

Conflicting Stakeholder Objectives and Decision Making in Insurance



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CASE STUDY

Introduction

Hareem Khan was having her morning coffee at Cluster Life. She was the Senior Sales Executive at a mid-sized life insurance company in Pakistan. In her three years at the company she had flourished as a sales person by selling group life insurance to huge companies, but lately her portfolio had taken some hits. She had recently lost two major clients in the banking and aviation sector to competition and was looking for new businesses to expand her portfolio.

Exhibit 1 - Hareem's Portfolio

Year	Portfolio Value (,000)	
	Renewals/Retention	New Business
2011	22,719	5,465
2012	23,397	6,121
2013	26,445	7,284
2014	22,154	7,939
2015	21,289	7,701

As the caffeine kicked in, Hareem noticed an email notification on her computer. The email was from Ejaz Akram, the Human Resource Manager at Crimson Auto Corp, an innovative and competitive automotive company in Pakistan. She was puzzled, but her expressions were mild at best. Ejaz Akram was not a stranger to Hareem, nor was Crimson Auto Corp.

Crimson Auto Corp. used to be Cluster Life's client in the years 2013 and 2014. Unfortunately in 2015 the company ran into some serious troubles and as a result it was running on reduced to low capacity for over a year. That meant cutting out on large expenditures that included, insurance covers, and missing scheduled premium payments, resulting in blacklisting. In 2016, the email from Ejaz Akram was proof that Crimson Auto Corp. had come back to life and was looking to get its employees insured once again.

Hareem saw an opportunity here, that too a big one. It was time for her to get working and generate a quote for this potential client, but will the management support her in this quest considering the fact that the word "blacklisted" was highlighted in bold letters in its history books? What about the other stakeholders at Cluster Life? Will the Senior Management be willing to take this client knowing the risks attached to it? And would the Management be similarly happy in associating its brand with a controversial client?

If there was anything Hareem vast experience in

insurance had taught her, it was the fact that each stakeholder had a different perspective. Will the different stakeholders at Cluster Life be able to reach a common ground and take a decision that was in the company's best interests?

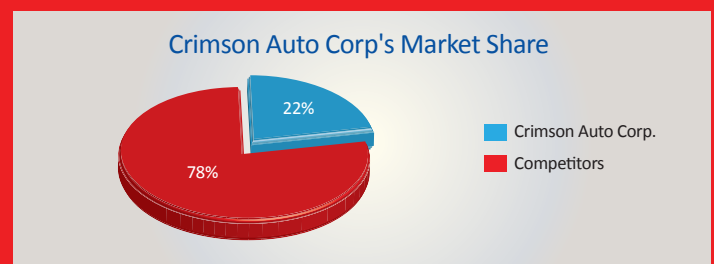
Crimson Auto Corp.

Crimson Auto Corp. was first established in the year 2010. Upon its launch the company had made it clear that it was going to bring high value semi-luxurious consumer vehicles to the market at a suitable price. Crimson was not a brand that associated itself with the term 'compromise', and it launched itself with a tagline that conquered millions of hearts of the population, "Because you deserve the best".

In its first year the company ended up selling 20,000 units across the country, and each year with the help of creativity the numbers kept on increasing. The competitors of Crimson Auto Corp. were having a tough time keeping up even though they were themselves doing well in a growing and spending economy. Nonetheless, the market share was dividing, and Crimson was after the biggest piece of the pie.

Exhibit 2 - Crimson Auto Corp's Sales

Year	Sales	Revenue (Billions)	Share Performance
2010	23,000	27.86	99.3
2011	25,530	35.70	113.6
2012	29,360	48.63	237.1
2013	35,231	58.36	489.0
2014	41,573	69.91	445.2



The reason why Crimson Auto Corp. was doing so well was because of its low cost manufacturing techniques that kept the price of its products significantly low, and its marketing techniques that reached out to the general public.

Unfortunately, Crimson's success was short lived, and before even celebrating its 5 year anniversary in the market, the company found itself in hot water with the government. It was discovered that Crimson Auto Corp's products were not as environmentally friendly as the company claimed. A statement was directly published by the

Environmental Protection Agency that read, “The entry of Crimson Auto Corp. in this industry was premature. The company has not only failed to meet environmental standards, but it has cheated and has continued to do so to make its products look green.”

The statement did not look good for the company. Further legal proceedings and research highlighted that Crimson Auto Corp. had minimum budget allocated to research and development, specifically for fuel efficiency. Moreover, employee exploitative manufacturing practices of Crimson also came into the limelight and they did not reflect well on Crimson Auto Corp. and on Cluster Life by association. Cluster Life had after all, been providing accidental death and disability cover to Crimson Auto Corp.

A legal case that was supposed to be solved behind closed doors in a courtroom in front of a jury was eventually brought to media’s attention, adding fuel to the fire. It was no secret that the competitors of Crimson were having a delightful time.

After a year in courtroom, the company was allowed to operate once again. Crimson paid millions in settlement, and was ready to start off from where it left, but there were some hurdles that it had to conquer first.

Management of Cluster Life

Danish Obaid, the General Manager of Group Life division of Cluster Life was the first person to know, after Hareem Khan, that Crimson was interested in bringing its business back to Cluster Life and on picking up the relationship from where they had left off.

Hareem Khan had nothing on her mind except the huge premium payments that Crimson was willing to bring. She wanted to expand her portfolio, and Crimson’s business would help massively.

While Hareem was thinking like a salesperson, Danish on the other hand had other considerations. He knew that the pressure from the sales side would be huge, but he needed to weigh out the pros and cons.

There were some factors that he had to keep in mind though. It was obvious that Crimson Auto Corp. had approached Cluster Life first and exclusively. If the management showed any time

lag in decision making, Crimson would not hesitate in contacting other insurance companies.

Looking at the sums at risk of the collective employees of Crimson Auto Corp., Danish had a clear idea that the premium amount would be significant. “Maybe this is the year we beat the Individual Division of Cluster Life”, Danish thought to himself, knowing the fact that the Individual Life division brought in 5 times more premium than the Group Life division in the past year.

Exhibit 3 - Cluster Life's Financial Highlights

	2011	2012	2013	2014	2015
Group Life Gross Premium (,000)	1,012,028	1,113,231	1,335,877	1,536,259	1,459,446
Investment Income (,000)	293,488	278,308	293,893	430,152	452,428
Claims (,000)	222,646	311,705	333,969	399,427	452,428
Profit After Tax Ratio	7%	8%	6%	6%	8%
Return on Equity	23%	28%	39%	33%	27%
Current Ratio	3.90	1.92	3.95	2.10	3.87
Price Earning Ratio	11.9	12.3	10.6	14.7	11.8
Dividend Yield	5%	8%	4%	8%	6%
Return on Asset	2.6%	3.8%	2.9%	3.0%	3.9%

“Guess what? Crimson wants us to pay all of the outstanding claims of 2014 as well”, Hareem casually added, interrupting Danish’s train of thought. By the end of 2014 when Crimson found itself busy with the legal proceedings, the company defaulted on a portion of premium payment. Due to this reason any claim intimated during that period was not paid. Crimson was now willing to pay that outstanding premium as well, but it wanted all the claims paid in full.

“How convenient”, Danish thought.

Risk Analysis

While the management and sales were playing their roles actively in this scenario, Usman Hayat, the Actuarial Manager of the Group Life’s division of Cluster Life had his own reading of the situation. Since he was the person who was supposed to approve the quote that was going to be presented to Crimson Auto Corp., he had to ensure that risk assessment was carried out as accurately as possible.

Usman was anything but short sighted. He always preferred to acquire businesses that had credibility, financial stability and continuity. Crimson’s credibility and continuity was questionable since

there was a default risk attached to it. The company could undergo yet another crisis and default on premium payments. Default risk was not something Usman had ever applied to his pricing model of insurance policies, and it was clear that an unconventional method was supposed to be adopted to price such scheme.

Usman calculated the mortality premium of Crimson, which was coming out to be 4,502,250 rupees. This was the pure cost that Cluster could expect to incur in the form of claims from Crimson. When Usman applied the claim experience of Crimson on his pricing model, the mortality premium increased to 6,020,250 rupees. He called this premium the 'experience rated premium' which Cluster could expect to incur in form of claims based on the client's past claim history.

Exhibit 4 - Insurance Coverage and Risk Analysis

Insurance Coverage Summary			
Category	Designation	Sum at Risk	Number of individuals
A	Executives	10,000,000	10
B	Management	3,500,000	200
C	Office Staff	1,500,000	450
D	Contractual	1,000,000	250
Total Sum Assured		1,725,000,000	
Average Sum Assured		1,895,604	
Average Age		39.5	

	Rate	Premium
Mortality	2.610	4,502,250
Experience	3.490	6,020,250
Demanded Premium by Crimson	3.900	6,727,500

* Rates are per thousand sum at risk

Crimson's Claim Experience		
	2013	2014
Premium	5,997,086	5,999,897
Claims	5,096,026	5,313,028
Loss Ratio	85%	89%
Outstanding Premium	-	650,000
Outstanding Claims	-	995,076

There were also some concerns about the health of Crimson's employees who were working in poor conditions. Usman knew that he had to put a lot of faith in the underwriters who would accurately calculate the death risks associated with the employees. The nature of work was something Usman was concerned about. Recently he had rejected insurance coverage to two companies on similar grounds. One company was involved in risky electrical wiring business, while the other had hundreds

of miners working in dangerous locations.

Usman quickly got to work while glancing at the total sum at risk associated with Crimson Auto Corp. He knew that Crimson's business was significant, but he wanted to consult the Marketing Head as well.

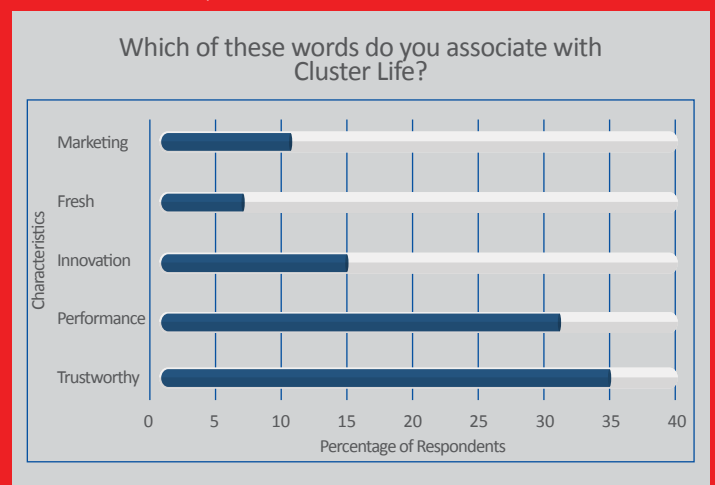
Brand Management

Naseer Khalid, the Marketing Head of Cluster Life with experience of over a decade in the insurance industry was also in the loop regarding the coverage demands of Crimson Auto Corp. It was also his responsibility to assist in executing and sustaining corporate strategic initiatives that might publicly impact the Cluster Life's image and when a client with such controversy had approached for insurance, that too with such a significant volume of business, he knew that he might be called upon to provide his own input.

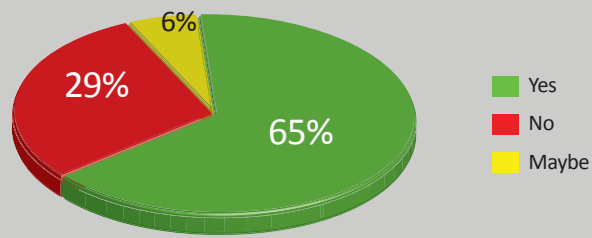
Naseer had been the Marketing Head of Cluster Life for three years, and in those three years he had worked very hard to build a strong brand image for his company. He did work closely with the marketing department to support exciting campaigns that not only boosted the company's sales, but also built a lot of credibility for Cluster Life that resulted in a positive consumer perception towards the brand.

There was one main factor that worried Naseer. Crimson Auto Corp. could find itself in legal issues once again, and this could affect Cluster Life's brand image. Naseer did understand that Crimson Auto Corp. was about to bring in a significant volume of business, but he also had to keep in mind the consumer perception of brands associated with controversial clients.

Exhibit 5 - Consumer Perception



Would your perception of the brand change if it had controversial clients?



There was an ethical issue as well that Naseer did not want to ignore. It was clear that Crimson Auto Corp. cheated its consumers and was not providing its employees with adequate facilities at work. He recalled that in the past several insurance companies refused to offer insurance coverage to a textile company which was popular for exploiting child labor. Would the same rules apply in this situation as well?

The Decision

This was not a normal working day at Cluster Life. The four stakeholders who are directly involved in the decision making process are in a difficult situation. It is evident that a controversial client has returned for insurance coverage for its employees and brought with it, a tricky decision to make. How will the different stakeholders arrive at a decision that both looks after the long and short term interests of the Company?