in the earthquake-affected region of southern Turkey, which represents 50% of the region's residential properties.

In addition, TARSIM (Agricultural Insurance Pool) has disbursed nearly TRY3m in compensation for crop and livestock losses in the affected region. The agricultural pool was established in 2005 to provide insurance coverage to farmers against risks related to agricultural production, such as drought, frost, hail, flood, fire, disease, and pest attacks.

While insurance cannot prevent disasters from occurring, it can help to reduce the financial burden that comes with recovery efforts.

However, the insurance industry's contribution to managing disaster risk extends well beyond financial protection. For instance, insurance can support disaster preparedness by supplying resources for emergency response efforts. Many insurance companies have disaster response teams in place to help coordinate their response efforts. They may also work closely with government agencies and other organisations to ensure a coordinated and effective response.

Insurers can directly finance disaster relief efforts or partner with disaster response organisations to supply resources and extend assistance. This can entail providing temporary shelter for people displaced by a disaster, donating supplies and equipment to first responders, or providing logistical aid.

In the wake of the recent earthquakes in Turkey, insurance companies can play a critical role in promoting community resilience by partnering with local governments and community organisations to identify vulnerabilities and develop plans to strengthen resilience. For example, insurance can

work with local government officials to assess the earthquake risk in certain areas and recommend improvements in building codes, infrastructure, and early warning systems.

Insurers can also invest in community resilience measures such as public education and community-wide risk reduction programmes. Public education campaigns can help to raise awareness about earthquake preparedness and safety measures. Community-wide risk reduction programmes can encourage community members to take steps to reduce their risk of loss from earthquakes by retrofitting their homes, securing loose objects, and creating emergency kits.

The devastating earthquakes in Turkey serve as a stark reminder that the threat of natural disasters can strike at any moment and without warning, and that being prepared and having effective disaster risk management strategies in place are crucial for protecting lives and communities. However, the events have also proved that the insurance industry can function effectively, even in extreme occurrences, and that the industry plays a key role in disaster risk management.



D&O IN THE CROSSHAIRS

UNDERSTANDING THE GROWING THREATS & RISKS

As companies face increasingly complex challenges, the role of directors and officers (D&O) in safeguarding their organisations becomes more critical. However, with this growing responsibility comes a growing risk of litigation. In recent years, D&O liability has become a significant concern for corporate boards and their members, as they face a range of legal and regulatory risks. This article explores some key risk trends in D&O and identifies the main drivers of potential lawsuits against companies and their board of directors.

One of the most significant drivers of D&O risk is the rapidly changing regulatory environment. Companies face increasing regulatory scrutiny in areas such as data privacy, environmental protection, and financial reporting. In response, regulators are cracking down on non-compliance with tougher fines and penalties, and shareholders are more likely to bring lawsuits against companies and their directors and officers for non-compliance.

In 2020, a financial institution was fined \$1 billion by regulators for violating anti-money laundering laws. The company's directors and officers were held responsible for the failure to comply with regulations, leading to significant D&O risk and legal action by shareholders.

Environmental risks are also a growing source of D&O liability. Companies and their D&O can be held responsible for environmental violations, including pollution, hazardous waste disposal, and climate change. As climate change continues to pose a significant threat to the environment, companies are under increasing pressure to take action to reduce their carbon footprint and other environmental impacts. As a result, greenwashing activities, in which companies make misleading or false claims about their ESG efforts, are becoming prevalent.

An example of D&O liability and greenwashing involves a clothing retailer that was sued by the Federal Trade Commission (FTC) for making false and misleading claims about the environmental benefits of its products. The company had marketed its clothing as made from recycled materials, when in fact only a small percentage were recycled. The FTC held its D&O responsible for the deception, resulting in a settlement and changes to the company's marketing practices.

The use of digital technologies has become increasingly widespread in today's business landscape, with companies relying on these tools to manage their operations, store sensitive data, and engage with customers. However, digital transformation has also made them more vulnerable to cyber threats, including data breaches, hacking, phishing and malware attacks.

D&O liability in the context of cyber threats can arise in several ways. For example, if a company suffers a data breach due to the lack of appropriate cybersecurity measures, shareholders may sue the company's directors and officers for breaching their fiduciary duty. Similarly, regulators may impose fines or penalties on D&O for failing to comply with cybersecurity regulations.

In 2022, the former Chief Security Officer of Uber was convicted of criminal obstruction charges for failing to report a cyber breach to the authorities. In another instance, the CEO of an online beverage delivery company based in the US was held responsible by the FTC for the company's security lapses that resulted in a cyber breach, exposing the personal data of 2.5 million customers.

Trends in D&O liability are influenced by multiple factors, including regulatory changes, cyber threats, and environmental risks. As companies navigate these risks, they must take steps to mitigate D&O liability, including implementing robust compliance programmes, regularly assessing risk exposures, and purchasing D&O insurance coverage. By doing so, companies can protect themselves and their directors and officers from potential lawsuits and other legal actions.

