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THURSDAY 18 SEPTEMBER 2014

ISSUE 4,192

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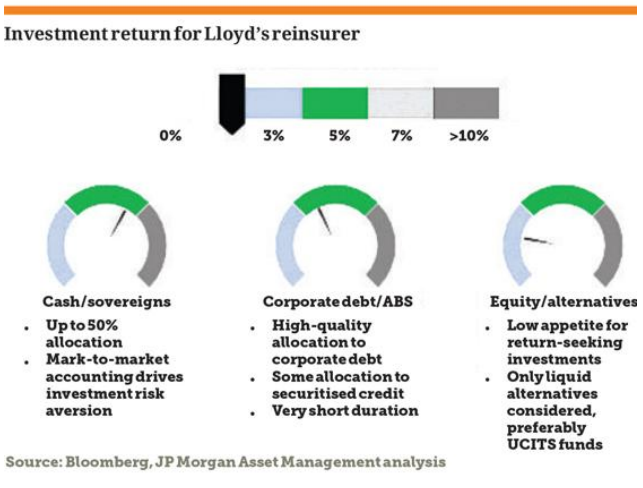

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Insurance Day is the world's only daily newspaper for the international insurance and reinsurance and risk industries. Its primary focus is on the London market and what affects it, concentrating on the key areas of catastrophe, property and marine, aviation and transportation. It is available in print, PDF, mobile and online versions and is read by more than 10,000 people in more than 70 countries worldwide.

First published in 1995, *Insurance Day* has become the favourite publication for the London market, which relies on its mix of news, analysis and data to keep in touch with this fast-moving and vitally important sector. Its experienced and highly skilled insurance writers are well known and respected in the market and their insight is both compelling and valuable.

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ISSN 1461-5541. Registered as a newspaper at the Post Office. Published in London by Informa UK Ltd, Mortimer House, 37/41 Mortimer Street, London, W1T 3JH

Printed by St Clement's Press, Unit 16, Bow Industrial Park, Carpenters Road, London E15 2DZ

Search for improved RoE can undermine future business, Lancashire investor head warns

Market's poor decisions due to 'inexperience', Creagh-Coen says

Sophie Roberts
Deputy editor

The current market environment requires the industry to find new ways boosting return of equity (RoE), but companies should be mindful of undermining long-term business strength, Lancashire's head of investor relations has warned.

Jonny Creagh-Coen told *Insurance Day* at Monte Carlo: "We're seeing insurers try to improve RoE by retaining more risk on their balance sheets, but in the long term, this may impact combined ratios.

"This is when cycle management becomes very important. This strategy is really only a short-term fix," he said.

"What insurers should really be doing is gearing themselves up for future losses by buying more reinsurance – particularly given the current pricing environment."

The low interest rate environment is a concern but Creagh-Coen said Lancashire is not prepared to instigate a "risky play" to ride this part of the cycle out. "We've put in a few things in place to mitigate [low] yields and we'll continue to keep an eye on what the returns are doing."

Creagh-Coen observed some bad practice within the market place in search of higher yields, but put this down to inexperience.

"I think there are some poor decisions being made, but I also think this is down to inexperience," he said. "Those market individuals who have successfully brought businesses through difficult market cycles before are hot property at the moment."

Lancashire is shrinking some of its business lines, including energy, marine and property reinsurance.

"We've never been a business that has grown just for the sake of growth, but we are having to shrink some areas, if slightly reluctantly," he said. "It's really just a reaction to what's going on in the market. Lancashire is geared up to deal with severity losses where a lot of the current pricing pressure resides."

Creagh-Coen said earnings could be down slightly down next year. "But we'd maintain a healthy combined ratio – that, I'm confident about," he said.

Lancashire's acquisition of Cathedral syndicates 2010 and 3010 was an important step for the company. "We wanted more of a presence in Lloyd's but we didn't feel we could make it from scratch," he said. "Cathedral has a great track record and is extremely relevant. It's everything we thought it was and better."

On whether Lancashire would want to make further acquisitions in Lloyd's, Creagh-Coen said: "There are a lot of decent syndicates out there, but we want to focus more on underwriting than on further consolidation.

"We've inherited, in my opinion, the best aviation team out there in the Lloyd's market and with what's going on in that area of the market, I expect good things here," he said.

Lancashire running rule over cyber-risk product

Jonny Creagh-Coen told *Insurance Day* there is a potential opportunity for Lancashire to develop a cyber risk product, but there are concerns about modelling the exposures.

"We're doing due diligence on it but it's a potential loss which is completely untested. How big could it be? The answer is, we don't know. Certainly, if a big bump came and we could collate data on that, we would be in a better position to consider it. But we can't quantify what a big loss would look like, and that's a risk," he said.

With the threat from cyber attacks increasing over the past few years, a rising number of insurers are looking at launching cyber products.

Fireman's Fund p/c business to merge with Allianz Global Corporate & Specialty

Allianz is to integrate the Fireman's Fund commercial property/casualty (p/c) business into Allianz Global Corporate & Specialty (AGCS), the group said, *writes Michael Faulkner*.

The combined AGCS and Fireman's Fund commercial p/c business is expected to total more than $3bn in revenues, based on gross written premiums in 2013.

Allianz said the move will strengthen the Allianz brand in US commercial p/c.

The Fireman's Fund commercial p/c business focuses on a range of industry and product specialisation, particularly those with domestic exposures across the US, while AGCS concentrates on large corporations or specialty risks, particularly those with multinational exposures.

The move follows the 2009 transfer of the Fireman's Fund Marine business to AGCS, which brought the latter nearly $600m in annual gross premiums.

Allianz said various options are being considered also to build scale for the personal lines business of Fireman's Fund. This business area, which focuses on high net worth customers, represents approximately one-third of the Fireman's Fund business by gross premiums in 2013.

Andrew Torrance, chief executive of Fireman's Fund Insurance Company, said: "This move gives our commercial p/c business greater direction and focus. AGCS will offer many benefits to Fireman's Fund's clients and business partners in the US, with its global reach, recognised expertise and AA-rated financial strength."

Axel Theis, chief executive of AGCS, added: "The integration of the Fireman's Fund business into AGCS allows Allianz to focus on opportunities in commercial insurance, operate under the Allianz brand and build on the commercial p/c insurance solutions and relationships already offered in the US by AGCS."

NEWS

Alternative capital could play key role in tackling cyber challenge: McGavick

Scott Vincent
Editor, news services

Alternative capital could play a crucial role in developing effective cyber coverage, according to XL Group's chief executive, Mike McGavick.

McGavick, who has consistently called for the industry to innovate to maintain its relevance in a rapidly evolving risk landscape, said the insurance and reinsurance sector had still not done enough to tackle major social needs, such as cyber and flood risk.

"On the major challenges such as cyber and flood the industry is doing things at the margins but not at the hub of the matter," he told *Insurance Day* at this year's Rendez-Vous in Monte Carlo.

Getting expertise into the insurance sector to deal with issues such as cyber is the next major challenge, he said.

"The great minds who work in preventing cyber intrusion in this world probably aren't working for insurance companies. They are likely to be working for government or big software companies.

"The real cost to society is the lost opportunity from crashed machines and lost data. At present, the cover for this tends to be a form of warranty product but I don't see that as the most efficient way to protect against this risk. Alternative capital may be an important element to develop solutions to make a real impact."

"I find it gratifying the innovation theme is rising in the common context. When people commit themselves to innovating, they tend to be held to account on it. This will eventually make a difference"

Mike McGavick
XL Group

McGavick said this year's Rendez-Vous had seen a change in attitude towards the capital influx in the market.

"This year there is a sense people are realising the capital is not going to go away, but also that it presents opportunities as well as challenges," he said.

"I find it gratifying the innovation theme is rising in the common context. When people commit themselves to innovating, they tend to be held to account on it. This will eventually make a difference."

Extracting risks such as flood from government programmes to the private market is another area where the XL chief executive believes there are growth opportunities.

"Across the world, governments don't have the resources to do what they need. Whenever a market-driven solution is available to a social problem, that frees up resource to tackle other problems that may not have market-based solutions. Even in the US, when hurricane Sandy struck, only half the economic loss was insured.

"There are three pillars that can drive this change. First, the government has to give shape to the market. We then need to step in to provide the product. And a combination of these two pillars needs to change behaviour.

"If this is achieved, it can have a major impact on social problems. But when government gets it wrong, you can have situations such as the US flood programme that is inefficient, politically driven and not competitively priced."

McGavick said XL's growth strategy will continue to focus on both developed markets and regions that are under-penetrated.

"We are undersized in the US relative to our total book. We are growing in Latin America, particularly in primary, and also growing in Asia substantially.

"I've been really pleased with growth on the insurance side. We are building a crisis-management business and our US property team we put together four years ago has built a better book of business.

"One place we would like to have a more visible role is Africa. In the long run, I'd like to think we will have a physical presence on the continent."

XL had also developed its political risk business, given the ongoing turmoil across a number of regions of the world, McGavick said. "These are fascinating times. In World War I, civilised nations came to the conclusion chemical weapons were unacceptable and they were effectively banned from use by convention. In the past couple of years, we've seen a government essentially gassing its own people," he said.

"There has also been the situation in Crimea – we haven't had a forceful annexation of a territory since World War II.

"We've had two world wars and the enduring principle which emerged from both has been undermined in the past two years," McGavick added.

Insurers face '£100m-plus' VAT bill from landmark ruling on intra-group services

Banks, insurers and other financial services firms across Europe face extra VAT costs, running into hundreds of millions of pounds in the UK alone, according to tax experts, following a European Court of Justice (ECJ) judgment yesterday, *writes Michael Faulkner*.

The ruling, which concerned Skandia America Corporation and the Swedish Tax Authority, means services supplied between a group's headquarters and its branches may now be subject to VAT.

Other tax authorities across the EU will now consider how they implement the rules.

Stephen Morse, tax partner at PricewaterhouseCoopers, said many financial services firms will see their VAT bills soar as a result.

"The case significantly expands the VAT net for financial services firms. Banks and insurers are likely to be affected most," he said.

It is standard for head office costs to be shared between a group's subsidiaries. The ruling means any internal costs between a firm's branches will now face VAT, rather than just the external costs.

Morse added: "It's surprising the ECJ decided any supply between a firm's headquarters and its branches is liable to VAT, rather than focusing on specific scenarios.

"We need to see how different countries will interpret the ruling and until then there will be considerable uncertainty for the financial services sector.

"Banks and insurers need to consider how they could be affected."

Collateral trust licence opens door for new Eastern European retro capacity

Reinsurers will be able to access new sources of retrocession capacity from eastern Europe after a Kiev-based insurer was awarded the first central and eastern Europe (CEE) region-wide licence for collateralised retro activities, *writes Michael Faulkner*.

Brokbusiness has been awarded a licence from the National Bank of Ukraine to post collateral abroad as part of its retro reinsurance capacity provision.

The licence is the first of its kind throughout the CEE region and paves the way for other insurers and financial institutions in Eastern Europe to obtain similar licences for retro capacity.

Previously, no CEE insurance company has been granted permission to post collateral directly into a designated Western bank as part of collateral trust arrangements.

Eastern European capital providers can find it challenging to provide capacity directly to cedants through traditional reinsurance structures because of a lack of financial strength, weak local sovereign rating or their size.

The capacity will be available through Bermuda-based niche reinsurer Phoenix CRetro, which provides a platform via which Lloyd's syndicates and global reinsurers can access retro capacity.

Kirill Savrassov, London chief executive of Phoenix CRetro, said the licence, which took nine months to negotiate, will set a precedent for others to be obtained from the region's national banks.

"The licence provides an additional flow of virgin cat capacity. The aim is to expand deeper into Ukraine and get more participation for January 1 renewal and then to expand within the region," he told *Insurance Day*.

Phoenix CRetro hopes to have $100m in retro capacity from the region's insurers within five years. This figure could be higher if hedge funds, asset managers, banks and high-net-worth individuals provide capacity.

"As well as providing a timely boost to the local CEE insurance sector, this initiative will also widen the frontiers for regional institutional investors by providing them with access to insurance-linked securities as a new class of assets," Savrassov added.

Towards a more robust investment

To protect earnings as reinsurance margins compress, reinsurers should consider the role investments can play during a soft market

Gareth Haslip
JP Morgan Asset Management

The reinsurance marketplace has been evolving rapidly in recent years, driven by the inflows of additional capital from insurance-linked securities fund managers and hedge fund reinsurers, alongside a relatively benign period of catastrophe losses. In combination, these factors have led to a continued softening of the reinsurance market, with renewal rates across the majority of classes in decline.

Reinsurance margins in some programs today stand at levels not seen for a generation[1]. Furthermore, investment yields are at historical lows, caused by the ongoing low yield environment that has persisted since the global financial crisis in 2007-08.

For reinsurance companies, this is a difficult environment to generate adequate risk-adjusted returns for shareholders, while maintaining current market share. As noted by AM Best, the continuing compression on investment yields and underwriting margins will ultimately place a drag on the financial strength of the reinsurance industry[2].

Reflecting the weakening fundamentals of the reinsurance market, AM Best has recently joined the other three major rating agencies in expressing a negative outlook for the reinsurance sector.

Underwriting profitability will not improve until the level of reinsurance capital falls below the demand in the market.

However, it is estimated a $100bn or greater insurance catastrophe event would be required to meaningfully disrupt market reinsurance pricing[1], and therefore the soft market is likely to persist for some time to come.

While there is no short-term solution to the soft market, reinsurers have greater flexibility to change their investment strategy, which, while weakened by the low-yield environment, can still be used to provide a cushion against difficult underwriting conditions.

Reflecting the weakening fundamentals of the reinsurance market, AM Best has recently joined the other three major rating agencies in expressing a negative outlook for the reinsurance sector, saying underwriting profitability will not improve until the level of reinsurance capital falls below the demand in the market

There are a number of different approaches to investment strategy within the reinsurance market, and the level of investment return among reinsurers in 2013 varied from below 0% to more than 21%, around a median return of 3.3% (see graphic).

This significant variance in investment performance reflects a number of factors, including the reinsurer's business model, its appetite for investment risk, level of capitalisation, and accounting environment. In Figure 1, we also provide an overview of the main investment characteristics of reinsurance companies, highlighting the key differences between global reinsurers, the Lloyd's reinsurers, and the new breed of hedge fund reinsurers.

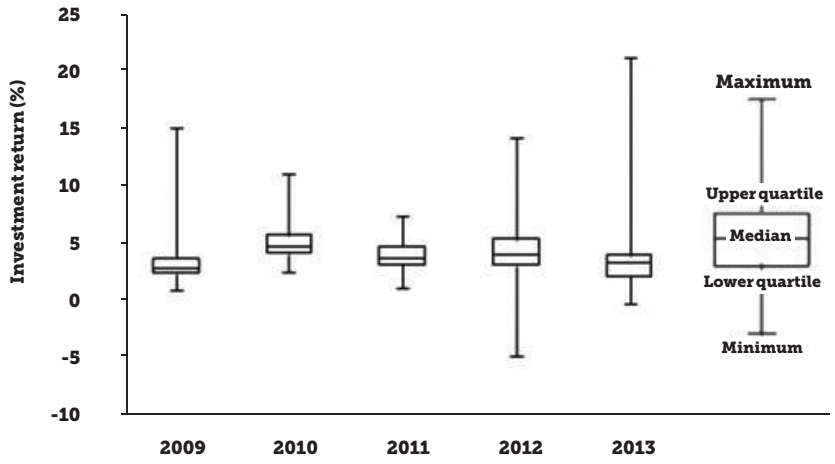
Global reinsurers

The world's largest reinsurers have the strongest investment capabilities, with large investment teams providing in-house expertise, and are hence able to employ sophisticated investment strategies. They hold well-diversified portfolios of fixed-income investments, including corporate bonds, asset-backed securities, private credit, and a small allocation to government bonds to provide liquidity.

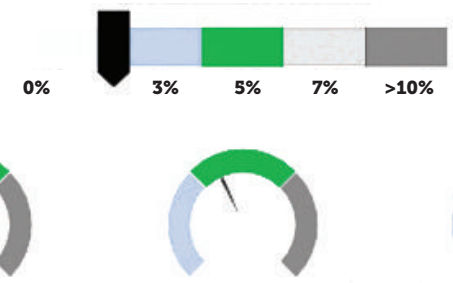
Outside fixed income, they hold return-seeking assets such as equities, real estate, hedge funds, private equity and infrastructure investments. On average over the past three years, the largest global reinsurers achieved stable investment returns in the 3.5% to 4.5% range.

We include the Bermudian reinsurance market in the global reinsurance category and highlight they follow a similar investment strategy to the largest reinsurers, except with less dedicated investment resources. Reflecting this difference, we see greater variability and less consistency in their investment performance. On average, over the past three years, the Bermudian reinsurance market achieved investment returns ranging from a little below 2% to nearly 5%, but with greater year-to-year volatility than their larger counterparts.

Figure 1: Reinsurance market investment performance



Investment return for Lloyd's reinsurer



Cash/sovereigns
- Up to 50% allocation
- Mark-to-market accounting drives investment risk aversion

Corporate debt/ABS
- High-quality allocation to corporate debt
- Some allocation to securitised credit
- Very short duration

Equity/alternatives
- Low appetite for return-seeking investments
- Only liquid alternatives considered, preferably UCITS funds

Source: Bloomberg, JP Morgan Asset Management analysis

Lloyd's reinsurers

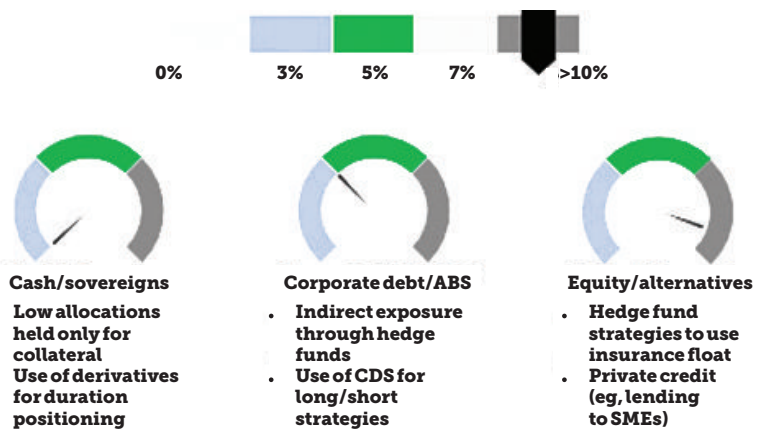
The Lloyd's market is still the most traditional of reinsurers in its approach to investment strategy. In 2013, the average Lloyd's syndicate held more than 50% of financial assets in cash equivalents and short-duration government bonds, and the remainder largely in corporate bonds.

This strategy has led to a continued reduction in investment performance since 2007, driven by the low-yield environment, and also the impact of the sovereign debt crisis[4]. There are several drivers of this low-risk investment strategy. First, a number of syndicates have small investment teams and are not resourced to manage the risks in a more complex investment strategy. Second, due to Lloyd's mark-to-market accounting environment, any investment volatility will have a direct impact on the syndicate's reported earnings. This is in contrast to the US and Bermuda, where reinsurers use an available-for-sale accounting treatment of fixed-income investments, under which investment gains and losses do not generally pass through the income statement, but through the other comprehensive income statement instead. Finally, many syndicates view their primary business objective as being a carrier of insurance risk and actively avoid allocating capital to investment risk.

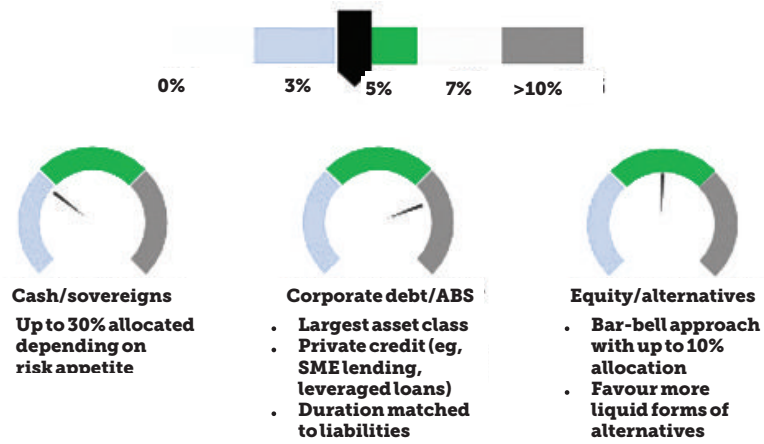
However, as reinsurance rates continue to decline, and syndicates seek to defend profitability, we are seeing an increased interest to build out investment capabilities and develop higher-yielding and more-diversified investment portfolios in the Lloyd's market.

performance

Investment return for hedge fund reinsurer



Investment return for global reinsurer



Hurricane Katrina: it is estimated a $100bn or greater insurance catastrophe event would be required to meaningfully disrupt market reinsurance pricing

Hedge fund reinsurers

A recent trend in the reinsurance market is the emergence of the hedge fund reinsurer. These entities generally aim to write low-volatility reinsurance business and invest the "float" (the money held to pay claims in the future) in hedge fund-type strategies. They normally hold little direct investment in fixed-income assets, although they may have some indirect holdings within the hedge fund allocation, and may use derivatives to match liability interest rate duration. In recent years, hedge fund reinsurers have generated investment returns as high as around 15% to 20%, but with significant volatility year to year.

Difficult underwriting conditions continue to persist, and without the occurrence of a significant insured catastrophe event, this is unlikely to change in the immediate future. In order to protect earnings as reinsurance margins compress, reinsurers should consider the role that investments can play during a soft market.

While many global reinsurers are well positioned to place a greater reliance on their investment portfolios, the Lloyd's reinsurance market may need to adapt its approach to avoid an ongoing strain on profitability. Maintaining market share comes at a cost, and in the longer term, we believe the most successful reinsurers will be those that can maintain sufficient underwriting discipline during this soft market, and supplement weaker reinsurance margins with robust investment performance. ■

Gareth Haslip is head of UK strategy and analytics, global insurance solutions, JP Morgan Asset Management

Notes:
1) Reinsurance Market Outlook, June and July 2014 Update, Aon Benfield.
2) Weakening Operating Fundamentals Tip Reinsurance Sector Outlook to Negative, August 19, 2014, AM Best.
3) Source: Bloomberg, JP Morgan Asset Management analysis
4) See Adapting investment strategies to the post-crisis environment, G Haslip, JPMAM, Insurance Day, November 28, 2013.

LAW & ORDER

Insurance industry must make compelling case for retaining block exemption

Sector is facing another anti-trust consultation

Yves Botteman and Guy Soussan
Steptoe & Johnson

The European Commission (EC) released a questionnaire mid-summer, seeking views of stakeholders on how the Insurance Block Exemption Regulation (IBER) is being used by the industry and whether the industry would be adversely affected by its non-renewal.

This questionnaire is the latest development in a long saga of consultations and inquiries that started in 2007 with the sector inquiry into business insurance in Europe.

The IBER was last renewed and adopted in 2010. At the time, following intense consultations with the industry, the EC was eventually convinced two forms of co-operation among (re)insurers were sufficiently unique and necessary to warrant their renewal:

At present the IBER:

1) Exempts information gathering and data exchange among (re)insurers to better assess the average cost of coverage of a given risk or, for life insurance products, the construction of mortality, illness, accident, or invalidity tables. The exemption encourages the industry to ensure the data collected is statistically significant and, hence, promotes participation in data exchange between the largest possible number of market operators, in particular national trade associations. In the same vein, it encourages parties to define as many risk categories as actuarially possible to allow for product and service differentiation by those making use of the compilations and tables; and
2) Exempts pooling of subscription capacity to facilitate the coverage of catastrophic risks, which otherwise would not be (re)insurable under economically acceptable conditions. The exemption for co-(re)insurance pools comes with certain conditions, including market share thresholds and the requirement to ensure the pool does not restrain the ability of participating (re)insurers to offer competing policies outside of the pool and to exit the pool without adverse consequences. In addition, co-reinsurance pools must not be used to align commercial premiums for direct insurance.

Importantly, the IBER – and the present consultation – does not cover ad-hoc arrangements on the subscription market, whereby a lead underwriter is appointed by a broker following a competitive call for tenders.

The EC took issue with ad-hoc arrangements in its conclusions following the business insurance sector inquiry, suspecting the subscription process led to de facto premium alignment between the lead insurer and followers.

In that respect, the EC commissioned EY to conduct a comparative study to assess the main differences and competitive issues associated with co-(re)insurance pools and ad-hoc arrangements. EY published its report in February 2013 (NB, it appears a new edition has been published by the EC in July 2014, following comments from several pools).

The report highlighted that clients valued pools to cover new risks for which it is difficult to assess the risk and the potential claims, or where the market might be unable to provide a solution. Conversely, ad-hoc arrangements were preferred where the client was looking for a bespoke solution. Concerning the risk of premium alignment, we merely note the report downplayed the issue. Specifically, it highlighted

i) the selection process leading to the appointment of the lead insurer is competitive and
ii) the implementation of the BIPAR principles provides an effective industry-led solution. Those considerations fall outside the scope of the present market consultation.

Given the very short timeframe between the report publication and this consultation, one would expect the EC to have sufficient data on pools. It should be guided by the extensive market findings contained in the report.

This time around, the EC will assess the extent to which the IBER is adequate and fulfilling its intended purposes. Specifically, the EC will assess the way in which the exemption has facilitated setting up and continued use of pooling arrangements and what effect non-renewal of the exemption would have on their availability to buyers.

Not so special?

The debate is likely to revolve around whether, assuming non-renewal of the exemptions, the general rules on co-operation among competitors – which apply transversally to all industry sectors – would be adequate and sufficient to provide the necessary antitrust guidance to co-(re)insurance pools. In other words, the question will be: "Is co-(re)insurance so special as to merit specific exemption rules?"

Another aspect of the EC's consultation investigates how the industry is using the IBER and whether the instrument facilitates and fosters antitrust compliance by co-(re)insurance pools. Worryingly, the report concluded "response rates to questions relating to self-assessment, relevant market and market shares were disappointing.

Some of these pools had not conducted a full self-assessment because they considered themselves exempted from covering new risks, or they were confident their market share was below the 20% threshold.

Overall, awareness of the IBER appeared mixed, though those pools that had reassessed their position since the issue of the new BER did not report a change in their compliance status.

We expect the EC to test further whether pools are making use of the IBER in their day-to-day compliance activities and, if not, whether non-renewal of the sector-specific rules would act as a wake-up call.

The above is not specific to insurance. In the past, industry-specific exemptions and safe harbours have been often wrongly interpreted by their beneficiaries as a blanket licence to operate. In fact, the EC has consistently reminded operators safe harbours do not mean firms are exempt from their duty to ensure business practices comply with antitrust rules, ie, whether their operations are within the boundaries of the safe harbour.

Industry exemptions are merely a tool to facilitate self-assessment as they take on board specificities that are not well captured by the general rules, but it does not mean companies can avoid conducting antitrust audits of their business practices. This is a common misunderstanding the Commission is keen to address.

In light of the foregoing, the EC has demonstrated growing scepticism towards industry-specific exemptions. This was already in evidence during the IBER renewal in 2010.

Not surprisingly, this consultation is aimed at assessing the likely impact of non-renewal of the IBER on co-operation among (re)insurers in the two areas mentioned above.

A serious option for the EC is therefore to let the IBER lapse and to force the insurance sector to come under the umbrella of the general cross-sectoral rules governing co-operation among competing companies.

To avoid such an outcome, it will be critical for the industry to provide compelling evidence the IBER instrument is not only useful to foster co-operation, but, more importantly, it is actually used and its conditions of application are well understood by the antitrust and compliance departments of insurers and pools across Europe.

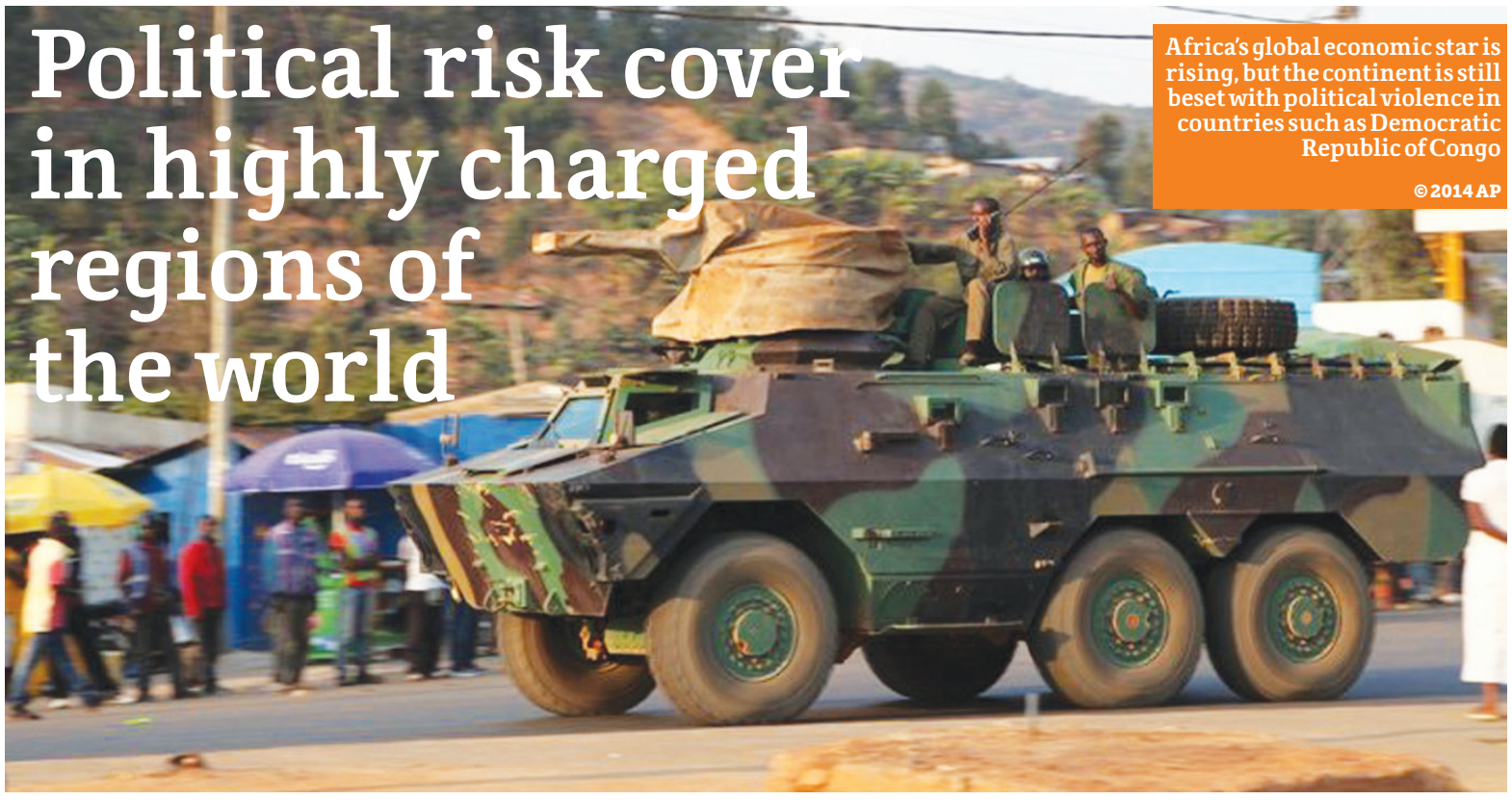
The EC is gathering input from all stakeholders and will reach a decision on the way forward by end 2015, early 2016. The current IBER expires on March 31, 2017. ■

Yves Botteman is an EU competition partner and Guy Soussan an EU insurance partner at Steptoe & Johnson in Brussels

The EC will assess the extent to which the IBER is adequate and fulfilling its intended purposes

Max Ebrahim
Clyde & Co

Political risk cover in highly charged regions of the world



Africa's global economic star is rising, but the continent is still beset with political violence in countries such as Democratic Republic of Congo

Many troubled 'hotspots' are also rich in mineral and other resources, presenting significant opportunities for multi-nationals, which may in turn be hit by trade sanctions

In the context of global trade and investment, the alleged shooting down in July of Malaysia Airlines Flight MH17 is significant for two reasons: it highlights the tension between globalisation and geopolitical conflict and it has, in stark terms, reminded us there are still a number of politically highly charged regions in the world where any activity carries significant risk.

However, one only has to look at, for example, the list of countries the Federal Aviation Administration (FAA) either prohibits airlines to fly over, or which it otherwise believes present a high risk to aviation (a list that includes Iran, Iraq, Libya and the Democratic Republic of the Congo and briefly, in July, also included a major airport in Israel), for it to be evident many of these troubled "hotspots" are also rich in mineral and other resources. They are therefore highly attractive to multi-nationals looking for new markets, presenting significant investment and trade opportunities.

Iran, in particular, presents an intriguing case. For decades, following the Islamic revolution of 1979 and the subsequent internecine war with Iraq, which lasted throughout the 1980s, it was considered a pariah state. Yet by 2010, Iran ranked sixth globally in attracting foreign direct investment. This achievement may, in some part, be due to the promulgation of the Foreign Investment Promotion and Protection Act (Fippa), which was introduced in 2002.

Iran's government has used Fippa to promote foreign investment, most particularly in the development of activities linked to industry, mining, agriculture and services aimed at, inter alia, upgrading technology.

Foreign investments made under the authority of Fippa enjoy a number of protections, including restrictions on expropriation or nationalisation of foreign investments (and, in the alternative, providing for compensation to be paid in circumstances where expropriation or nationalisation is "unavoidable and in the public interest").

However, central to the success of Fippa is art17, which makes provision for the procurement of foreign currency to pay yields on foreign investment, including purchases from the banking system by the Central Bank of Iran.

The impact of Fippa has been noteworthy: by 2008, firms in more than 50 countries had invested billions of dollars in Iranian projects or businesses. The opportunities created by this investment, however, have not been without their risks, particularly since the Iranian government began, once again, to court controversy.

By 2010, concerns in respect of Iran's nuclear arms capabilities were such that the US, the UN and the EU started taking proactive steps to heighten sanctions aimed at preventing international companies from operating in Iran.

Economic, trade or financial sanctions, which can range from freezes on the assets of, and travel restrictions on, nominated individuals (as we see in relation to sanctions imposed on Russia), to bans on the financing of state-owned enterprises, prohibitions on the supply of technical, financial and other assistance and outright prohibitions on trade, are imposed by governments or the UN to exert pressure on individuals or political regimes and for the advancement of foreign policy objectives.

The main aim of UN sanctions is to implement decisions by the UN Security Council to keep or restore international peace and security, whereas EU and US sanctions tend to focus on furthering their foreign or national security objectives.

US sanctions programmes have targeted foreign countries and regimes, terrorists, narcotics traffickers, activities related to weapons of mass destruction and others, and penalties for breach include fines and imprisonment.

In the UK, a person or company thqt breaches the terms of a sanction is guilty of a criminal offence, with a maximum penalty of seven years imprisonment or an unlimited fine.

The sanctions imposed on Iran impact on all dealings with Iranian companies by:

- Suppliers and advisers;
- Banks;
- International brokerages and insurance companies; and
- Staff and directors of these companies.

The most severe consequence has been the inability of Iranian companies to source sufficient foreign currency in the currency market to repatriate dividends to foreign companies that have invested in their businesses.

To illustrate the point with an example from Africa: according to its chief executive, MTN Group – Africa's largest mobile phone operator – has approximately $550m "stuck" in Iran due to the inability of MTN Irancell (in which MTN holds a 49% stake) to repatriate monies due. By March 2014, this situation had lasted nearly two years and, as yet, there is no indication when matters may be resolved.

Of course, this scenario is not unusual and the sums involved are often even more significant than MTN's $550m.

Furthermore, it is not only those regions beset by sanctions which present difficulties for foreign investors, including in relation to the repatriation of dividends.

Africa's renaissance, for example, presents a double-edged sword for investors: even though its global economic star is rising, with a consequent leap in foreign investment and development, the continent is still beset with political violence, civil wars, terrorism and uncertain government policy (especially in relation to the expropriation of assets and respect for the rule of law).

There is some irony in the fact that, of the 10 fastest-growing economies in the world, six are part of the same African continent that also houses six regions considered no-fly zones by the FAA.

Notwithstanding the risks of expansion into these regions and others like it, the opportunities for financial gain are sufficient that development is unlikely to slow.

The result is, alongside the usual and obvious due diligences and risk assessments that accompany such expansion, there is an increasing focus by companies operating internationally on the need to insure against political instability, including the risk of sanctions.

This remains, however, a small market, and cover for this kind of loss has become an undertaking which is often the sole preserve of syndicates or multiple insurers. In fact, in many instances, political risk cover is now underwritten by public agencies established for the very purpose of promoting the expansion of international investment and trade.

Policies tend to carry onerous trigger provisions and typically impose extended waiting periods before they respond. Atypical policy conditions tend to gravitate towards proper monitoring of the risk being insured and insureds therefore bear considerable responsibility for their own risk.

Quantification of losses is also a matter which can be complicated by matters like referral to assessors and is rarely straightforward. Disputes frequently arise and legal advice is always recommended.

While the mere purchase of political risk cover will not guarantee a safe passage, it will certainly go some way towards ameliorating the consequences of doing business in some of the world's more challenging areas. ■

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World Loss Intelligence

Tropical storm Polo threatens storm-weary Baja peninsula

Alexis Burris
Reporter

Another tropical storm has formed off the coast of Mexico as the Baja peninsula struggles to clean up the aftermath of hurricane Odile.

Tropical storm Polo is expected to strengthen to hurricane force. As of September 17, Polo had sustained winds of 45 mph and was located several hundred miles off the coast of Acapulco, Mexico.

The storm remains a threat to Los Cabos, Mexico, which was recently hit by hurricane Odile. Category three storm Odile brought widespread devastation to the resort town of Los Cabos earlier this week.

Damage to roofing, windows and flood damage was reported throughout the area.

In addition to property losses, significant business interruption is also expected with widespread power outages throughout the affected areas, as well as commercial property damage and possible beach erosion.

A woman looks at what remains of her house after it was destroyed by Hurricane Odile in Los Cabos, Mexico

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16 Named storms so far in east Pacific 2014 hurricane season of which

10 Have reached hurricane status

Robert Muir-Wood, chief research officer at Risk Management Solutions, said: "The insured losses in Cabo San Lucas are going to come from hotels, marina damage and also to high-value individual properties, which are likely to be insured through US-based insurers."

Hurricane Odile has weakened to tropical storm status and continued to move up the south-west coast of the US, bringing extreme rainfall to Arizona, which is still recovering from heavy rainfall from hurricane Norbert.

"We're expecting to see a combination of insured losses from Mexico and the US from Odile," Muir-Wood said.

The east Pacific hurricane season has been particularly active, with 16 named storms and 10 hurricanes. The average number of storms a year is 15, with eight reaching hurricane status. "We are seeing a particularly active year for hurricanes in the east Pacific compared to a relatively quiet Atlantic season," Muir-Wood said.

> **"We are seeing a particularly active year for hurricanes in the east Pacific compared to a relatively quiet Atlantic season"**
>
> Robert Muir-Wood
> Risk Management Solutions

Wildfire destroys 100 homes in northern California

Fire approaches the shore of Bass Lake, California; hundreds have been forced to evacuate their homes

© 2014 Yosemite Landscapes.com, Darvin Atkeson/AP

Property losses in California are climbing after a wildfire destroyed homes in the northern part of the state, *writes Alexis Burris*.

The Boles fire in northern California has damaged or destroyed 100 homes in the town of Weed near the Oregon border and is threatening more than 1,200 other structures, prompting the evacuation of at least 1,500 residents.

Late September 16, the fire had charred 375 acres but was only 20% contained. The blaze broke out on September 15 and was stoked by winds gusting up to 40 mph.

Cal Fire, the state's firefighting agency, has offered a reward of $10,000 for information leading to the cause of the blaze.

Dry, windy conditions in the state have prompted an above-average number of fires so far this year. US wildfires cost the insurance industry $385m in 2013.

California is one of the highest-risk states for wildfires, with nearly two million properties categorised as being at high or extreme risk in 2013. The state has historically experienced some of the worst fires in terms of insured losses.