We hope that you will enjoy this edition of the EOS RISQ report. We feature articles covering a wide range of topics all of which relate to the increasingly complex risks that face businesses and the opportunities that these complexities create for brokers as advisors and advocates to their clients.

Unlike the WTC loss in 2001, the ferocious hurricanes that took place last year around the Gulf of Mexico and which caused such widespread devastation both to property and to the population in the vicinity, have not resulted in a uniform increase in rates as occurred after WTC despite the aggregate quantums of loss being higher than WTC.

The upward pressure on rates has been predominantly limited to certain classes of insurance and reinsurance, in particular those that produced the losses and to catastrophe programmes with high windstorm exposures. In most other classes and territories, clients continue to achieve rate reductions and capacity is sufficient for all but the largest of risks.

EOS RISQ has continued its expansion during the past 6 months with the opening of an office in Russia and this report carries a profile of that new initiative. We look forward to expanding our presence in this important world economy.

The increasing tendency for corporations to expand their activities internationally is generating insurance needs and advice that traditionally have only been required by the larger global or international companies. The ability of corporations to gain a competitive advantage by either outsourcing or relocating parts of their businesses to lower cost environments provide us our international alliance with an opportunity to prove our value to our customers providing local knowledge and solutions under the umbrella of internationally agreed service standards and operating procedures.

We hope you enjoy this addition of the EOS RISQ report and will not hesitate to contact us around any risk issues on which you have any concern.

Wishing you all the best,

John Percy-Davis
Chairman EOS RISQ
The quality of medical care in diagnostics, therapy and care has been continuously improved in the course of recent years by implementation of manifold external and especially internal measures. This is essential in times of economisation, rationalisation and globalisation. The number of reported liability losses claimed by patients against hospitals parallels the quality-improvement campaign and establishment of certification procedures, and reaches record level. Today's hospital patients are increasingly informed and capable of criticism, and are not willing to accept the outcomes of modern medicine science as being fate. They articulate their expectations for medicine and care, and object alleged malfeasance. In future, these patients will read up more on preventive standards, assumedly more than they will catch up on quality management and certification.

The number of reported liability losses claimed by patients against hospitals parallels the quality-improvement campaign and establishment of certification procedures, and reaches record level.

The players in healthcare - physicians in the first instance – ought to respond the claims development, which constitutes another trend causing concern, with the implementation of prevention measures in terms of risk management. Statistics show that allegations of error in treatment are without legal cause in many cases. One third of claims is settled, two thirds are filed away without assuming any liability. This constant level extends over several years.

Nonetheless, each reported allegation involves time-consuming investigations, hearings and entails analysis efforts for the accused. The situation becomes particularly tragic for clinics, if potential allegations of error in treatment are passed to the blaze of publicity and the media becomes interested. This could nullify the longstanding efforts to create a positive image in a short time. There are numerous examples of it – and a reversal of this trend is not expected.

Risk management is nothing new! Daily team meetings, ward rounds, mortality conferences etc. are measures of prevention that belong in variable degrees to the repertoire of therapeutic teams in every specialist department. Methodical risk management surveys structures, processes and results of medical and care procedures from the perspective of former claims. It concerns prophylactic strategies for error prevention and thus, reduction of forensic risks by gathering existing weak points and potential losses.

If not before, it is then, when losses occur, that risks of clinics or specialist departments become known – it is easy to be wise after the event – but then it is too late. Professional risk management capitalises on an ample wealth of experience gathered from incidents that occurred in other comparable facilities. These experiences and their derivable prevention measures are passed on to the clinic staff during the implementation of risk management processes.

Risk Management Process

The development and implementation process of a risk management system consists of four steps. The phase of risk identification is followed by risk assessment. This is followed by risk handling and implementation of appropriate actions for the optimisation of the safety level. After implementation of these steps, known and reorganised risks are controlled through the determination of suitable supervision parameters for risk monitoring and controlling. This risk management process basically matches the PDCA – cycle [plan, do, check & act], which is known from the quality doctrine.

Essential, real and looming risks are defined for the respective clinic or specialist department and its medical focus during the phase of Risk Identification. In anaesthetics, these are for example risks of misintubation, or problems with false diagnosis regarding emergencies in accident surgery, or misapplication of chemotherapeutica in oncology. These are examples deriving from loss experience for specific risks. The threat potential equals the menace to the care mission. Risk identification
requires attentiveness, consciousness and sensitisation of all involved members of a therapeutic team; it is not only the responsibility of physicians, but also a task for the nursing care and medical assistance professions. Staff members usually know the thread potentials of their direct working area through their vocational education, further trainings, and last but not least through their work experience. However, risks seem to be controllable due to certain routine processes that emerge, especially, if risks have not resulted in losses in the past. Therefore, it is important to take the opportunity for unreserved and self-critical reflection, which is offered during the phase of risk identification. It must not be affected by hierarchic structures and other disruptive factors.

Potential consequences of identified risks are quantified in the Risk Assessment phase. The degree of risk is assessed by quantifying the probability of occurrence and the size of potential loss involved. The outcome is shown in a simple two-dimensional risk-portfolio-scheme, for example:

The area between the opposing poles of loss potential and occurrence probability shows the therapeutic team the need for action. The assessment of identified risks ignites a fruitful interaction process, and mostly a practicable solution is being elaborated at its final stage.

Risk Handling constitutes phase 3 of the risk management process. The task is to draw consequences from the risks that were previously identified and assessed.

Manifold measures, which have been defined in line with risk identification and assessment, become effective as risk handling strategies:

Examples for department-specific risks in

...surgical care
• Development and implementation of requirements-oriented, pre-operative preparation standards.
• Continuous medical device-related training and instruction.

...in-patient care
• Establishment of scoring systems for the risk of patient fall and decubitus ulcer.
• Development of interdisciplinary treatment paths.

...emergency care
• Resuscitation trainings for all therapeutic team members and interactive CRM measures (Crew Resource Management).
• Continuous critical retrospective analyses of emergency missions.

...anaesthetics
• Provision of centrally available material sets for complicated intubations, and training of employees.
• Development of interdisciplinary association / enlistment rules.

From medical everyday life it is known that sources of incidents, complications and losses are multifactorial. Misinterpretations, lacks of attention and misunderstandings add up to a constellation, that overrides the established safety barriers. The meanwhile well-known ‘Swiss-Cheese-Scheme’ adapted from Reason, illustrates, that single holes in a multifaceted safety net are non-effective, but that holes fatefully correspondent to one another will cause the unintentional result. This visualization may be employed in a useful way in order to create risk awareness and to control risks and hazards in the risk management process.

Considering, for example the problem of wrong-side surgery in surgical care, safety barriers are established in all clinics; however, in a differently developed manner and pervasion. In risk management it is to question for example, whether:
• the surgeon knows the patient to be operated on;
• the surgical area is adequately marked where appropriate;
• the patient is adequately interviewed before anaesthesia;
• a suitable identification system is provided.

Clinic-wide Risks

Not only discipline-specific risks, but also perils that are irrespective of specialist departments and which require a preventive concept for the entire clinic, are revealed by each analysis performed on risk management grounds. Over the past years, media have shown a continuously growing interest in the topic ‘medical malpractice in hospitals’. This has brought vexatious experiences to some clinics that have been through the mills of journalism without chance of an unbiased, objective statement.
Risk management also provides preventive training measures for this purpose, such as:

- writing press releases;
- simulation of press conferences;
- creation of a code of practice for the 'case of media emergency';
- pre-test interviews for live performances;
- clinic-internal information activities.

A strength and weakness analysis of the hospital’s public relations section is required in the course of the risk management process implementation. The phase of **risk monitoring** completes the risk management process. The effectiveness of newly defined safety measures is to be monitored continuously, and as the case may be modifications have to be accomplished where necessary. To do so, appropriate instruments are inevitable. This particularly comprises a continuous loss monitoring including causation assessment and return information to the persons involved.

**A sustainable consciousness for risks and perils has to be achieved in clinical care.**

A CIRS (Critical Incident Reporting System) should be installed and trained, as it is an effective instrument, that allows for identification of known and unknown risks. This procedure gathers near losses, i.e. incidents, which had the potential to lead to an undesirable outcome if left to progress (e.g. malfunction of an alerting system and as a consequence thereof, physician was not reached). The awareness that critical incidents, slight and severe complications, as well as serious losses are associated with each other, forms the basis of such a system. The systematic examination of critical incidents without consequences of loss and identification of its causation may help prevent potential real losses by introduction of adequate prevention measures. A comprehensive risk survey and reorganisation, i.e. implementation of the entire risk management process is inevitable, as otherwise the introduction of a CIRS may be ineffective. Initially, a process of growing consciousness has to be started. Members of the therapeutic team screen their respective fields of activities under the aspect of risks, and introduce preventive measures during this process. The process of growing consciousness may be followed by CIRS for stabilisation and completion purposes.

**Conclusion**

Staff members of clinics have to keep pace with the rapid development of medical science, but their possibilities are restricted by legal practice and claims settlement. Moving within this field of tension requires medical and legal expertise.

Risk management is based on four pillars:

- efficient documentation on services rendered in diagnostics, therapy and care;
- extensive patient education and information;
- organisation of work flow;
- proper and professional treatment.

A sustainable consciousness for risks and perils has to be achieved in clinical care. A comprehensive approach, which embraces all occupational groups beyond hierarchy levels, and the understanding for risk reduction, which was elaborated in these groups lead to the fact, that sensitive work processes are not only eyed from the medical and economic perspective, but also from the liability-relevant point of view.

Normally, clinics dispose of a tight network of safety barriers, and of a critical incident instrument by implementing a house risk management system (e.g. the software riskop).

Liability insurers of hospitals increasingly ask for evidence of prevention measures for the elevation of patient safety, as precondition for risk coverage.

A clinic-wide risk management concept that is integrated into the quality management structures, offers a distinguished chance to visualise measures of risk prevention and, last but not least, its demonstration to patients.

---

**Contact**

Peter Gausmann  
Klingenbergstraße 4  
32758 Detmold  
Germany  
E-mail: pgausmann@grb.de
GDP – Size and Growth Rate

One of the biggest questions absorbing the minds of today’s economists is: “When will China’s economy be as big as that of the United States?” Based upon available historical economic data and patterns of people development, it might reasonably be estimated that the Chinese economy will achieve this sometime between 2012 and 2016. Per capita GDP, however, it is not likely to approach that of the US until decades later.

These projections may be somewhat on the optimistic side because they take no account of the potentially negative impact of constraints in resources such as energy, clean water supply and improved air quality. Without proper management of these fundamentals, economic growth will arguably fail economists’ brightest expectations. Indeed, many Chinese businessmen believe that environmental issues will ultimately prove to be China’s Achilles’ heel.

From published data, China’s cumulative GDP growth over the period 1978 to 2002 was 814%. Extrapolating this data using various tried and tested economic models produces an average annual growth rate in GDP of between 6% and 10% for the period 2003 to 2025. If true, this means that by 2025, China’s economy will be nine times as large as it is today.

Many Chinese businessmen believe that environmental issues will ultimately prove to be China’s Achilles’ heel.

There are, however, less optimistic views out there. Some economists predict average annual GDP growth during the next ten years to be less than 5%, although this can probably be considered the worst-case scenario. These observers cite the accumulation of inventory and transition from export-oriented to domestic consumption-based growth as the main issues for China to successfully manage.

However even the pessimists, whilst predicting a slowdown in the short term, still consider longer term prospects to be good, due principally to the continued supply of cheap labour and the existence and further development of first-world infrastructure such as transportation and port facilities.

Structure of the Economy

“China’s economy is not booming – the world economy is booming in China.”

Foreign participation in the Chinese economy is remarkably high, despite the fact that common wisdom would suggest that it has long been closed to foreign participation. Consider the following OECD figures, giving the share of the three sectors in China’s economy, and ask yourself how they would have compared with similar analyses at the same stages of development of, say, the Japanese and Korean economies:

<table>
<thead>
<tr>
<th>Sector</th>
<th>1998</th>
<th>2003</th>
<th>2005 (est)</th>
</tr>
</thead>
<tbody>
<tr>
<td>State</td>
<td>47%</td>
<td>36%</td>
<td>31%</td>
</tr>
<tr>
<td>Private Domestic</td>
<td>35%</td>
<td>42%</td>
<td>45%</td>
</tr>
<tr>
<td>Foreign</td>
<td>18%</td>
<td>22%</td>
<td>24%</td>
</tr>
</tbody>
</table>

[It should however be remembered that Taiwan and Hong Kong are considered foreign in this analysis and that almost half the foreign participation described would relate to investment from these two sources.]

Foreign companies operating in China today produce 87% of the country’s high-tech exports and 60% of exports overall. Whereas in terms of industrial manufacturing foreign participation appears to have reached a plateau (due largely to the rise of private domestic manufacturing), foreign-produced exports from China are still growing in absolute terms. This suggests they must be moving upwards into higher-value products and services.

The above data also tell us that domestically there has been a reversal of the balance between state and private sector participation in the economy, which has resulted in increased productivity. There is still however an enormous amount of state-owned enterprise that could be privatized, with consequent improvements in efficiency.
**Future Growth Areas of the Chinese Economy**

“Will the world continue to absorb China-made products?”

There is currently such a huge stockpile of unsold PRC manufactures that arguably the world has already reached saturation point.

China’s mushrooming inventories, the product of government-sponsored overproduction aimed arguably at bolstering GDP at all costs, are estimated to represent one-quarter of GDP growth in recent years. Their distribution “could cause one or two quarters of negative growth in the near future,” according to one economist recently.

China’s future lies in the development of non-industrial, higher value products and services such as health and medical, technology development and money management.

All of this nonetheless belies a temptation for us to continue thinking as if we are living in the 19th century; whereas China’s future, even in the relatively medium term, almost certainly lies in the development of non-industrial, higher value products and services such as health and medical, technology development and money management.

**Impact of China’s Growth on the World Economy**

China’s entry into the global economy as a major source of low-cost manufacturing is a continuing threat to other countries whose economies likewise rely upon industrial manufacturing. Hence Japan, Korea and parts of continental Europe such as Germany and France will be among those most affected. Down globally (the so-called ‘China price’) and through increasing demand pushes up the price of raw materials.

The more service-oriented economies such as US and UK are to some extent less affected by China’s phenomenal growth. However, in the final analysis China may still be judged guilty of a global erosion of manufacturing profitability.

These countries face a ‘triple whammy’ as China imports less of their products, pushes the price of manufactures.

For Asian countries, many of which are raw-materials suppliers, China’s move into export-oriented manufacture has been beneficial. In fact, two-thirds of China’s imports are sourced from within Asia and its growth has helped ‘pull along’ Asia’s developing economies such as Indonesia and Vietnam.

**Global Profit Warning?**

“China will drive a slowdown in global profits.”

**China’s Share of World Manufacturing**

<table>
<thead>
<tr>
<th>Year</th>
<th>Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>1800</td>
<td>0%</td>
</tr>
<tr>
<td>1950</td>
<td>&lt;1%</td>
</tr>
<tr>
<td>2005</td>
<td>9%</td>
</tr>
<tr>
<td>2030</td>
<td>20%?</td>
</tr>
</tbody>
</table>

China’s share of global manufacturing will, by some estimates, more than double in the next 25 years. Some economists believe that this growth is ‘virtually unstoppable’ as a package of third-world labour costs and first-world infrastructure combine to deliver unbeatable value to global consumers.

As ever, there are alternative views on how China’s place in the world economy will develop and not all predict such a rosy future. For example, if the Chinese Yen — or Renminbi — is allowed to find its own value, then some of China’s comparative advantage, such as cheap labour costs, will likely be eroded. In the words of one economist:

“China’s competitive advantage arises because it is the cheapest place on earth to make things at the moment. The emerging platform companies are well-equipped to move their manufacturing at a stroke to the world’s latest, cheapest place…”

**Human Resources**

There are many who believe that China’s continued economic growth will be a function of ‘people.

<table>
<thead>
<tr>
<th>Cause</th>
<th>Effect</th>
<th>Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic oversupply of industrial manufactures</td>
<td>Reduced requirement for foreign imports</td>
<td>Foreign manufacturers export less product to China</td>
</tr>
<tr>
<td>Domestic manufacturers seek to increase exports as local consumption reaches saturation</td>
<td>Global prices pushed down as Chinese manufactures flood market – the so-called ‘China Price’</td>
<td>Profitability declines as the global market tries to compete with Chinese product</td>
</tr>
<tr>
<td>Growth in demand for raw materials to support increased export-oriented production</td>
<td>Price of raw materials increases</td>
<td>Profitability further declines</td>
</tr>
</tbody>
</table>
development’. The simple fact is that the huge number of people in this most populous of nations has long been hypnotic to outsiders.

However, the population of China is aging rapidly: throughout the world, only Japan has an older population. The rapid decline in the birth rate in China is not something that will be easy to reverse.

China’s population data, of which the year 2000 census would be the latest example, suggests that there are on average 17 million new births per annum. However, recent ministry of education data supports a growing suspicion that there has been a rapid decline in the birth rate in recent years.

Trends in the available data also suggest the following:

- for the last ten years there have been, on average, an additional 8 million new workers entering the market each year;
- for the next ten years, on average, there will be no net growth;
- China’s population will continue to grow until 2015, from when it will stabilize and then diminish;
- its labour force will be in decline from 2009.

In short, therefore, these trends indicate that within the next quarter century, the number of educated people entering the workforce will diminish, as well as the size of China’s labour force overall. With it, a large part of China’s comparative advantage will be eroded.

Summary – China’s Growth Will Decelerate

So what does the future hold?

“There are many things that cannot be imagined, but there is nothing that may not happen,” is perhaps an appropriate Chinese saying, for even a panel of informed economists would find difficulty agreeing on China’s likely position in the world economy 20 years from now.

But there are some common areas of thinking:

- economic growth will increasingly be driven by domestic consumption and no longer rely almost entirely upon export-oriented investment;
- however, accumulation of inventory (domestic oversupply) will persist;
- there will be a tightening of money supply with Chinese companies having to adapt to a scenario whereby the cost of capital is higher;
- China will continue to drive down global profitability;
- China’s population and workforce will peak at some point between 2009 and 2015, then diminish;
- China’s growth will begin to decelerate, sometime soon.
Impact of new Chinese Business Insurance Legislation

EOS RISQ UK – Kirk Austin

New insurance business legislation has recently been enacted in China that has implications for clients of the EOS RISQ network and other partner brokers.

Effective 1 December 2005, the new legislation governs the way in which domestic insurance companies may reinsure and seeks to restrict the outflow of reinsurance premiums abroad. Through this the Chinese insurance regulator, CIRC, aims to assist the development of the local reinsurance industry.

The new rules apply equally to local Chinese direct writers, Sino-foreign joint ventures and subsidiaries and branches of foreign insurance companies. All modes of reinsurance business fall within its scope, including facultative placements and treaty reinsurance arrangements.

New legislation governs the way in which domestic insurance companies may reinsure and seeks to restrict the outflow of reinsurance premiums abroad.

The salient features of the new legislation are as follows:

- Direct insurers are instructed to give priority to China-domiciled reinsurers when entering into reinsurance arrangements.
- At least two domestic companies must be invited to participate in any reinsurance offering.
- At least 50% of any reinsurance placement should be effected with China-domiciled reinsurers.
- No more than 80% of any reinsurance placement may be effected with the same reinsurer.
- No more than 20% of any reinsurance placement may be effected with a reinsurer that is affiliated to the cedant.

What this means for the China-based operations of clients of the EOS RISQ network is that they will now have less flexibility over the design and control of their risk financing arrangements. For example, cessions to captive insurance companies through fronting agreements will henceforth come under close scrutiny and may well be restricted. There may also be security (rating) issues, which we are evaluating.

The penalties for non-compliance with the new directive include, in extreme cases, withdrawal of licence and suspension of business activities and as a result domestic insurers have initially indicated to EOS RISQ that they intend to fully comply with the legislation.

However, we have yet to see in practice how Chinese insurers will react in relation to their future handling of global insurance programmes and will keep our network partners informed of developments in the coming months.
How can the avian flu affect your business?

EOS RISQ Italy – Marketing and Communication Division

An avian flu pandemic could leave employers with decimated workforces and a host of insurance coverage questions, while insurers could suffer billions of dollars in losses. This is one of the alarming conclusions of an inquiry of EOS RISQ Italy on insurance consequences of an avian flu pandemic.

What is avian flu?

Avian influenza, or “bird flu” is a contagious disease of animals caused by viruses that normally infect only birds and, less commonly, pigs. The most important control measures of avian influenza are rapid destruction of all infected or exposed birds.

Particularly alarming, in terms of risks for human health, is the detection of a highly pathogenic strain, known as “HSN1”, as the cause of most of these outbreaks. HSN1 has a unique capability to jump the species barrier, causing severe disease, with high mortality, in humans.

Avian and human influenza viruses can exchange genes when a person is simultaneously infected with viruses from both species.

A new ‘mixed’ virus is different from either parent virus, and humans may have no immunity to it. And if the new virus contains sufficient human genes, transmission directly from one person to another (instead of from birds to human only) could occur. When this happens, the conditions of the start of a new influenza pandemic will have been met.

There were three influenza pandemics in the 20th century:
- 1918 Spanish flu - 20-40 million deaths worldwide;
- 1957 Asian flu - 70,000 deaths in the U.S. alone;
- 1968 Hong Kong flu - 34,000 deaths in the U.S. alone.

Both 1957 and 1968 pandemic viruses were a result of the re-assortment of a human virus with an avian influenza virus. The origin of the 1918 pandemic virus is not clear.

As reported by World Health Organisation (WHO), public health preparedness activities are:
- officials from the WHO are working across Asia to assist in establishing an extensive surveillance network to provide early warning;
- fewer than 10 countries are working on vaccines;
- Roche has committed to give WHO three million antiviral drug doses (Tamiflu);
- 23 countries have ordered drug stockpiles: delivery will take up to a year;
- about half of all countries now have a formal pandemic control plan.

WHO activities in Europe

As of 4 March 2006, sixteen countries within the WHO European Region have reported confirmed cases of avian influenza H5N1 in birds to the World Organisation for Animal Health (OIE): Austria, Azerbaijan, Bulgaria, Croatia, France, Germany, Greece, Hungary, Italy, Kazakhstan, Romania, Russia, Slovakia, Slovenia, Turkey and Ukraine. Three European countries have reported avian influenza H5 in birds to the OIE: Bosnia and Herzegovina, Serbia and Montenegro and Switzerland.

WHO experts are contributing to preparing integrated project proposals for the Global Programme for Avian Influenza and Human Pandemic Preparedness and Response (GPAI), which provides financial and technical assistance to individual countries. GPAI is funded by lines-of-credit from the World Bank and is coordinated with many other partners, including USAID, UNICEF, OIE and the Food and Agriculture Organisation of the United Nations (FAO).

An avian flu pandemic could leave employers with decimated workforces and a host of insurance coverage questions, while insurers could suffer billions of dollars in losses.

WHO has collaborated with the European Commission (EC) and the European Centre for Disease Prevention and Control (ECDC) to assess the national pandemic preparedness plans in the following countries: France, Greece, Italy, Kazakhstan, Poland, the former Yugoslav Republic of Macedonia, Turkey, Ukraine and United Kingdom. Missions to other European countries are also being planned.

All 52 Member States of the WHO European Region have been invited to attend workshops to review national pandemic preparedness plans, held in collaboration with EC and ECDC. The first pandemic influenza preparedness planning workshop took place in Luxemburg in March 2005, the second workshop in Copenhagen, Denmark, in October 2005, and the third workshop will be held in Stockholm, Sweden, in May 2006.
An avian flu pandemic could leave employers with decimated workforces and a host of insurance coverage questions, while insurers could suffer billions of dollars in losses.

The flu’s high mortality rate - greater than 50% in the 141 cases reported to the World Health Organisation - has sparked fears that the illness will sweep the globe if it mutates into a form that is easily transmissible among humans.

The World Bank has estimated that each year of a severe pandemic could cost the U.S. economy $100 billion to $200 billion, and economies worldwide could suffer a total per-year loss of $800 billion.

Those potentially dire consequences aside, there remains uncertainty as to whether employers would have the coverage to pay the health care, business interruption, workers compensation and other losses that could arise if the workforce were to be ravaged by the virus and productivity were to be dramatically slowed.

Insurers worldwide could suffer losses from $71.3 billion to $200 billion in a worst-case scenario, according to Standard & Poor’s Corp., which based its estimate on figures from its analysts and numbers compiled by the Insurance Information Institute.

New York-based S&P said in a report issued in November that losses would occur among health insurers, commercial property/casualty underwriters, life insurers, property and life reinsurers and retrocessional programs. Automobile and homeowners insurance would likely be the only lines «not to suffer a hit» by avian flu-related claims, S&P said.

An informal survey among members of the Federation of European Risk Management Associations (FERMA) revealed concern about the risk of an international influenza epidemic among European businesses, but differing perception of the severity of the risk and urgency of the need for additional risk management measures depending on type of business.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Cyprus</td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Georgia</td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Kyrgyzstan</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Moldova, Republic of</td>
<td></td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Romania</td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Turkey</td>
<td>x</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Turkmenistan</td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Ukraine</td>
<td></td>
<td></td>
<td>x</td>
</tr>
</tbody>
</table>

Risk managers or risk management associations from Denmark, France, Germany, Spain and the United Kingdom responded to questions from FERMA about how a flu pandemic could affect their business and what measures they are taking to manage the risk. Their responses showed that most sensitive sectors are health services, transport, telecoms and power suppliers and the food industry.

The most common areas of concern mentioned in the FERMA survey are:

- travel restrictions;
- the effect on suppliers in other countries;
- some companies also believe there could be an impact on their ability to fulfil contracts, and companies selling goods and services to consumers can foresee a risk of reduced demand;
- one company with interests in bio combustibles said it is somewhat concerned about the potential effect on the agricultural sector;
- one association drew attention to the pension implications if there is high mortality;
- a small number of businesses may find demand for their products or service increases. One company with IT operations said a major outbreak of flu might result in an increased call on its software management services for medical services and hospitals.

The most frequently mentioned risk management measures are:

- offering vaccination and anti-viral medication to employees. That this offer will not necessarily extend to employees’ families raises an issue, because supplies are likely to be inadequate to cover everyone. The French working group has found that employees would not take the anti-viral medication themselves but save it for their families;
- offsite, tele-working and use of new forms of communicating, such as webinars;
- the creation of employee information and advice services.
Prospectus Liability and Mergers & Acquisitions

EOS RISQ Belgium – Jan Van Hecke

Having recourse to public or private savings involves risks. The European and Belgian insurance market has already come up with solutions in the past. Few policies were taken out for various reasons. This changed in 2005 when supply and demand started to rise. The insurance market will become a fully developed market for such risks in 2006.

EOS RISQ Belgium has always followed this market closely and offered insurance solutions where possible. For this reason, we can now anticipate company needs in a more fully developed insurance market. In this case, we make use of the experience of our partners within the EOS RISQ network.

1. Having recourse to public savings: Prospectus Liability - Trends

For the first time since 2000, a major increase of initial public offerings in Europe for 2004 has been noted. With just two offerings, Belgium came third in 2004 after the UK with 191 offerings and France with 24 offerings.

The reason for this high ranking was the initial public offering of Belgacom, which amounted to $4,399 million. This was 4% of the overall capital attracted worldwide via Initial Public Offerings, abbreviated as IPO. The trend of the previous year continued in 2005.

Over the past two years, European and Belgian companies did not only have recourse to public savings via an IPO. We have also noted (secondary) capital increases, debenture emissions and public take-over bids.

A continuation of trends of the past two years are predicted for 2006.

1.1. Risks linked to having recourse to public savings

The legal basis of these risks lies mainly in the law of 22 April 2003. This law concerns the public offer of securities. This law is not limited to the public offering of shares, including IPO and (secondary) capital increase, but also focuses on the public issue of debentures, real estate certificates, interest instalment contracts, interest and currency swaps, right up to the public take-over bid.

According to the law of 22 April 2003, applying a European Directive to Belgian legislation, a public offer of stocks may only be made after a prospectus has been published that has been approved by the CBFA (Belgian financial banking and insurance commission). The prospectus must include data of the public needs to take considered decisions regarding the investment offer. It must also include the names of those responsible for the content of the prospectus, usually managers. They are jointly obliged to rectify any disadvantage that may be the immediate and direct consequence of the lack of or inaccurate nature of statements in the prospectus, its supplements or updates.

In addition, the law states that the issuer, the bidder and the intermediary are always jointly liable for the content of the prospectus, as well as for reports, means of advertising or other documents relating to the public offer. This can be, for example, press announcements and road shows accompanying the public offer and the issue of the prospectus.

The issuer is the company whose stocks are the subject of a public offer. The bidder is the person who makes a public bid, as with a public take-over bid. The intermediary is the financial institute that guides the issuer or bidder.

Apart from the law of 22 April 2003 other sections of the law, on whose basis a person can be held liable, continue to apply. This includes company legislation and civil code articles on whose basis managers and companies can be held liable. If managers are not mentioned in the prospectus this does not mean that they are in the clear.

1.2. Insurance facilities

The insurance facility we can offer depends on the coverage you are seeking and on the extent and nature of the public bid.

The insurance facility we can offer depends on the coverage you are seeking and on the extent and nature of the public bid. Do you wish to only insure the managers or should the company (issuer/bidder) also be included in the coverage? What about protection for the benefit of the intermediary? An IPO with limited capital needs a different insurance solution than an IPO with a large capital, a debenture emission or an OPA.
The insurance solution consists of either an extension of the existing policy manager liability or a separate policy that only covers the risks of the public bid. A separate policy only grants you a deposit for these risks. Such policies are usually taken out for a period of three to five years.

2. Having recourse to private capital: Mergers and Acquisitions (M&A) - Trends

Mergers and acquisitions remain numerous. 2005 was a good year for mergers and acquisitions. 2006 promises more of the same. These days, many private equity companies and venture capitalists want to buy and sell. The insurance world is responding to these increased activities.

We note that both sellers and buyers are currently interested in an insurance solution for the risks involved in an M&A deal. In turn, insurers respond with flexible underwriting and feasible (premium) conditions. However, the minimum premiums remain considerable, so insurance policies taken out today are more about M&A deals with a high transaction value. The European M&A insurance market will be a fact from this year on.

2.1. Risks related to having recourse to private capital

In a private take-over bid, the seller has recourse to the private capital of the buyer. In a private merger, both parties are seller and buyer. As these cases do not concern “using public savings”, the law of 23 April 2003 does not apply. This entails no prospectus or prospectus liability. However, the buyer wants to be informed about what he buys, just like the general public.

This is why a company that wishes to sell one of its branches writes a memorandum that includes data the potential buyer needs to make a purchasing decision.

The memorandum can be compared to the brochure. The layout and the issue of the memorandum are done in the disclosure phase. A data room is then installed on a regular basis. Here candidate buyers can consult even more data. This phase is called the “buyers due diligence”. The disclosure phase and the buyer due diligence results in a “Share Purchase Agreement”, abbreviated as SPA.

This agreement between the seller and the (prospective) buyer mentions several securities, known as warranties and indemnities.

Some examples:
- the seller declares that he will pay the unpaid social security debt;
- the seller declares that the pending damage claim will never amount to more than 10,000 EUR for the company.

When these warranties and indemnities are taken up, this entails a risk for the seller. He must compensate. The buyer also runs the risk if the seller cannot or will not compensate.

A much-used solution is the use of an “escrow account”; the buyer blocks a sum on an account that is used every time warranties and indemnities are taken up.

Both the seller and the buyer are increasingly on the lookout for insurance solutions for the following reasons:
- the seller wishes to give as few guarantees as possible, while the buyer would benefit from high guarantees. The difference can be bridged by an insurance contract. For example, if the seller wants to provide securities up to 1,000,000 EUR, while the buyer wants to increase this amount to 11,000,000 EUR. The insurance policy then insures the difference of 10,000,000 EUR;
- the seller recently bought the company he wants to sell, which makes it almost impossible for him to provide the requested securities. The insurance contract can again take over the value of the securities;
- the seller cannot block a large sum of money on an account for a longer period for financial reasons. Here the insurance contract can be an alternative to the “escrow account”;
- if the seller falls under a different jurisdiction than the buyer, this can result in uncertainties regarding the value of set warranties and indemnities. What is the value of warranties underwritten by a seller from Russia who wishes to sell a Romanian branch to a Belgian company? An insurance policy may solve this problem;
- the prospective buyer wants to distinguish himself from his competitors. He does not request warranties or indemnities from the seller, who is covered by an “escrow account”. He has covered this via his own insurance policy.

The success of the insurance contract not only depends on the price tag and the coverage, but also on the speed and flexibility of underwriting.

2.2. Insurance facilities

The success of the insurance contract not only depends on the price tag and the coverage, but also on the speed and flexibility of underwriting. This risk analysis by the insurer can run smoothly and quickly through our mediation. As soon as we receive a memorandum, we organise a conference call with the insurers and the client. An indicative offer follows within two working days that can be adjusted in the light of new additional information. However, in practice the indicative offer usually remains
the same. If changes need to be made to the first offer, they are usually to the advantage of the client.

Both the seller and the buyer can underwrite the policy.

If the seller underwrites the policy, then it covers liability resulting from given warranties and indemnities in the SPA. It then concerns liability insurance which excludes deliberate action by the seller and excludes errors committed by the seller of which he should have been aware on the day the policy was signed. In professional jargon, this second major exclusion is called “prior knowledge exclusion”.

If the seller underwrites the policy, then this does not cover liability insurance. This entails no deliberate action exclusion by the seller or ”prior knowledge exclusion”. This policy is more expensive, but covers a lot more than the above-mentioned liability insurance.

We usually start negotiations about an insurance solution with the seller, as the layout stage of the memorandum often does not concern a buyer. Once the buyer is known, further negotiations often take place with the buyer who then takes out the policy.
EOS RISQ, Europe’s leading provider of insurance broking and risk management services, has officially opened a new Russian company in Moscow – ZAO “EOS RISQ CIS” to consolidate a decade of serving clients in the Russian Federation and to take advantage of the growing market for the insurance sector in that country, and the rest of the former Soviet Union (FSU). EOS RISQ’s team in Russia will be headed up by Gleb Lobanov, who has over 12 years experience in insurance broking and risk management. An interview with one of the Russian insurance broking industry’s preeminent leaders in the Energy and Industry sectors.

The opening of the Moscow office enables EOS RISQ to provide an expanded level of service to both Russia and the FSU. The new office, which has staff dedicated solely to operations in the Russian Federation, will strengthen EOS RISQ’s positions in Central and Eastern Europe (CEE) and FSU.

Shavkat Mingaliev, Regional Manager for CEE and CIS noted, “The country office will improve the responsiveness of our Russian operations and strengthen our client orientation by establishing a streamlined and coordinated team of insurance specialists in Russia. Establishing a permanent presence in the region will provide us with greater control over both the global and local delivery of our services.”

“Mr. Lobanov, as you are in the insurance business for over 12 years now, can you please give us an update on the Russian insurance market?”

Recently there have been changes to the insurance law which will be fully implemented by 2007. The law has introduced new, higher capital requirements for both local and foreign insurers. We could expect the number of companies to be reduced heavily as a result of it.

Tough at present the number of local insurers is very high (a few hundreds), in reality we have about 20 serious players in the market who are buying very substantial reinsurance treaty protection from western companies. Local capacity of property treaties is about half a billion USD on Probable Maximum Loss basis and this amount keeps growing as more companies are becoming prepared to increase their limits. Here I would name Ingosstrakh ($150 Mln), Sogaz ($100 Mln) – captive of Gazprom, Rosno ($75 Mln). In marine, the Russian market can only cover sums up to $100 Mln.

Figures produced by the Ministry of Finance in 2005 suggest the real insurance market is around USD 115 mn in gross premiums for life, USD 3.63 bn in gross premiums for non-life.

A legal requirement to have motor third party liability insurance was introduced as of 1 July 2003 and became fully compulsory as of 1 January 2004.

How is the Russian insurance market regulated?

Until 2004 under existing legislation insurance companies could be composite, that is they could transact both life and non-life insurances. Changes to the Law in
2004 introduced a separation between life and non-life insurance, and insurers have until July 2007 to comply. Life insurers are able to offer personal accident and medical expenses insurances, which are regarded as non-life classes, in addition to life products. All insurers have to be licensed for each class of insurance transacted, but for reinsurance only a single license is needed.

The statutory insurance supervisory authority in Russia is the Federal Agency for Insurance Supervision (FSSN) known as Rosstrakhnadzor. Rosstrakhnadzor’s status was upgraded in 2004 and it is no longer a department of the Ministry of Finance, but an independent government body.

What are the current solvency margins applicable to insurers operating in the Russian market?

The solvency margin is established through a set ratio of assets and liabilities, with the company required to compare the actual ratio of free assets to liabilities to the ratio laid down by Rosstrakhnadzor, but the principles follow EU standards.

Companies are obliged to form premium and outstanding claims reserves and should create IBNR reserves if necessary. Companies may also form an equalisation fund to cover fluctuations in results.

Reinsurers’ share in the premium reserves of Russian insurers is limited and the percentages changed in the second half of 2005 to a maximum of 25% each rated Reinsurer (regardless of whether local or foreign) and 15% for a local, unrated company. Although these regulations provoked an adverse reaction when first introduced, they are understood not to cause any undue difficulties to companies operating in the market.

Rosstrakhnadzor has the authority to order remedial action in the event of the law being breached and the suspension, restriction or ultimate revocation of licenses, if necessary. If an insurer repeatedly infringes insurance legislation, Rosstrakhnadzor has the power to bring it before the courts and also to instigate liquidation proceedings against unlicensed insurers. Otherwise, there is no special insolvency system.

What international insurers are present on the market?

There are five international insurers present at the moment:

- Allianz – 100% subsidiary of Allianz AG, Germany. Registered in Russia in 1990 and offers Industrial, Engineering, Marine insurance;
- AIG - AIG Russia Insurance Company was licensed to operate in 1994 with headquarters in Moscow. In 1997 AIG Russia Insurance Company received its life insurance license and opened its Life Division in Moscow. As a result of the amendments to the insurance law about composite companies, there was a split into two companies: specialist general insurance company - AIG Insurance and Reinsurance Company (wholly owned subsidiary of AIG Europe, S. A.) and AIG Russia (Life, Accident and Pension).
  - Zurich – 100% subsidiary of Zurich Financial Services. Registered in 1992;
  - ERGO – operates as part of ERGO group since 2002;
  - ACE – was set up in October 2004 to provide Commercial Property & Casualty Insurance services in Russia. The company’s insurance and reinsurance license for 15 Product lines was received in March 2005. The 100% shareholder of the Company is ACE European Markets Insurance Ltd.

We experienced in other CEE countries that many companies very often stick to the former monopoly insurer and do not use their competitors. What is the situation in the Russian Federation?

The situation is not the same. Two former monopoly insurers Rosgosstrakh and Ingosstrakh have been sold to different industrial companies and though they remained market insurers their names are connected to the owners.

What is the common standard for insurance - book value or replacement cost value?

Depending on specific provisions of the insurance contract, the property appraisal methods used, the actual value of property at the moment of conclusion of the insurance contract may correspond to:

- full replacement value;
- book (depreciated) value;
- the sales value.

Common standard is full replacement value, though others can be applied also.

What are the most important issues for an international investor when it comes to their insurance needs when entering Russia?

These are the points which may differentiate Russian environment from Western approaches.

- Only admitted insurance companies are allowed to insure Russian risks.
- Despite the existence of a consumers’ law and rights and duties clearly set out in the Civil Code, litigiousness is very low and general third party liability insurance is therefore one of the weakest classes in the market. A certain group of activities are defined as being particularly dangerous and those carrying out these activities are strictly liable for any damage they cause according to the Industrial Safety Law passed in 1997.
This also provides for the compulsory third party liability insurance of enterprises involved in these hazardous activities (which include operating a lift).

- The Civil Code places a duty on employers to indemnify employees who are injured as a result of an employer’s negligence and, as compensation payable to an injured employee is not necessarily limited to payments from the Social Insurance Fund, this means that employers could have a greater theoretical exposure than they realise. At the present time, as state benefits are considered to be sufficiently high, courts are thought unlikely to insist on any extra compensation from the employer. Employers’ liability insurance (EL) is available but for the above reasons very little is actually bought. When it is, it is bought by foreign and joint venture companies which are used to buying this cover elsewhere.

Also there could be a rise in property insurance; A boom in construction, mortgage development and living quality improvement will be promoting this trend.

One of the most prospective growth sectors is PI insurance. With the development of litigation we will face more suits for damages compensation for faulty goods and services. PI of auditors, bookkeepers, valuers, doctors, lawyers, brokers, builders will be developing very fast.

What do you expect from the Russian insurance market in the future?

We have a few types of insurance which have growth potential. It is long term life insurance inclusive with investment program (as an alternative to different forms of investments), motor insurance, various types of liabilities, medium size and small business. Economic growth and strong competition will definitely support the growth of property and liability insurance of companies increasing the demand of industrial, construction and trading enterprises for insurance.

Contact details

Gleb Lobanov
Director General
EOS RISQ C.I.S.

12 Krasnopresnenskaya Embankment,
World Trade Center, office 1101, Moscow,
Russian Federation,123610

Tel/Fax: +7 495 258 12 05
Mobile: +7 495 768 38 45
E-mail: globanov@eosrisq.ru
European sprinkler regulation: rules and norms

EOS RISQ France – Gilles Lefrand and Guy Massart

On 16 March 2006, EOS RISQ France (DIOT) organised a debate on European sprinkler regulations in the prestigious Lutetia Palace (Paris). This debate, conducted by Chantal Delverdier, Director of DIOT Property Department, gathered Risk Managers, Loss Control Officers, Directors of Insurances, etc. of the local market.

Considering all sprinkler standards which appeared few years ago, it seemed interesting to draw up a comparison. During the first part of the debate, Gilles Lefrand and Guy Massart, DIOT Loss Prevention Engineers, compared different sprinkler regulations and standards including the new European norm n° EN 12845 (also known as French reference. NF EN 12845).

Sprinkler rules and norms

Available regulations, rules and standards can be summed up as follows:

<table>
<thead>
<tr>
<th>Europe</th>
<th>France</th>
</tr>
</thead>
<tbody>
<tr>
<td>National rules</td>
<td>R1 APSAD</td>
</tr>
<tr>
<td>EN 12845</td>
<td>NF EN 12845</td>
</tr>
<tr>
<td>CEA 4001</td>
<td></td>
</tr>
<tr>
<td>NFPA</td>
<td>Data Sheet FM</td>
</tr>
</tbody>
</table>

They can also be distinguished as follows:

In Europe:
- the European Insurance Committee rules (CEA 4001 – edition 2003) and/or national insurance rules (VAS, LPC, SBF...), conceived in the same way as the EN 12845 norm, but with insurance specificities (choice of water sources for instance...).

Why do specific insurance regulations exist for sprinkler installations?

- the insurance rules for sprinkler installations are the oldest (1898 for the rule R1 APSAD);
- the constant evolution of sprinkler systems and the change in risks has forced the construction of a common base;
- the integration of special sprinklers (Early Suppression Fast Response - ESFR, large drop...);
- rules are thoroughly investigated by third parties (VDS, ANPI, CNPP...) to interpret particular cases and to validate conformity;
- rules do not pertain to the installation of the systems, but they advise to enrol in a global system with:
  - a certification of the installers;
  - criteria for the definition of the water sources;
  - a follow-up in time by periodic control;
  - maintenance criteria and a life span of the system.

What are the common points and the technical particularities?

- The principles are similar with regards to the regulation of the activities and the products;
- the next edition of the rule CEA 4001 (1st quarter 2006) will introduce an important evolution (aggravation) of the regulation of the activities and the products;
- the norm NF EN 12845 remained globally demanding in terms of regulation of activities and goods. A similar
evolution to the CEA's is foreseen subsequently. This norm does not integrate the new technologies (ESfR); for the regulation of the given risk, all rules and European norms give a same density and a same demand area.

We have compared different main standards for different business streams, depending on the:
- density;
- demand area;
- flow rate of the fire pump;
- autonomy of the water sources.

Actually, for ‘classic’ activities, there are not a lot of differences between all the standards. The differences are more meaningful in industrial activities.

Conclusion

Industrials have a variety of standards at their disposal and, in agreement with their insurers, can choose the most suitable to meet the optimal security level for their activities.

At a European level, the forthcoming regulations will enable a harmonisation of all current installation rules.

One of the most important issues regarding the sprinkler system installation is the question concerning the periodic revision. On one hand, the European regulations are not sufficiently clear on this topic. On the other hand, a few national regulations are very demanding, such as the R1 rule of the APSAD.

EOS RISQ France suggests the ‘progressive steps’ developed for this periodic review of the current sprinkler installations. This action, including the latest European regulations, is essentially based on an actual analysis which will also integrate the use of new technologies such as endoscopies and ultrasonic sounds.

The goal is to ensure durability for the good operation of the installations, working closely with insurers on an objective and technical argumentation, to achieve substantial savings by minimizing the repair works.

Contact details

Chantal DELVERDIER, Property Department Director
cdelverdier@diot.fr - Tel : (33) 1 44 79 62 04

Gilles LEFRAND, LP Engineer
glefrand@diot.fr - Tel : (33) 1 44 79 62 67

Guy MASSART, LP Engineer – sprinkler specialist
gmassart@diot.fr - Tel : (33) 1 44 79 62 61
GLOBAL VISION, LOCAL PRECISION

- Europe’s leading insurance broking and risk management consultancy, providing practical solutions for our clients.

- Offering know-how and expertise, together with quick, personal and flexible service.

Check www.eosrisq.com for your local EOS RISQ office.