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**Professor Emeritus Boris Marović, PhD**

BOOK REVIEW

## **RISK MANAGEMENT IN INSURANCE AND REINSURANCE**

*Author: Professor Vladimir Njegomir, PhD*

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*Number of pages: 551*

A lot of effort and time that the author of this book, Professor Vladimir Njegomir, PhD invested in highlighting the issues of risk management in insurance and reinsurance proved worthwhile. The book came about as a result of an endeavour to integrate all novelties in risk management, insurance and reinsurance, and respond to future challenges.

This monograph is a result of good many years of author's research dedicated to the subject area and draws on the present studies, projects, published articles and books of the Professor Vladimir Njegomir, PhD.

Professor Njegomir focuses his research on insurance, risk management and reinsurance and is one of the most prolific young scientists. He holds dual PhD degree in structured finance in insurance and reinsurance and in the analysis of interrelationships between insurance and entrepreneurship. In 2001, he was awarded as the best student in his generation. He was employed in two London-based finance software companies, and worked as an advisor to the Department for Strategic Planning, Corporate Governance and Business Analysis of Dunav Insurance Company. He is currently employed at the Faculty of Law and Business Studies as an associate professor where he holds the position of a Vice Dean of Scientific Research. He is the author and a co-author of 14 published books and more than 150 papers, where over 20 papers were published in the leading journals of M20 category. For his scientific research, he was awarded by the National Bank of Serbia in 2011. He is an editor-in-chief of a scientific journal *Civitas*, a member of the editorial board

of the journal *Svet osiguranja*, and a member of the Balkan Scientific Association of Agrarian Economists and the International Insurance Society.

The monograph of Professor Njegomir was positively assessed by three peer reviewers, the doyens in the area of insurance: Professor Emeritus Boris Marović, PhD, Professor Zdravko Petrović, PhD and Academician prof. dr. phil. habil. Wolfgang Rorbah. Peer reviewers stressed that the issues addressed in the monograph were logically organised, presented in simple yet technical terms, and in a systematic and explanatory manner for easy reference. Since the book is all-encompassing it enables the reader to learn about general and specific milestones in successful risk management. The book is particularly interesting for its descriptions of all relevant concepts and numerous practical examples. Peer reviewers recommend the book to insurance professionals, customers of insurance companies, students, and all those who show interest in the complex issues it addresses.

In writing the monograph, the author used a vast body of literature comprised of more than 306 sources, 33 charts, 56 pictures and 12 tables. The book is a harmoniously structured work composed from preface in the Serbian and in the English language, notes, literature, glossaries of technical terms, terminology list and information about the author. It includes 17 logically arranged chapters written in five hundred and fifty one pages using standard line spacing and typeface.

*Chapter one* is dedicated to the concept of risk. Nature of risk is analysed where feelings attached to the risk are considered as well as its definitions and determinants. Relationships between the risk and uncertainty, peril and hazard are considered subsequently. Particular attention is paid to different types of risks: financial, non-financial, dynamic, static, fundamental, particular, pure, speculative and enterprise risks. The connection between a risk and economic growth is particularly considered.

*Chapter two* deals with the analysis of different aspects of insurable risks. The characteristics of an ideally insurable risk are firstly considered: the risk must be determinable, there must be a large number of exposure units, risks should be homogenous, independent from one another and, ideally, they must not be catastrophic. The loss occurrence must be fortuitous, unintentional, whereas the economic consequences and likelihood of the loss occurrence must be determinable. Probability of a loss must be low, whereas the risk should be in accordance with the public interest. Subsequently, types of insurable risks are discussed – personal, property, liability risks and risks relating to errors and omissions of others.

In *chapter three* the author defines the main concepts, links and relationships in risk management. He expands the definition of risk management and explains the need for such expansion. The author also places risk management in a strategic context, namely, stresses the importance of dedication to risk management as a strategic commitment and key commitment of corporate governance. Detailed elaboration

is provided regarding the functioning and importance of risk management in the circumstances of new solvency regulation in the European Union – Solvency II. The focus is placed on innovative solutions in risk management. The author stresses that in a modern business environment, the integrated risk management, which entails simultaneous management of all risks, is a must. Finally, the author draws attention to new positions and importance of directors and the risk management committee.

*Chapter four* is fully dedicated to general approach to risk management. Firstly the definition is provided and then the importance and limitations in risk management are analysed. The subject of risk burden and necessity of its management is analysed in detail, particularly in relation to individuals, organisations and society at large. Doing this, the author explains the fundamentals underlying the need to manage risks and implement insurance. Subsequently, risk tolerance and factors determining such tolerance are considered, whereafter risk management process is discussed in detail. Firstly, the author addresses goal-setting issues in risk management followed by risk identification and assessment and eventually, the management of risks. Within that subject, the author deals with risk control and financing i.e. the use of avoidance, prevention, reduction, transfer to insurance and other risk transfers. Subsequently, the actual implementation of risk management process and continuous monitoring thereof are considered. Innovations in that area, more precisely, the application of integrated risk management and information technologies as a support to that process are covered in detail.

*Chapter five* connects risk issues with those relating to insurance. The concept of insurance is analysed from different perspectives, namely, from the economic, technical and legal perspective. The emergence and history of insurance worldwide and in the region of former Yugoslavia is described in detail. Subsequently, main characteristics of insurance are considered such as risk transfer, fortuitous losses and indemnity. Attention is focused on economic significance of insurance, notably in terms of property protection, credit improvement, commodities exchange and trade, fund raising, efficient allocation of capital and social function, as well as economic costs of conducting insurance business whereby adverse selection, moral hazard and insurance frauds are considered. Economic principles of insurance were elaborated in detail: solvency, liquidity, profitability and cost-effectiveness.

*Chapter six* is dedicated to risk management issues which concern insurance companies. To that extent, it was pointed out that in order to ensure the basis for solvency and thus long-term sustainability, insurance companies need to simultaneously manage risks and capital. Subsequently, probability theory and the law of large numbers are considered together with the innovative approaches to quantification of insurance risks i.e. the role of risk modelling in insurance risk management. Natural catastrophe risk modelling and modelling of man-made disasters were particularly analysed. Relevant attention was focused on the real-life deviations

from the calculated mean values and on the management of risk correlation in the risk portfolios of insurers through insurance reserves and risk transfers utilised by insurance companies.

*Chapter seven* lays out the elements of insurance: subject of insurance, insured perils, insurance premium, insured event, and insurance indemnity. The views on insurance premium also include the significance of bonus and malus and deductible, whereas the section dedicated to insurance indemnity considers the issues of the insurance sum and the sum insured.

In *chapter eight* the author points out the concept, significance, relationships and specific characteristics of insurance market. The issues of insurance industry existence and operations in market economy are discussed. Insurance market determinants, those of demand and of supply, are explained in detail where particular importance is placed on respective price and income elasticity of demand and significance of capital for insurance supply. Subsequently, this topic covers all actors in insurance market: insurers, Lloyds syndicate, insureds, policyholders, insurance beneficiaries, holders of ownership rights over the insured object, acquirers of insured object, third party claimants, insurance agents and brokers, agencies dealing with the provision of other services in insurance industry and insurance and reinsurance pools.

*Chapter nine* covers different aspects of operations of insurance companies. Activities of insurance companies are analysed in relation to actuarial science, underwriting, marketing in insurance, claims management and the role of insurance companies as institutional investors.

*Chapter ten* is dedicated to regulating insurance industry and insurance contracts. Considered are the areas that are subject to regulations, the insurance law (as the most important source of rights arising from insurance), EU conventions and directives, and the special attention is paid to the review of a new EU Directive - Solvency II. The attention is subsequently devoted to the insurance contract, more precisely, the conclusion of insurance contract, terms and conditions and rules of insurance, and the judicial practice.

*Chapter eleven* considers the issues and analyses specific characteristics of property risks. This chapter deals with all types of property risks and key characteristics of property risk coverage such as the requirement that there is an insurable interest, that there is a purpose of property risk coverage, that the requirement for the prevention of the occurrence and salvage of the object insured is met, as well as the coverage of the loss by insurance, abandonment of an insured object, and destruction of an object due to an event not specified in the policy. The author also focuses his attention on overinsurance, underinsurance, multiple insurance, assignment of insurance contract and payment of insurance indemnity to another

person, as well as the assignment of the insurance rights toward a responsible party onto insurers.

*Chapter twelve* deals with the liability risks. This chapter considers the concept of insurance liability, subject matter of insurance, insured perils, liability insurance premium, sum insured, characteristics of the liability insurance contract, and the indemnity arising from liability insurance.

*Chapter thirteen* covers life insurance risks. The risks of death and survivorship were particularly considered in the context of life insurance, accident insurance supplementary to life, annuity insurance, unit linked insurance plans, and within the issues concerning life insurance lines from the perspective of a policyholder.

*Chapter fourteen* addresses the issues of catastrophe risks and their impact on insurance business. In particular, the attention is paid to the definition of catastrophe losses and the risk determinants of their occurrence, the impact of catastrophe losses, trends and causes of their occurrence including climate changes, terrorism, and earthquake risk. In addition, the implications of catastrophe losses on risk insurability are considered. The author points out that the present circumstances are such that catastrophe losses are becoming more frequent and destructive and impact the limitations of risk insurability, which in turn creates a need for cooperation in the insurance market between public and private sector.

*Chapter fifteen* considers the role of coinsurance in risk management. This chapter provides the definition and explains importance of coinsurance, types of coinsurance business, and characteristics of coinsurance contracts. Advantages and weaknesses of risk transfer from insurance to coinsurance are defined.

*Chapter sixteen* is dedicated to the analysis of the reinsurance role in risk management of insurance companies. This chapter provides the definition of reinsurance, background of its development, deals with individual characteristics such as the international character of reinsurance business, particular specialized insurers, universal character of reinsurance treaty, risk volume, compulsory as against voluntary character, and long-standing business relations. Similarities and differences in reinsurance and other forms of risk transfer made by insurance companies are subsequently analysed in connection with coinsurance, insurance pools or insurance or coinsurance and capital market instruments. The importance of insurance for insurance companies and macroeconomics is clearly defined. Considered are main terms used in reinsurance such as risk portfolio, self-retention and maximum probable loss, maximum possible loss, and probable maximum loss. Insurance principles are analysed in detail where special attention is paid to the following documents: insurance slip, cover note, reinsurance certificate and bordereaux. Thereafter, types of contract i.e. facultative treaties and reinsurance treaties are analysed in view of their bulkiness. In addition, in view of the obligations assumed by reinsurers, the subject of analyses are proportional reinsurance treaties which include quota share

and surplus reinsurance, and non-proportional reinsurance treaties which include per risk excess of loss reinsurance cover, per event excess of loss reinsurance cover, catastrophe excess of loss reinsurance and eventually, stop loss reinsurance. Finally, the attention is also paid to the limitations in the risk transfer to reinsurance.

*In chapter seventeen* the issues concerning alternative risk transfers in insurance are considered in a quite unique manner. These alternatives notably appear as a supplement to the traditional insurance risk transfer to reinsurance and are used when the capacities of reinsurance and retrocession markets are limited. The concept, relevance, history, advantages and disadvantages in the application of particular forms of alternative risk transfer are highlighted. Special attention is given to finite risk reinsurance, instruments of conditional capital, insurance derivatives and reinsurance sidecars, whereas the greatest focus is placed on risk securitization - particularly non-life catastrophe risks. Finally, analysed are the issues of present advantages and limitations in development as well as possibilities of further development of new risk transfer forms complementary to the traditional reinsurance.

In its scope and with the specific issues it covers, the book is notably intended for professionals. Professionals, corporate clients of insurance companies, entrepreneurs, management of insurance companies (particularly at the strategic level) and insurance brokers and agents are the ones who will mostly benefit from its reading. In addition, the students studying economics and law may find useful the reference literature contained therein, whereas the book will be of interest to all those who wish to learn about the complex issues of risk management, insurance and reinsurance.

*Translated from Serbian by: **Zorica Simović***