Rewriting the rules of corporate governance

Board of directors should use this time to review their organisation's objectives and understand how the organisation and its people will cope with significant change, says Mr John Crawley of GCC Board Directors Institute.

As we journey through the uncharted waters that COVID-19 has brought to our shores, board of directors are asking themselves if they are providing the right governance for their organisations.

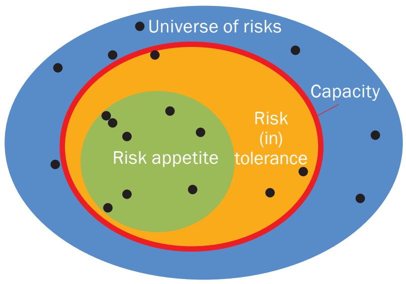
In times of crisis it is appropriate to reconsider an organisation's purpose. It is often the case, after a thorough search for this purpose, that without board intervention there is a real risk that organisations can continue to operate from behind empty statements of intent and broaden the gap between proposed purpose and tangible outcome.

Crises are never desirable, but when they are here, they force us to rethink and revaluate our direction, intentions and outcomes. We should "never let a good crisis go to waste", as Winston Churchill famously said. Board of directors must use this time to give a critical eye to their organisational objectives and be firm in their reassessments of them. This is especially the case considering how completely the pandemic has altered the nature and type of risk organisations are confronted with.

The dilemma

Do you take more risks and seek higher rewards while others are hunkering down and riding out the storm, or do you do as others are doing and hold on tight to mitigate further risk while the chaos whirls around overhead? To find answers to this conundrum, ask yourself three questions.

Figure 1: Risk appetite diagram



First, does your current board's 'risk appetite framework' reflect your COVID-19 reality? If you are not singing from the same hymn sheet as the wider world, you will soon find yourself as a lone voice, kicked out of the choir.

Second, if you are revising what is expected in this new normal, how are you reflecting those changes in the tonality and messaging from the top? For instance,

the expectation that staff must always report through their management structures any deviations from the norm, are they being offered and afforded the transparency from senior management engagement that their concerns and observations are being registered, investigated and looked into? Top brass cannot afford to lock itself away in a distant ivory tower and ignore the calls from those staffers on the ground witnessing and dealing with the real-world repercussions of the pandemic's disruption to daily life.

And third, are you proactively engaging with your regulators? As an insurance organisation you have a responsibility to engage regularly with your national regulator. As an example, the Saudi Arabian Monetary Authority (SAMA), reported in 2Q2020 a notable increase in insurance companies' combined solvency ratio and a decrease in investment income. It goes without the need for over-emphasis that these results have a direct impact on board members orchestrating their organisational directives and future moves. One can only imagine the kind of catastrophic consequences of strategies formed without prior knowledge of what's happening in the market from the regulator's perspective. Are you having these risk appetite conversations within your organisations?

However, it is one thing having knowledge and access to the market data and shifts, and another being able to act on them. And this leads us to a term that you will hear more often in the coming months: organisational resilience. The ability of an organisation to take and recover from a shock is, naturally, the need of the hour.

Coping with significant change

In a PwC report 'Middle East insurance industry – beyond COVID-19' published in May this year, several insurer responses were identified in the wake of the pandemic. They included the suspension of policies and policy rebates due to a disrupted value chain; early access to policy benefits and delayed regulatory changes and levels of supervision; financial support packages for vulnerable clients including delayed premium payments and easing of penalty fees; changes to cashflow interactions with stakeholders; and conducting scenario analysis and stress testing.

With this context in mind, a key consideration from a governance perspective is to understand how the organisation and its people can and will cope with significant change. For insurers, we should be looking at three means of achieving this.

- Absorbing – can the organisation and its people absorb change? Can it deal with or without interruption?
- Adapting – can the organisation and its people adapt to change? This generally means people are taking on extra activities and sometimes displacing existing tasks which may be putting the organisation at higher risk. This trade-off is an important consideration to make.
- Transforming – typically managed under a 'change' programme requiring investment in people, processes or assets, transformations require deep strategic thinking and planning.

With these measures in mind, board members should pay particular attention to change that requires too much adapting. This will create additional risks that can compound the already strenuous workflow and strain on a company's time and resources.

In the GCC countries in particular, we have seen regulators increase their powers with the aim of protecting both consumers and the market. In other parts of the world, this would be categorised as 'conduct risk'. For boards and the executives of insurance companies, the challenge is to understand the pace and substance of new regulations, especially because COVID-19 will continue to accelerate the pace of change in digital insurance.

Key areas of focus

For instance, Deloitte surveyed insurers from Europe, the Middle East and Africa earlier this year and concluded that there are clear areas in which leading insurers need to focus, including new solutions for the new customer base, a different roadmap for growth, and negotiating better deals.

Interestingly, 57% of respondents said they believe the most efficient way to build customer loyalty is through access to friendly and knowledgeable staff. Meanwhile, regulatory obstacles were considered a key challenge over the last three years, and 45% of respondents believe that rapidly evolving customer needs will be the next challenge for insurers.

According to the data, more than a third of insurers generate 30% of their income today from service-based, rather than product-based businesses. And this is predicted to rise to over 60% in the next three years. By 2024, 33% of premium volumes will come from brand-new propositions. These are the evolving market conditions that insurers must adapt to if they are to remain relevant in the long term.

Furthermore, 72% of respondents to Deloitte's survey believe that half of industry growth will be driven by M&A activity within the next five years, with 52% expecting to complete two or more M&A deals in the next three years.

Given these sentiments, board directors must ensure, now more than ever, that their organisational purpose is pursued and the organisation is resilient to change and agile enough to deal with the change that tomorrow brings.

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