SPECIAL REPORT:

PROPERTY RISKS

24 **Hot property risks**
Risk management evaluations are central to understanding property risks and the communication of these risks to employees plays a vital role in the overall property risk mitigation process

25 **Made to measure**
Tailoring a property risk management approach based on a company's specific business operations is a smart solution to a tough challenge

26 **Primary property concerns**
Risk managers must understand the specific property risks of their business and match them with a detailed and tailored insurance policy

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Hot property risks

Risk management evaluations are central to understanding property risks and the communication of these risks to employees plays a vital role in the overall property risk mitigation process

APPRECIATING THE EXTENT of an organisation's various property risks is only half the challenge. The other half is determining how this information, and any actions and processes that must be undertaken, can be effectively communicated to employees.

Some of the best tools for communicating property risks are training, drills and exercises, according to Singaporean risk manager Gordon Song. Song says that the purposes of these are to test the robustness of response plans and to ensure that employees are continuously familiarised with business interruption threats such as fire and outages.

"Normally, companies select a scenario, or perhaps a few scenarios throughout the year, and simulate a threat event that blocks access to a facility," says Song. "Examples [can include:] a facility semi-destroyed by an explosion and fire; operations having to run below 100% capacity [following] an event such as a pandemic outbreak where some staff members may be quarantined; or if an alternate site needs to be activated – and such sites are usually not exact replications of the size of the original facility."

Song says the first step is often the 'activation' of the crisis, resulting in what is known as a 'call cascade' or 'call-tree activation'. This is where people contact each other in a cascading fashion via phone or SMS.

"The response plan is then activated and some companies do simulate this with the full extent of role-play, set up of the crisis centre and the like," he explains. "Pre-assigned observers take notes of what they observe throughout the drill. A debrief is conducted after the exercise has been called to a stop. Following this, normally within a week or two, a formal report will be tabled outlining the good, bad and ugly [elements] of the exercise, with recommendations for improvement. This then normally results in the response plan being revised where necessary."

Song says this process is known as a 'full-crisis simulation exercise', and it can be performed for any kind of risk, such as a pandemic outbreak, fire, IT system downtime and flood. "The nature of the test determines what is involved," he says. "For example, in some countries where power outage is a major risk, the test would include whether the UPS [uninterruptible power supply] kicks in, and how long the backup genset [generator set] can last with the diesel supply. One company ran this test and found out during the drill that the backup genset, which needed to be manually turned on, was locked behind a steel shutter that was opened electronically, which obviously could not be opened since the power supply had been cut."

Song says exercises can also be run on 'table top', a process known as a 'desktop simulation'. "In such an exercise, there would be an overall 'exercise in-charge', this is sometimes outsourced to a consultant or expert," he explains.

"The simulation is called to a start and involves the senior management team being called to a crisis room. The in-charge then bombards the senior management team with 'injects', which adds dimensions to the crisis. For example, if the crisis being simulated was a fire in a warehouse, one of the injects could be that the incident was now going viral on social media, with wild speculations of the company concealing unsecured hazmat [hazardous materials] on its premises. This would test the senior management's response to the development of a PR crisis, in addition to the operational crisis. The benefit of a table top exercise is that such side-scenarios can be added to spice up the exercise and test more dimensions of the response plan."

> *'The problem is that too many compliance and risk education and communications programmes operate according to a one-size-fits-all approach'*
> **OCEG**

Culture and communication

To perform effective risk communication, a company must assess its culture through qualitative and quantitative research methods. These can include personal interviews, focus groups, surveys and observations to understand employees' attitudes, beliefs and values. It is also important to understand the influences on culture, such as people, leadership, policies, procedures and processes.

However, what constitutes company culture? A white paper produced by risk consultancy Protiviti defines it as a "set of shared values, attitudes, goals and practices that characterise any group".

Titled *Mitigating Risk Through Targeted Communications Requires Understanding Organisational Culture*, the white paper emphasises the importance of comprehending a company culture when communicating risk to employees.

It lists steps that can help to achieve a successful cultural assessment, such as: understanding the problems and issues; understanding what employees believe their role is with regard to these issues; determining what employees would do differently compared to current methods; determining the best methods for educating employees about the desired behaviour(s); and developing the most effective method for associates to receive and be receptive to the information.

The idea is that, once a company culture is better understood, risk managers are more able to provide targeted risk communications that will grab the attention of employees. When communicating property risk, employees will progress in their understanding of these risks only if they have paid attention to the communications on these matters.

Chief risk officer at Scentre Group Eamonn Cunningham says the best approach to communicating property risks to employees is with brevity of messaging.

"Messaging to staff [should be] short and straight to the point, described in the manner that people truly understand," he says. "Using the examples that are relevant to the audience assists in getting the message home as [does reminding] employees on a regular basis. Short, punchy emails can be very effective."

Cunningham explains that one of the better ways of being confident that the message is understood is to have employees actively engaged in developing control measures.

"These may be new measures or the enhancement of existing ones," he says." [Employees] own the risk and therefore have to play their part in doing whatever is possible to reduce the likelihood of occurrence or the consequence should it arise."

Cunningham adds that self-assessment questionnaires remind employees of their responsibilities, but also encourage the adoption of previously agreed protocol. "Certain key employees in our business are obliged to complete self-assessment questionnaires on a regular basis," he says. "This can then be backed up by compliance checks undertaken by the internal audit department. Self-assessments form a part of a workflow system whereby a supervisor or manager will review what [employees] say [they] have done or not done. In addition, audit monitors any lack of adherence to agreed procedures."

Assessing relevance

According to corporate performance think-tank OCEG, many executives want to know how risk training and communication can be made more effective and efficient. To answer this, risk managers must first ask an equally important question, namely as to how relevant their education and communications efforts are. OCEG finds that, unfortunately, the answer is often that these are not sufficiently relevant.

An OCEG illustration titled *How Should We Educate And Communicate About Compliance Risks* states that: "The problem is that too many compliance and risk education and communications programmes operate according to a one-size-fits-all approach. When all employees, regardless of the degree to which they encounter potential compliance risks on a daily basis, are dipped into the same vat of education, many employees will find the content to be irrelevant. Those employees not only retain much less of the education content, but they can also become less receptive to future training and communications that are highly relevant to their job roles."

Not only do too few companies tailor their compliance messages and training, many organisations overload their workforces with less-than-relevant risk content. So how can property risk communications be made more relevant? The OCEG suggests that this process should start with a risk analysis of jobs, as not all job roles – even those that are located in the same function or department – have the same level of exposure to a given risk.

As the OCEG puts it: "Once the risk relevance levels of different jobs have been identified, governance risk management and compliance managers should determine what knowledge each role requires given its risk relevance. In other words: what is the desired level of risk awareness and skill for someone in this job? At that point, the content and delivery method of compliance training and communications can be tailored to eliminate gaps between actual and desired levels of risk awareness."

The OCEG also advises that greater attention to delivery methods can help to improve the overall effectiveness and efficiency of compliance training and communications.

"Employees in high-relevance jobs might receive in-depth classroom-based training instruction on a specific risk (or set of risks) while employees in low-relevance jobs might receive computer-based training or, simply, sign off that they have read the appropriate policy and procedure related to the risk," it states.

"Similarly, employees in high-relevance jobs would receive more frequent communications about the risks – such as e-mail newsletters, blog posts, e-mail reminders and/or refresher courses. The higher the risk relevance of a job, the deeper the initial compliance training for that job – and the more frequent ongoing compliance communications and support – should be."

Made to measure

Tailoring a property risk management approach based on a company's specific business operations is a smart solution to a tough challenge

A VITAL CONSIDERATION OF property risk management is the acknowledgement that every business will have different considerations. It is therefore incumbent on risk managers to ensure that their plans are tailored to the specific demands and situation of their companies.

Regional director of engineering and risk management at Willis in Asia, Kevin Snowdon, says that risk managers have to work with multiple teams to identify property risks and to formulate mitigation and control strategies.

"An ERM framework will aid the generation of risk registers and hazard logs through multi-disciplined risk workshop sessions," Snowdon says. "The resulting risk registers clearly articulate and aggregate the combined knowledge of property risk from all the various teams that are knowledgeable and responsible for each. Only through a multi-disciplined view will a risk manager be able to understand the full scope of the property risk spectrum."

Two major phases

Director of Tunstall Associates Steve Tunstall says that two major phases should be considered when evaluating unique property risks. "First, comes the design and construction of the property [phase]," he explains. "Almost every jurisdiction has strict codes of practice around the quality of construction and design, the materials that are utilised, plus the layouts of the rooms and compartments depending what type of building is being constructed.

"The second phase is the actual management of the building once it is in operation. Clearly, if a system is put in place, even a world-class system, but it is not maintained, updated or modified, then the risk exposure will increase over time.

"It is important to make sure those systems are maintained, not only for insurance purposes, but also so that local law and regulations are not breached. [If a risk manager knows that] the building is managed and maintained properly, then [they will know they are] ready to respond in the event of a crisis. [Knowing this] will certainly assist during discussions with insurers, too."

Suitable strategy

Snowdon says that a suitable risk management strategy can be defined only by identifying and understanding the property risks at hand.

"The risk identification process must be designed to be suitably robust and systematic and be led by personnel with experience and insight into

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Steve Tunstall, Tunstall Associates

the hazards and risks associated with the unique business activities."

Snowden adds that, in the early 1970s, chemical company ICI developed the HAZOP hazard and operational review process to address the nuances and multiple combinations of process activities. "This process broke each system into its component parts and forced design engineers to consider every combination of incorrect operation that may lead to property damage," he explains.

"The application of this hazard identification process during the design stage then allowed for inherent safety features to be added into the design to address the myriad risks and hazards inherent with the business."

Brad Tymmons, enterprise risk and insurance manager at EnergyAustralia and president of the Australasia chapter of the Risk and Insurance Management Society, says it is vital to understand company objectives and then develop a risk management strategy that the business can implement.

"[A firm] cannot implement a broad-ranging strategy and then have no resources and plans to achieve the strategy," he says. "For instance, [it] might want to run [its] assets with very minimal outage. To do so will require additional risk capex [capital expenditures], regular monitoring and reviews. This cannot can done without the capability, both resources and a plan."

Tunstall says a key task relating to a tailored property risk management approach is ensuring that the management systems for a property have the right insurances and that those are aligned with the key performance indicators of the business.

"With a market dealing desk business, or a share trading business, the access requirements and the quality of services required in that sort of business are at a high level," he says.

"The tolerance for anything not being available or for business interruption is low; [there is] no tolerance for time-outs and interruptions in any way. However, if comparing that to a warehouse, which might be holding commodity stock, the tolerance for something going slightly wrong will be different.

"This should be reflected in the building management systems that are put in place, how those systems are maintained, and it should certainly be reflected in the way policies are structured in the event of something going wrong."

Mapping, monitoring and warning systems

A paper by The World Bank, *Preventable Losses: Saving Lives and Property through Hazard Risk Management. A Comprehensive Risk Management Framework for Europe and Central Asia*, highlights the importance of using mapping, monitoring and warning systems.

The report states: "Mapping, monitoring and warning systems entail larger investments but should nevertheless be considered priorities for particularly vulnerable regions. Investments in physical infrastructure – such as flood protection and retrofitting of housing and public structures (bridges, hospitals, schools) for seismic resistance – are very expensive.

"Selection of the most suitable investments should be carried out by applying cost-benefit or cost-effectiveness analysis. Monitoring and warning systems can significantly reduce damage to lives and property from some hazards."

Primary property concerns

Risk managers must understand the specific property risks of their business and match them with a detailed and tailored insurance policy

BUSINESS PROPERTY RISKS are primary covered through three major types of insurance coverage: industrial all risks; property all risks with machinery breakdown; and business interruption, according to Joseph Kung, Lockton's chief technical officer and director of international risks.

Kevin Snowdon, regional director Asia, engineering and risk management at Willis, says that a property all risk offering is the primary policy for property risks coverage.

As this type of insurance coverage excludes only risks that have been specifically outlined in the contract, Snowdon says the title "is a misnomer since the policy covers all risks expect those that are excluded.

"At Willis, we must first fully understand a client's business before we can recommend a suitable coverage," he adds.

Snowdon explains that a property all risk policy includes various sub-limits that may limit cover for a client's property risk. Key clauses to be tailored for various property risks include business interruption; increase in cost of working; additional increase in cost of working; machinery breakdown; suppliers and customers extensions; infectious disease; denial of access; debris removal and demolition; and natural perils limits.

Designing to size

Managing director of Australian firm LMI Group Allan Manning explains that for clients with assets of more than US$10m, the most common policy used is the industrial special risks policy.

"For smaller risks, insurers have developed business pack policies, with some having specialist package policies for farm, motor trades or office risks," says Manning.

"These policies have multiple sections, including a property or sometimes a so-called fire section, which is designed to protect the physical assets. Other sections that include property are the money, burglary/theft; transit, and/or general property sections, which provide cover away from the insured's premises. This is good for, say, a tradesperson who takes their tools to site."

Eamonn Cunningham is chief risk officer at Scentre Group, which is the combined property interests of each of Westfield Retail Trust and Westfield Group in Australia and New Zealand. He says the firm carries the typical policies for property risks, including business interruption, casualty and terrorism.

"The classes of insurance themselves are not unique to the business, but the true value comes from specifically tailoring or manuscripting your individual insurance form to suit your circumstances," Cunningham says.

Major mistakes

Irene Lye, head of risk management at Ascendas, points out that a common mistake when arranging property risk insurance is not understanding how insurance covers are structured and the risks exposure of the buildings to be covered.

Manning takes the view that under-insurance is the biggest mistake to avoid. "Most policies penalise

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> **Allan Manning,** LMI Group

the insured if they do not insure their property fully," he says. "For example, if they insured the contents and stock for, say, US$1m and the value at risk at the start date of the policy was US$2m, then the insurer would not pay the full loss suffered by the insured."

Singaporean risk manager Gordon Song says that a general property damage/business interruption policy, otherwise known as property all risk policy, would normally cover most property risks. "However," he adds, "the devil's in the details when it comes to property risk cover, and the risk manager must work closely with the broker or advisor to ensure that specific exclusions in the policy do not render the company with financial exposures."

Song suggests that issues in relation to master versus local policy are "key considerations for a company with multi-territorial operations, particularly in some jurisdictions where the local insurance market may not be well aligned with global standards".

"It is therefore important to select a strong lead broker and insurer with multinational coverage and expertise," he adds.

"Another important consideration is whether bailee's customer coverage is required and available under existing policies, such as coverage for third-party property." **SR**

Property insurance checklist

LMI Group has produced a property insurance renewal checklist, which it suggests is best used every year about 60 days prior to the renewal of commercial insurance policies. It states:

- If you own or are responsible for insuring the building, have you reviewed the replacement value of the building?
- Have you conducted a thorough review of the value of your machinery and plant, tenant's fixtures and fittings, office equipment and stock (including raw materials, work in process and finished goods), and customers' goods?
- Have you reviewed your policy sub-limits for removal of debris, extra costs to comply with changes to the building code, theft, and others? If no, speak with your insurance adviser.
- Have you reviewed the range of perils that your policy provides protection against, including accidental damage, flood, machinery breakdown and others?
- Have you added or removed any security, alarms, bars, security systems or the like?

THOUGHT LEADERSHIP

Mid-market recovery alters risk landscape

As the dust settles after the debilitating financial crisis of the late 2000s, the green shoots of recovery have altered the ambitions of today's corporations.

The economically turbulent times witnessed in the past eight-to-10 years caused many mid-market firms to forgo the benefits of expansion and innovation.

Nowadays, we are witnessing exciting growth for mid-market firms in a time of economic improvement across the region. They are starting to go on the expansion trail and establish themselves in new markets across the globe.

As this shifting mid-market focus unfolds, the risks that affect these burgeoning businesses are changing. For example, in the wake of fast-paced global expansion, risk managers could be left concerned that a local insurance policy issued in one country would be inferior to the master policy in their domiciled country.

As businesses begin to focus once more on growth, the role of the risk manager must evolve to protect the company as it enters new markets. So the role of the insurance industry must also shift, as we seek to support and enable our clients' growth aspirations.

In recognising this, AIG developed 'Property Performance', an innovative new product that offers consistent global cover (subject to local legal and regulatory requirements), greater control for the risk manager and faster payment in the event of a loss. The product will launch shortly in Australia and be available in other territories within Asia-Pacific soon after.

Property Performance provides the covers that might be expected of a standard property insurance product, and extends this to address areas not covered by typical property policies. It offers full machinery breakdown cover, cyber cover, environmental clean up, full theft coverage and an upgrade to certified green materials when rebuilding damaged property.

After a large loss, AIG advances the insured 50% of the agreed property damage, clean up costs and expenses to reduce loss once coverage has been confirmed and the estimate for damage has been agreed. The product also has a major enhancement in its business interruption cover that enables the client to have the benefit of a claims settlement based on the higher calculation of either a gross profit or gross earnings specification.

In short, Property Performance reduces the degree of uncertainty and ambiguity risk managers might have around their insurance needs and provides easy to comprehend global property coverage.

The financial crisis is behind many fast-growing firms, and these companies are undertaking exciting, bold moves into new markets and territories. At AIG, we are proud and honoured to help fuel this engine of growth.

Nick Wood, head of global property Australasia, AIG

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