CHAPTER 12

UNDERWRITING.

Credit risk underwriting in this report refers to the following three activities:

1. The assessing of a prospective client’s:
   - Debtors book;
   - Bad debt experience;
   - Credit control policies and administration;
   - General degree of exposure to credit risk resulting from the prospective client’s market position;
   - Financial position, and
   - Integrity.

The reason for this assessment by the credit insurer is to decide whether he should accept the prospective client as a policyholder. If so, the information and its assessment are required in order for the underwriter to frame the terms and conditions of the policy (including the premium rates) he would be prepared to offer. This part of the underwriter’s work is hereafter referred to as “policy underwriting.”
2. The assessing of the credit risk\(^{45}\) pertaining to a particular debtor\(^{46}\) of the policyholder so that the credit insurer can decide whether to accept the risk for underwriting purposes and, if so, the level and terms and conditions of the credit limit\(^{47}\) on the debtor. This part of the underwriter’s work is hereafter referred to as “credit limit underwriting.”

3. The evaluation of country risk (political and economic) on importing countries so that the credit insurer can decide on the acceptability of such country risk and the relevant premium rate and terms of cover. This activity is referred to as “country underwriting.”

**POLICY UNDERWRITING:**

For the purpose of this report it is assumed that a credit insurer offers three different types of credit covers:

- Domestic credit insurance.
- Short-term export credit insurance.
- Medium-/long-term contracts cover.

Please refer to chapter 10 “Introduction to Credit Insurance” for an explanation of these products.

**CREDIT LIMIT UNDERWRITING:**

Credit limit underwriting is confined to domestic and short-term export credit insurance. The policies for these covers are merely frame agreements, setting out the administration details, the terms and conditions of the cover in general and the premium cost. The credit insurer will then issue credit limit annexures to the policy document, being cover notes for each of the policyholder’s debtors stating the amount for which the insurer is prepared to go on risk for such debtor and detailing any special conditions subject to which the

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\(^{45}\) Credit risk means the risk that a debtor may not be able and/or willing to pay a legally binding debt, which is due and payable.

\(^{46}\) As a rule credit insurers cover risks on businesses only, not on private individuals.

\(^{47}\) A credit limit is the amount, which the credit insurer covers as a maximum on the relevant debtor and should ideally represent the amount owed at any one time by the debtor to the policyholder. A credit limit can carry conditions, e.g. security requirements such as guarantees or other types of security.
credit limit has been approved. For instance, a steel merchant will have as customers many different engineering, building and manufacturing firms. The credit insurer would investigate the credit worthiness of each of these clients and establish appropriate credit limits. Thus the insurer may agree to cover credit up to a limit of R500 000 on firm “A”. The relevant credit limit annexure to the steel merchant’s policy may state that such insurance cover is only of force provided the policyholder has obtained the personal guarantees of the directors of “A” for all amounts owed by “A” to the steel merchant. Should the policyholder not comply with the condition he would not enjoy cover on “A” and would have to bear any loss as the result of “A’s” demise entirely for his own account.

COUNTRY UNDERWRITING:
Due to the “political” risks cover in short-, medium- and long-term export credit insurance policies, country underwriting needs to be practiced by the credit insurer. It evaluates the degree of risk that payment may not be received for an export due to political actions enacted after the exporter has lost control of the goods, such as the placing of restrictions on the importation of the goods/services forming the subject of the export or prohibiting the transfer of funds for settlement of the debt resulting form the export transaction. A country’s possible inability, due to economic circumstances, to make available the necessary currency required for payment of the debt resulting from the import, and other similar hazards, are also part of country risk assessment.

ETHICAL PROBLEMS THAT CAN ARISE IN UNDERWRITING.

1. Domestic and short-term export credit insurance policy underwriting.
   a. The underwriter could be tempted to purposely mislead by formulating a credit insurance offer which is most advantageous to the insurer but which may be unsuitable or unnecessarily comprehensive and thus expensive for the prospective client. Alternatively, the underwriter could deliberately disadvantage the insurer

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48 In medium-/long-term contracts cover the credit limit is included in the policy document because it is specifically drawn to cover one contract only.
in order to bring the policy on the insurer’s books or to favour the prospective client for some other reason, e.g., collusion.

b. Carelessness on the part of the underwriter can lead to the issue of an inappropriate policy at the expense of the client or the insurer.

c. The underwriter could make promises that cannot be kept, e.g., offering to issue a particular credit limit, extending cover for exports to a market not acceptable to the insurer, undertaking to provide unrealistically speedy decisions (credit limit underwriting as well as claims) or offering future premium reductions.

d. Where only a limited amount of political cover is available on a particular export market, the underwriter has a duty to ensure fair distribution among needy policyholders. It would be unethical to prefer one exporter over another without valid reasons, e.g., the larger, better, loyal policyholder may deserve some preference.

e. Because the credit insurance product is complex and its value for a new prospective client not that easy to assess, it is difficult for a purchaser of credit insurance to gauge the reasonableness of the premium cost, which can allow the underwriter to quote a premium rate that is unfair compared to like risk profiles. The market for credit insurance is not very transparent due to asymmetry in information/knowledge. This puts a greater responsibility on the insurer to treat clients fairly.

f. Policy wordings can be unclear, ambiguous and not easily understood. Insurance policies are often full of “small print”.

g. When difficulties or conflicts between the policyholder and the insurer arise, the policyholder may not know who to turn to for unbiased advice. This is particularly so if the policy was not bought through a competent insurance broker.
h. Due to the nature of a credit insurance policy the policyholder needs to be able to communicate easily and instantaneously with knowledgeable, trustworthy people in the insurer’s office. If the insurer is not able to make such people available to the policyholder it will lead to frustration and loss for the policyholder and the insurer.

This list highlights unethical behaviours, i.e., deliberate or careless actions by the underwriter/insurer, which result in unfairly disadvantaging the client or the insurer. As has been said earlier, respect for the dignity and autonomy of others is basic to Kant’s ethics. Building and protecting a business’s reputation and strengthening the trust it can expect from its stakeholders is vital for the long term success of a business and cannot be achieved without heeding Kant’s call. Reputation and trust depend on reciprocity in open, fair dealings, in giving credence to the need for moral behaviour. If the competition with which the credit insurer has to contend is not very strong and if the broker market is not sophisticated, it is of course much easier for the underwriter/insurer to get away with unethical behaviour toward the client. But even in a very competitive environment, the credit insurer has to guard against complacency because the complexity of the credit insurance product will, even under such circumstances, allow unethical behaviour.

The following are suggestions that, if implemented, can help to avoid such unethical behaviour:

- Underwriters should have explicit instructions not to suggest a type of credit insurance policy that is inappropriate for the prospective client. For instance, where a prospective client has a large number of small customers, don’t insist on insuring them – it is usually in the client’s best interest, from a cost and administration point of view, to be his own insurer for such small, well-spread exposures. It is the large debtor’s account which can have a devastating result for the client if that debtor defaults, that should be covered by credit insurance. If the
client deals with some AAA accounts, such as Anglo American or Coca Cola, the insurer should be prepared to exclude them from cover if the customer so desires but only after having made the consequences abundantly clear in writing to the prospective client. In export credit insurance, an exporter does not, under certain circumstances, have to offer for cover his exports to all his export markets. The pros and cons should be clearly explained to the prospective policyholder.

- The company culture should guide all staff members not to make promises that cannot be kept.

- The insurer should make it a rule that the terms, conditions and administrative requirements of the policy are carefully explained to the prospective client. An easily understandable “Policy terms and Conditions” booklet should be available to the prospective clients, but it should be pointed out that the policy wording is final and that non-compliance with the terms and conditions of the policy may prejudice any claim that the policyholder may have.

- The insurer’s underwriting instructions should make it clear that underwriters are to be consistent and fair in the setting of premium rates. Like risk profiles should carry similar premium rates unless there are good reasons for variations.

- Segmentation of the risks accepted by the credit insurer is even more important than segmentation in marketing. The credit insurer’s risk universe needs to be subdivided into:
  1. Industry levels (primary, secondary, tertiary etc.);
  2. Trade levels (mining, manufacturing, wholesaling, retailing, etc.);
  3. Legal entities (listed, public, private companies, partnerships, etc.);
  4. Geographical areas (countries, provinces, cities);
  5. Size categories (aggregate exposure per risk in value bands);
  6. Risk quality (poor, medium, good, etc); and
  7. Causes of loss (insolvency, protracted default, repudiation, etc.).
Declared insured turnover or debtors balances, premium income, claims paid and salvages received need to be allocated according to these segments so that underwriting has a sound foundation for establishing premium rates. Such statistics are also needed to ensure that the insurer does not accept too much risk in one particular segment and thereby endangers the stability of the business. Reinsurance arrangements (see chapter 14 “Reinsurance”) are also based on these statistics and in case of need they allow the insurer to act quickly where a particular segment is suddenly exposed to a considerable change in its risk profile, e.g., a natural disaster, such as the recent Tsunami, which may result in a serious increase in the risk of business failures in the effected region.

Not only are these statistics necessary in order to direct the business but they are a manifestation of a professionally run organization that is able, at least to some extent, to perform its underwriting duties ethically. However, that is only true of statistics that are based on a sufficiently large sample. Statistics are usually not 100% reliable because of too small a sample and because significant factors influencing the risk do not remain constant, e.g., random fluctuations in claims – that is the unpredictable bunching of a number of large claims (in line with the Monte Carlo fallacy\(^\text{49}\)) or due to a gradual change in the risk factors. Even if the statistical picture would be totally reliable, the market may not bear the “correct” premium (due to the insurance cycle or because of competitive pressures or reinsurance availability) or the insurer may, for business reasons, accept the business at inappropriate rates.

Other statistics that help to pitch premium rates at the right level are:

- Credit insurance association (Berne Union and ICISA) statistics which provide world wide credit insurance experience per cause of loss and geographical area.

- National statistics concerning liquidations, insolvencies and the establishment of new businesses.

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\(^{49}\) The fallacy that although when tossing a coin, over the long run, more or less 50% of the time it will show heads and 50% tails, this does not mean that if heads has not come up for some time heads must be “due” to come up at a greater than one-half probability. The probability of heads coming up remains one-half for each toss.
Industry association statistics, e.g., building industry bad debt experience.

Individual policyholder statistics, e.g., bad debt ratio.

While reinsurance (see chapter 14 “Reinsurance”) provides an umbrella against random risks and changing risk factors, the insurer needs to be permanently vigilant and alive to constantly altering perils.

- As is known, insurance is based on the collection of comparatively small amounts of premiums from many for the settlement of losses sustained by the few. Is it ethical to take premiums from many people who may never have a claim? I think it is because:
  - No one is forced to buy insurance.
  - Everyone who buys it knows it is quite possible that one may not incur an insured loss and thus collect an indemnity.
  - The assumption-of-risk theory explains why premiums paid for possibly one’s whole life during which no losses have been sustained have not been paid “in vain”. The insured has transferred the chance that she might suffer a loss to the insurer and it is for the assumption of this risk, the hazard that he may have to pay an indemnity, that the insurer is entitled to the premium.
  - Moreover, in credit insurance not just insurance is provided. The credit limit service and other advice available from the insurer are of considerable use to the policyholder and are there to help avoid losses in the interest of both the insured and the insurer.

- Is it equitable that all policyholders, whose insured risk profile is similar, pay more or less the same premium rate notwithstanding that they may be in very different economic circumstances? According to Rawls’s difference principle, economic inequality is justified provided it is to the greatest benefit of the least-advantaged members of society. Small and/or poor businesses clearly benefit from the considerable premium contributions of large, well-off organizations. Not only do the payments of the latter increase the pool out of which claims can be paid but, their contributions
also help in reducing the premium cost for all. In fact, without the large and wealthy organizations being part of the insuring community, there would probably be no insurance scheme and this would hit the small and/or poor businesses hardest because they can least afford sustaining a loss.

An insurance premium rating system based on risk profiles and not on the insured’s ability to pay is therefore basically fair. But insurers are pressed into and generally agree to give premium rate discounts to large, good clients and such premium reduction can, if overdone, lead to the distortion of the insurance pricing mechanism. If taken to extremes, such discounting would result in every insured paying a premium more or less equal to his claims and that would of course negate the reason for and the principle of insurance. Thus insurers must be circumspect in discounting premium rates for reasons that are not strictly based on the overall risk profile into which the insured falls.

- Any special arrangements agreed with the prospective client must be in writing, preferably within the policy document.

- While it is unavoidable that credit insurance policies include quite a number of terms and conditions, they should be worded clearly, unambiguously, in user-friendly language and print. So-called “small print,” as well as highly technical terms and complex wordings, should be avoided at all cost. The policy wording lays down what is expected from the client and it must be made quite clear that non-compliance may result in the repudiation of a claim or the withdrawal of the entire policy. The client (who in credit insurance is always a business) can be expected to be a fully rational being, capable of understanding the credit insurance contract, and it is therefore fair and ethical that he be held fully responsible for his errors and omissions, as long as the insurer has complied with his duties.
• A final policy should wherever practical be delivered to the new client by both the sales person and the underwriter who will service the policy. This will ensure that no promises are made which the underwriter cannot keep.

• The policy should give all the relevant details of the Insurance Ombudsman so that the policyholder can refer any dispute he may have with the insurer for evaluation to the ombudsman. The policy must obviously comply with all the disclosure requirements laid down by the South African Financial Services Board and the credit insurer needs to comply with the industry’s code of conduct, e.g., the code of ethics designed by the South African Insurance Association for the South African insurance industry.

• Although many credit insurance policies are sold through the intermediary of an insurance broker, it is important that direct, personal contact is made at the earliest possible time between the prospective client and the relevant expert staff of the insurer. Due to the intimate understanding that the underwriter needs to have of the client’s business and because of the continued interaction that needs to take place between these two parties, clear, direct (with copy to the broker) communication between the policyholder and the credit insurer is vital for an efficient and satisfactory relationship between all the parties involved so as to avoid misunderstandings and delays and help build a good, trusting relationship. Sales personnel and underwriters must, in addition to being experts in the technical aspects of credit insurance, have good personal relations skills, be sensitive to a client’s needs and be aware of the implications of their own fiduciary position vis-à-vis the client, broker and the public in general. An enthusiastic, open, helpful and entirely ethical attitude is required in order to

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50 Personal knowledge by the underwriter of the prospective client’s business is very important so that the underwriter can consider whether the insurer should offer cover. A business that does not have the ability to administer a credit insurance policy or one that is clearly unethical should not be granted credit insurance in order to avoid difficulties for both parties at a later stage. If cover is granted, the underwriter needs intimate knowledge of the policyholder’s business so that he can offer the most appropriate type of cover and provide an efficient service to the policyholder.

51 There can be a multitude of communications that have to take place between the two parties, even in one day, because of the constant change in the policyholder’s debtors book.
represent the credit insurer in a proper manner and serve the client professionally. (For the broker/insurer relationship refer also to chapter 11 “Marketing and Sales”).

- The underwriter must advise the prospective client before selling him a policy if cover on one of his export markets is not available or can only be provided on restricted terms. For example, the credit insurer may have no capacity or only a limited amount of cover available on a particular export market. Alternatively, the credit insurer may be prepared to grant insurance cover only for a certain market on restricted payment terms (only on letter of credit or cash against documents terms of payment etc.). Perhaps no transfer of funds cover can be offered or no credit to government departments or institutions is available. If the prospective client can purchase only commercial or only political risk cover, he needs to be told and the implications clearly explained. Usually an exporter does not have to offer for cover his exports to all the countries he sells to. Again this needs to be discussed and the advantages/disadvantages pointed out.

- If relevant, the underwriter should explain the effects that the credit insurer’s reinsurance arrangements for political risks may have on the exporter.

- The credit insurer should audit the administration of the credit insurance policy on a regular basis (both in the client’s and its own offices). This will ensure that both parties comply with the terms, conditions and undertakings and will avoid the position later where the insurer repudiates a claim due to non-compliance. Such checks will help the insurer in making certain that he receives the premium due to him, and they will foster good relations and assist the insured in case difficulties are experienced in administering the policy.

- The underwriter should not feel any trepidation if called on to disclose decisions and actions to a superior, the CEO or the board of directors – this is a measure of ethical, fair and correct dealings by the underwriter.
• Prompt, professional service by the insurer is vital for the client to obtain full value from his credit insurance policy. It is therefore helpful for all parties concerned if the insurer has at regular intervals a market research study done by an unbiased third party to gauge the quality and speed of service and the market’s perception of the insurer’s product. Such market research reports are an excellent basis for a constant effort by the insurer to improve his service and build a satisfactory and loyal clientele.

2. Medium-/long-term contracts policy underwriting.

The ethical problems that can arise in domestic and short-term export credit insurance policy underwriting as listed above can to some extent also appear in contracts underwriting. The remedies would be similar to those mentioned there, but, due to the size, complexity and possible social, political and/or environmental effects of large projects, additional ethical questions arise in contracts policy underwriting with which the insurer has to deal:

a. Tendering for and negotiating such large projects involves the exporter in considerable time and expense. In order not to waste such effort and costs, the insurer should be able to advise the exporter in advance of the availability of credit insurance cover and export finance. However, international political and economic circumstances can change very fast with the result that export credit insurance on a particular country may no longer be available or only conditionally accessible at the time the tender is awarded.

b. The importance of the under-mentioned issues need to be discussed with the exporter:
   • The level of equity required to be invested by the promoters of the project;
   • The local content stipulations\(^{52}\);
   • Payment guarantees/security requirements;

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\(^{52}\) In many cases a minimum percentage of the value of the export contract has to originate from the export credit insurer’s country of domicile in order for the contract to be eligible for the credit insurance cover.
• The need for feasibility studies;
• Environmental impact studies;
• The legal enforceability of the export and finance contracts, any guarantees, and other pertinent documents and payment mechanisms in both the exporting and importing countries;
• The possible requirements of export/import permits and operating licenses;
• The need for a special letter of approval of the contract from the government of the host country;
• Foreign exchange approvals;
• The availability of the necessary infrastructure and inputs (funding or physical material/labour) from third parties;
• Logistical problems and
• Administrative requirements.

The above should all be drawn to the attention of the exporter and need to be resolved in a manner that will allow the credit insurer to support the proposed project with credit insurance/finance.

c. The credit insurer will not wish to underwrite a project proposed by an exporter who is not capable (financially or technically) of executing the proposed export contract or who appears to act unethically (wanting to use shortcuts, employing deceptions, refusing to provide information etc.). The insurer’s risk will be considerably higher due to the likelihood that the exporter will not perform in terms of the agreed export contract or due to legal disputes or incorrect behaviour on the part of the exporter.

d. Certain types of goods/services may not be acceptable to the credit insurer for underwriting purposes, or may require special security conditions due to past bad experience with such projects or because they are ethically not acceptable.
e. A credit insurer should not support the exports of armaments or other military supplies into a volatile region unless there are special circumstances that justify supporting the side fighting the war and wanting to purchase the weapons. A “just war” (28. Singer, 1993: 386) could be described as one that is fought:

- In national self-defense;
- In defense of another state against external aggression;
- To recover rights previously lost in an unjust aggression against the party that lost the rights;
- In defense of fundamental human rights;
- To punish an unjust aggressor;

and provided that:

- Not more violence than is required to achieve the aim is used;
- The bad consequences do not outweigh the expected good consequences of the war; and
- It is fought only against persons who are legitimate targets of attack.

f. The credit insurer should not support projects that will have negative environmental or social implications unless there are very strong mitigating circumstances.

g. Although a project may produce jobs, profits, foreign exchange through exports and tax earnings for the host country, the affected population in that country may be seriously opposed to the project because it might pollute, destroy recreational or ecologically sensitive areas, damage the tourist industry, be aesthetically unacceptable or clog up the infrastructure.

h. The credit insurer must also keep in mind international conventions, values and laws when considering an application for credit insurance for a large capital goods export project.
i. Where the insurer knows that the project to be exported is clearly not viable, he should not support it.

Many of these issues are difficult to solve. The obvious solutions are often contrary to the interests and wishes of the exporter and/or the importer. The credit insurer should promote export business in the interest of his client, the exporter, and also the exporting country’s economy. But the credit insurer should at the same time not aid unethical or back non-viable projects. The long period involved from conception of the project to realization and final payment make the risks difficult to assess and the ethical issues particularly complex.

Here are some guidelines that may help in approaching the ethical questions raised:

- The credit insurer must assist the exporter in the negotiation of the export contract and the related financial agreements so that they are in line with the credit insurance requirements. This includes advice as to the likelihood of the availability of cover for the contemplated project and about any foreseeable special conditions that may attach to such cover. In this way the credit insurer alerts the exporter to any obstacles that may be in the way of a satisfactory insurance and financial package required to realize the export business. It also gives the exporter an opportunity to withdraw from the business if cover is not available or if the exporter finds the requirements too onerous, before having spent too much time, effort and expense in pursuing the project. Some credit insurers will provide the exporter with an undertaking – usually valid for a 3 months period, which can be extended – that in principle, cover for the particular project will be made available within the period of validity of the undertaking. A commitment fee is payable by the exporter for such an undertaking.

- The credit insurer should help the exporter to deal with the issues raised in b. above. While the credit insurer cannot have all the expertise required for matters such as legal opinions, technical studies and other expert reports and inputs that
may be necessary, the insurer has a moral obligation to point out to the exporter that such preconditions, documentation and requirements may be needed. Clearly, it would be unfair and unethical not to advise the exporter of such preconditions because, in terms of Kant’s categorical imperative, the exporter’s dignity, which is grounded in the capacity for practical rationality, would be squashed as the exporter would be precluded, due to the insurer’s negligence, from doing the correct thing founded on all the relevant information. It is the exporter’s duty to comply with all such conditions and the credit insurer’s advice is given without obligation. Non-compliance by the exporter could lead to the non-issue or withdrawal of cover or the repudiation by the insurer of a claim at a later stage.

- It is the insurer’s obligation to advise the exporter immediately should he not wish to support him for a particular project. Where possible the credit insurer should tell the exporter of ways and means to overcome the shortcomings, e.g., by suggesting that the exporter works together with a financially sound or technically capable partner. The insurer has a duty of care toward the exporter because he is the specialist in the field of export credit insurance and finance and therefore possess insights that the exporter may not have. Through the credit insurer’s advice the export may be won on a basis acceptable and advantageous to all parties. As previously mentioned, it is the credit insurer’s duty to encourage sound export business rather than to stand in its way.

- If the credit insurer feels that he cannot support a project or can only do so subject to particular terms due to the type of goods/services that are to be exported, he must communicate such fact to the exporter immediately and alert him to restrictions or special conditions that may be require in order to afford insurance cover to such exports. Some examples of problematic projects are:
  o Credit insurers have experienced many problems with the repayment of loans made available for the financing of contracts for the building of hotels. Often these difficulties are due to political, economic or security changes that adversely affect the tourist industry and thus the occupancy rate of the hotel.
To make such a proposed export contract insurable may require special payment guarantees and mechanisms and a higher equity investment by the promoters than may be needed for other types of projects.

- Casino building projects can raise serious ethical problems. Their undesirable effects on some members of society, who may not be able to withstand the lure of gambling, need to be carefully considered by the credit insurer before he decides whether to support such projects. There are no established guidelines to help resolve such questions but it might be worthwhile to discuss the issue with the government of the importing country, with religious and labour movements and relevant NGOs in the host country. The credit insurer needs to avoid espousing a paternalistic attitude but if the local community and government are strongly opposed to gambling it is likely that the credit risk inherent in the project is considerably higher. The culture of the importing country may not support casinos and under such circumstances it would be foolish for a credit insurer to extend his facilities to such a project (see also chapter 5 – Cultural Relativism).

- Where credit insurance cover for the exports of armaments and other military materials is under consideration, guidance from the exporting country’s department of foreign affairs as well as from the United Nations could be sought before a decision to cover such business is made. The definition of what a “just war” is in ethical terms (see page 133) can also be drawn on, although this is a description still under debate in philosophical circles.

- When a credit insurer has to decide whether to provide support for a project that has negative environmental implications, he may experience considerable difficulties in arriving at a decision that is fair to all participating parties. Where there is no doubt that a project will have severe adverse impact on the ecology, the credit insurer should, for ethical and risk reasons, refuse to provide insurance cover. We have a responsibility towards all rational beings. Ignoring serious ecological problems that will result from a project only so that the exporter can succeed in winning a lucrative order at the expense of the affected population is
disregarding their human rights and dignity, is treating them, in Kant’s language, merely as means. The problem lies with projects where it is not entirely clear what their ecological impact will be. While an environmental study provided by the exporter may well indicate that the impact is nil or minimal, a similar study by an independent expert may show that there is a major ecological problem with the project. A third study provided by the importing country’s government might yet again say something different, depending on the importance of the project to the government concerned. While the findings of an independent expert should be decisive, the exporter and importer may have valid counter arguments, particularly considering that the study of the environment is not an exact science. What should guide the export credit insurer in deciding? The following may be of help:

EQUATOR PRINCIPLES. 25 international banks involved in project financing have agreed to what they have called the “Equator Principles”, which they designed to help them to ensure that any larger ($50 million or more) projects they become involved in are socially responsible and environmentally sound.

Export credit insurance, the same as project financing, plays a major role in worldwide economic development and therefore has considerable leverage in backing and promoting ecologically friendly infrastructure, production and service projects and ensuring that socially responsible, ethical practices are employed in

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53 At June 2005 the following 31 international banks had signed the Equator Principles: Australia: Westpac Banking Corp.; Belgium: Dexia Group and KBC Bank N.V.; Brazil: Banco Bradesco, Banco do Brazil, Banco Itau and Unibanco; Canada: Canadian Imperial Bank of Commerce, Royal Bank of Canada and Scotiabank; France: Calyon Corporation and Investment Bank; Denmark: Eksport Kredit Fonden (Export Credit Agency); Germany: Dresdner Bank AG, HVB Group and WestLB AG; Italy: MCC S.p.A.; Japan: Mizuho Corporation Bank, Ltd.; The Netherlands: ABN AMRO Bank NV. ING Group and Rabobank Group; Spain: BBVA S.A.; Switzerland: Credit Suisse First Boston; United Kingdom: Barclays plc, HSBC Group, Standard Chartered Bank and The Royal Bank of Scotland; United States: Bank of America, JPMorgan Chase, Citigroup Inc. and Manulife; European Union: European Investment Bank. In 2003, 23 of the above banks arranged US$55.1 billion of project loans using the Equator Principles. This represented 75% of US$73.5 billion project loan market for that year (64. Equator Principles).
the execution and subsequent operation of such projects. The “Equator Principles” provide that for all projects likely to have significant adverse environmental impact, or that will have potentially adverse environmental impact on human populations or environmentally important areas, finance should be made available only provided that:

a) An Environmental Assessment (EA) satisfactory to the lender has been completed.

b) The EA has addressed all of the following points:
   o Assessment of the baseline environmental and social conditions.
   o Requirements under host country laws and regulations, applicable international treaties and agreements.
   o Sustainable development and use of renewable natural resources.
   o Protection of human health, cultural properties, and biodiversity, including endangered species and sensitive ecosystems.
   o Use of dangerous substances.
   o Major hazards.
   o Occupational health and safety.
   o Socioeconomic impacts.
   o Land acquisition and land use.
   o Involuntary resettlement.
   o Impact on indigenous peoples and communities.
   o Cumulative impacts of existing projects, the proposed project, and anticipated future projects.
   o Participation of affected parities in the design, review and implementation of the project.
   o Consideration of feasible environmentally and socially preferable alternatives.
   o Efficient production, delivery and use of energy.
   o Pollution prevention and waste minimization, pollution controls (liquid effluents and air emissions) and solid and chemical waste management.
o Compliance with applicable host country laws, regulations and permits required by the project.
o Compliance with the minimum standards applicable under the World Bank and IFC Pollution Prevention and Abatement Guidelines and
o Compliance with the IFC Safeguard Policies.
c) An Environmental Management Plan (EMP) based on the EA and which suggests mitigations, action plans, monitoring, management of risk and scheduling.
d) The lenders must be satisfied that groups affected by the project, including indigenous peoples and local NGOs, are consulted in a structured and culturally appropriate way, which includes making the EA available to the public for a reasonable period in local language and in a culturally appropriate manner. An independent expert advice and review can be called upon by the lenders.
e) The buyer/borrower has undertaken to
  o Comply with the EMP in the construction and operation of the project.
o Provide regular reports, prepared by in-house staff or third party experts, on compliance with the EMP and
  o Where applicable, decommission the facilities in accordance with an agreed Decommissioning Plan.
f) If necessary, lenders have appointed an independent environmental expert to provide additional monitoring and reporting services.
g) In case of need the lenders will engage with the borrower/buyer and seek solutions to bring the borrower/buyer back into compliance with its covenants.

As the EA demands, the basic facts about the ecological or social problems need to be well understood. If not, individuals will differ about the action that should be taken, not because they have different ethical standards but because they hold different factual views. The need for a good understanding of the issues involved when deciding on the morality of supporting a project is the same as the absolute requirement of defining and agreeing the problem accurately when trying to solve
a dilemma in business as discussed in chapter 8 “How to deal with Dilemmas in Business Ethics”.

The “Equator Principles” comply with the normative ethical theory of Kant (the demands of the categorical imperative (see pages 11-17) and Sustainable Development (see chapter 3 “Sustainable Development”). A project that complies with the “Equator Principles” will be in line with the categorical imperative because the principles force the promoters/contractors and financiers to:

- Consider all people affected by the project;
- Treat those affected not merely as means but as ends-in-themselves;
- Protect the dignity and autonomy of those concerned by informing them properly of the project and by consulting the effected community;
- Take into account not only those presently affected but also future generations; and
- Bear in mind that any decommissioning of the project needs to be carefully planned.

The benefit distribution of a project that complies with the “Equator Principles” is also likely to be the most acceptable, complying with Rawls’ “difference principle” (see pages 24 to 26). A project that damages the environment and ignores the social and health needs of the population may on the face of it be cheaper to build and as a result may have a better profitability, but its benefits will be distributed only to its owners, employees, and the state in the form of taxes. The poor who are detrimentally affected by the project are likely to receive none of the benefits, but have to endure all the harm it causes. A project that complies with the “Equator Principles” will ensure that the harm is minimized, that the benefits are fair and sustainable (provided the completed project turns out to be economically viable) and that those who are affected by it, who are not employed by the project and who are worse off, will at least receive some benefit from the
project as a result of the growth of the economy in the region, possible improvement in health care, schooling and other amenities.

Complying with the “Equator Principles” and thus Kantian moral theory should generally be of greater importance to the host country than utilitarian (see pages 8 to 10) justifications because the concern of the affected people – even if they are a minority – cannot be overlooked if the project is to be an economic and political success. The complexity lies in balancing the social and environmental harm against the economic benefit. As Beauchamp and Bowie point out in their book *Ethical Theory and Business Practice* (30. Beauchamp, 2001: 22): “The problem with utilitarianism is to decide whether units of happiness can be measured and compared in order to determine the best course of action. In deciding whether to open a pristine national wildlife park to coal mining, for example, how does one compare - in terms of utilitarian theory - the combined values of an increase in the coal supply, exports, jobs and consumer purchasing power with the value of wildlife preservation and environmental protection?” The categorical imperative and Rawls’s Justice as Fairness provide a more satisfactory guide. Rawls requires a decision from people in the original position, from behind the veil-of-ignorance, as this process will produce a rational answer, not one based merely on a guess as to which action may in the future maximize utility. All the facts, but no partisan views, are taken into consideration in this decision-making process and thus a fairer, more just decision is taken. The categorical imperative forces taking affected peoples’ needs into consideration, not only of present but also of future generations. It demands that monetary returns do not trump people, and that careful thought be given to the maxim, the principle on which the final action is founded – it must be universalizable.

The crucial issue is that the “Equator Principles” must be correctly implemented, and here the credit insurer could perform an important role. Although these principles are very ambitious and somewhat idealistic, I believe credit insurers should strongly promote them and make their cover dependent on their adoption.
Finance draw-down certificates should be approved by the credit insurer only if he is satisfied that up to that stage of the project the “Equator Principles” have been complied with or, if there are difficulties, acceptable steps have been taken to ensure rectification. Naturally, there will be exporters and/or importers or borrowers who will have all kinds of reasons as to why the principles cannot or should not be applied to their particular project. Credit insurers may have to be flexible but they should push hard for the adoption of the principles and should demand valid reasons for non-compliance before considering approval of credit insurance cover. This is obviously an area where lenders, credit insurers, exporters, governments and other relevant parties, such as NGOs, should co-operate, exchange experiences and develop refinements to the “Equator Principles”. Such co-operation can only be in the interest of all parties involved and will be of great significance to the socially healthy and sustainable development of projects and economies (see also chapter 6 “The Importance of Institutions”). The credit insurance industry, via its international associations, should develop a common policy of backing these principles. As has been pointed out in chapter 3 “Sustainable Development”, ecologically efficient projects can be more cost-effective than environmentally unfriendly ones.

The “Best Practical Environmental Option” is defined in King II (50. King, 2002: 112) as that option that has most benefit, or causes least damage, to the environment at a cost acceptable to society.

Now that the Kyoto Protocol is coming into operation after the long awaited ratification by Russia, the market mechanisms to help the parties to the Protocol achieve their national emission targets at lowest cost will be established. These will allow, among others, a contractor/exporter in an industrialized country to earn emission credits by funding an ecologically friendly project in a developing country. Credit insurers should be fully aware of these new mechanisms because they can help to reduce the costs of projects and support sustainable development.
Credit insurers should consider such projects more favourably when deciding on underwriting terms and conditions.

Credit insurers, financers and exporters must be seen to act legally and responsibly in their support of large projects as has been demonstrated by the Shell Brent Spar case (see page 45). The media takes great interest in big projects and can seriously harm the reputation of the parties involved if they act unethically.

A credit insurer cannot be a moral preacher – it is not his duty to ensure that everyone does the right and good thing, but he has a duty to support what ever can be done to turn an ecologically unfriendly project into an environmentally friendly one, keeping his own interest in mind. Underwriting projects that seriously injure the environment cannot be in his long-term interest because it increases the credit risk\textsuperscript{54} and is likely to result in severe criticism of the credit insurer and even the exporting county. What about projects that prove ecologically damaging only after they have been completed? Provided all reasonable precautions, investigations and enquiries were made before the project was implemented and all indications were that the project would be ecologically acceptable, neither the insurer, nor the financier or the exporter should be held responsible. Kantian ethics is not dependent on the outcome but rather on the Good Will with which the project has been undertaken. That means the project must have been willed rationally by a free agent, employing reason only and acting from duty and on a maxim that is universalizable (see page 11). As the parties concerned with this project seem to have complied and thus acted from Good Will, their action would be ethical. The project’s environmental problem would rest with the importer and the importing country’s government. The purchaser of a project accepts certain risks and this would include the

\textsuperscript{54} A project may, because of its ecological problems, not be viable; both politicians and the local people may attack it; it may stir up international condemnation or be harmed by Green Peace; it could be severely detrimental to the economy of the host country.
environmental risks. It may however rebound on the export credit insurer if, as a result of ecological problems, the importer does not pay.

- The credit insurer should not support an export contract that makes provision for unduly large commissions. Although customs and conditions vary from country to country, commission rates, other percentages or rake-offs that are not in line with internationally accepted, ethical practices may hide bribes and corruption and must therefore not be supported by a credit insurer.

- Providing support for the export of machinery to a country where child labour will be employed to operate it may be ethically wrong, but without knowing the full details of the circumstances prevailing in the importing country, it may be very paternalistic and even harmful to the children involved if the export does not take place due to the credit insurer’s refusal to provide the required cover. The insurer needs to obtain the relevant information before making a decision.

- A project that may have as its object the plunder of the natural resources of the importing country for the benefit of some external party should not carry the support of the credit insurer.

- Where the insurer knows that the contemplated project is clearly not viable, he should not support it. This is in the insurer’s own interest (increased payment risk) as well as in the interest of the importing country, where it will damage the local economy. So-called “white elephant” projects, such as a palace for the despot of a poor country, have been the source of many financial and political problems, and credit insurers have a duty to help prevent them. Such projects are unethical because the country’s resources – its tax revenue for instance – are used for the sole pleasure of the ruler; the resources are stolen from the community. Society is treated by the dictator merely as a means and the act is not compatible with Kant’s Formula of the Kingdom of Ends (see page 13).
• The “Berne Union”, the international association of export credit insurers, which has as its members most export credit insurers in the world, agrees on maximum credit terms for particular types of projects in order to prevent ever longer terms of credit and so as to make sure that the size of a project and the type of goods/services involved receive appropriate credit conditions. Credit insurers need to comply with these international agreements.

• Finally, the reader’s attention is drawn to chapter 5 “Cultural Relativism” which deals with the question of ethical conduct in other countries.

3. Domestic and short – term export credit limit underwriting.

1. The credit insurer markets himself as an expert in credit risk evaluation. The policyholder relies on the insurer to advise him in a highly professional manner about the credit risks involved in his business. Should the insurer not live up to the trust placed in him he will incur losses for both the policyholder and himself and will have abused the policyholder’s faith in him. A central aspect of the credit insurance policy is negated and the insurer will have forfeited his raison d’etre through his unprofessional behaviour. The policyholder has good reason to discontinue his relationship with the insurer and could even have a legal case against the insurer for breach of trust.

2. An underwriter who does not take sufficient care in deciding whether to accept or reject a particular credit limit acts unethically because he:
   • Does not provide the professional service to which the policyholder is entitled;
   • Does not do the job for which he is employed, trained and receives his salary;
   • Probably damages the business of the buyer by denying credit facilities.
   • Damages the buyer’s reputation by advising the policyholder that cover on the buyer is not available.
   • May preclude the policyholder from transacting some profitable business;
• Prevents his employer from earning the premium he could have earned if the risk is in fact acceptable and a credit limit had been issued;

• Exposes the credit insurer and the policyholder to unreasonable risk if he underwrites the limit\(^{55}\) even though the risk is unacceptable.

• Acts in bad faith: It is often so that the insured knows more about his client than the credit insurer. Due to the insured’s duty of utmost good faith (uberrima fides), the basic insurance principle forming part of all insurance policies, the policyholder is obliged to advise the insurer of any adverse information he may have about the buyer and to refrain granting credit to such a buyer, without specific prior approval by the insurer, even if a valid credit limit on the buyer is in force. This duty of utmost good faith should not be a one sided obligation. The credit insurer (underwriter) should have a similar responsibility towards the policyholder.

• May lose the client for the insurer due to his uncaring attitude.

3. Granting credit insurance facilities that are too generous, too restrictive or subject to inappropriate conditions (e.g., guarantees or other security provisions such as cessions of debtors or bonds, etc.) may have similar consequences as mentioned above and is therefore also unacceptable. Credit limits that are unreasonably high will induce the buyer and the policyholder to overtrade with a concomitant increase to the credit risk. This should not be seen as paternalistic but merely as responsible credit management.

4. Some people believe that credit loss predictability indicators should not dominate business because they encourage risk-avoidance. Those advocating this stance believe that risk taking is the essence of business. Encouraging risk taking enhances business growth, we are told. While I fully agree that risk taking is unavoidable in business, it would be unethical to accept risks willy-nilly or

\(^{55}\) The policyholder may incur a loss due to the co-insurance clause, which is found in most credit insurance policies. The clause means that the insured will only be indemnified a percentage (usually 80\%) of a loss, the insured retaining for his own account and uninsured the remainder of the loss. The reason for the co-insurance clause is that it should induce the policyholder to act prudently and with due care in all his credit transactions.
consciously entering into highly risky transaction only because they might help
grow one’s business. It is unethical because high risk is synonymous with a high
chance of loss and because loss is usually harmful to others, e.g., creditors,
shareholders and society, in addition to the agent himself. It is immoral to
recklessly or carelessly accept high risk (see also page 165). Weighing the risk
carefully before venturing into the transaction is therefore the right thing to do.
Credit insurance is a sensible tool for protecting the creditor from major bad debt
losses and for safeguarding that credit is extended to reasonable risks. The credit
insurer will use financial and other relevant information including viable
prediction indicators in deciding whether to underwrite a risk. But clearly the
insurer has to be prepared to accept risk, otherwise he would not have any
policyholders and there would be no justification for the credit insurance product.
The market forces the insurer to be a risk taker and it is the credit insurer’s job to
try and turn unacceptable risks into acceptable ones and thus enable business to
flow where it otherwise may be blocked. This can be brought about by, inter alia,
security arrangements, more in depth credit investigations or by negotiations
between the creditor, debtor and the credit insurer. As has been pointed out
elsewhere in this report, the large numbers and the wide spread (over industries,
geographical area, size, etc.) of exposures enable the credit insurer to accept more
risk than a single supplier is capable of absorbing. The insurer also acts as an
excellent distributor of the costs associated with bad debts. A tiny premium
charge paid by all insured creditors covers the bad debt losses of the few suppliers
who might well be forced into liquidation themselves had they not taken bad debt
insurance.

5. Delaying credit limit decisions unnecessarily represents not only poor service but
is also unethical because of the adverse consequences (e.g., not being able to
satisfy the buyer’s needs) all concerned parties will suffer. But by the same token,
taking decisions too quickly is also detrimental. As mentioned earlier, care is
required and it is better to provide a quality decision a little later than a poor,
careless decision quickly.
6. An underwriter must guard against being unduly influenced by either the policyholder who is pressing for the cover in order to execute a profitable order or by the buyer who is interested in obtaining as much suppliers’ credit as possible. In many instances the buyer will use all manner of tactics to talk the credit insurer into providing insurance cover to his suppliers. The underwriter is in a conflict situation vis-à-vis the policyholder. Excellence of service to the policyholder is and must be his aim. Policyholders frequently use this and the personal relationship that develops between them and underwriters as a tool to try and squeeze more cover out of an underwriter than is justifiably acceptable.

7. Collusion between buyers, policyholders and underwriters can lead to considerable losses for the credit insurer.

8. Information obtained form a policyholder needs to be kept strictly confidential. Imagine the consequences if the credit insurer were to pass on details of one policyholder’s debtors to another or if he would tell a competitor of the policyholder about the trading details of the policyholder. All information about the debtor - the credit risk - must also be treated with great circumspection. Leaking such information may damage the debtor’s business and can lead to a defamation action against the insurer.

9. Underwriters have mandates within which they can bind the insurer to credit risks accepted by them. By exceeding an underwriting mandate, an underwriter can expose the insurer to substantial risks/losses.

10. Problems can also arise with the allocation of a limited amount of available cover. The credit insurer must avoid preferring one policyholder above another and so

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56 Supplier’s credit is usually the cheapest form of credit and often obtainable without having to reveal information which the buyer would prefer to keep to himself.
57 This is usually so because the buyer’s business cycle and limited own capital requires substantial, external finance, funding that may not be available from his banker and/or is more expensive.
channel trade to one at the expense of another policyholder. To clarify: The insurer will be prepared to underwrite a certain maximum amount on a particular risk. If he receives applications for cover from a number of clients which in aggregate vastly exceed this maximum, the insurer will have to allocate the available cover between the various applicants. It would be unfair (and against Rawls’ Justice as Fairness principle – see page 24) were the underwriter to give the total available cover to just one policyholder, thereby allowing this client to trade with the risk on an insured basis to the exclusion of all other policyholders.

11. It would also be incorrect for an underwriter to knowingly underwrite fraudulent and/or unethical businesses. Such action would expose the credit insurer to additional risks, would misdirect resources and would be contrary to the interests of the community at large.

12. The more difficult risks (size, complexity and/or quality) need to be underwritten with particularly great care, attention to detail, caution, vigilance, experience, knowledge of the trade and professionalism in evaluating and underwriting such exposures. Imagination is required in order to find ways and means to make a difficult risk more acceptable.

13. Due to constantly changing circumstances, continuous supervision, management and re-evaluation of all underwritten risks is vital in order to avoid unnecessary loss for the policyholder and the insurer.

14. Ethics also requires that the insurer keep proper records of the accumulation of the total of all exposures, consisting of credit limits underwritten for a number of policyholders on the same debtor. Only in this way can the insurer control and manage his exposure on a particular debtor and such detail is vital for the purchasing of appropriate re-insurance by the credit insurer.
15. Every insurer needs re-insurance facilities because his own financial strength is not sufficient to enable him to settle major claims that he may be called upon to pay. The policyholders rely on the insurer’s integrity, financial strength and re-insurance arrangements when they place their risks with him.

Ethics requires that the credit insurer considers carefully what steps he needs to take to avoid these problems from arising. Here are a number of suggestions:

- Credit limit underwriting is not done on an actuarial basis. Each individual risk requires separate investigation and assessment due to the type of risk involved. The underwriter has a certain authority to bind the insurer and with this authority goes the responsibility to act fairly - with due care - towards all parties. Credit limit underwriting is not an exact science and requires experience and a feel that develops over time. This is particularly so because the factual information available on the risk is often limited. The credit insurer therefore has a duty to the underwriter, the policyholder, and the buyer and to himself and his other stakeholders, to ensure that the underwriter is properly trained in the techniques of underwriting and that he is allowed time to build the experience needed to perform the job diligently.

- The underwriter must be factually neutral. In assessing a credit risk he cannot allow himself to be swayed by the policyholder, the buyer, rumours or emotions. The factual information available and cool, professional judgment is what must be the basis of the decision. It is the underwriter’s duty to extensively gather the facts about the risk without using this activity to unduly delay a decision. An ethical decision is an informed decision. A decision that is taken blindly or based on convenient ignorance is unforgivable. It is worth noting here that King II (50. King, 2002: 148) recommends that private companies should also disclose their financial situation in the service of transparency and good corporate governance.
• Consumers demand assurances that the goods they purchase are safe, are produced in conditions that do not deny workers their rights and that they are not damaging the environment in their production, consumption, or disposal. If the consumers’ demands in this respect are not satisfied, they may well boycott the product concerned, with obvious detrimental consequences for the supplier that may well rebound on to the credit insurer. Labeling of products has become a popular tool for manufacturers to communicate effectively to consumers the ethical standards their merchandise complies with. The credit insurer should take an interest in the way a risk it underwrites addresses environmental and social issues because they do affect the long-term quality of the risk. Not only can the risk be seriously hurt by a consumer boycott but governmental actions, such as fines or even forced closure can lead to a loss for both the policyholder and the insurer.

• A company that complies with a sound corporate governance policy (see chapter 2 “Corporate Governance”) will be a more acceptable risk for the credit insurer, and I believe that it is the credit insurer’s duty to set an example by following its own responsible corporate governance and ethics policies. Through such actions the credit insurer can help to improve the standard of business conduct and disclosure to the advantage of the national economy.

• In chapter 4 “Impact of Ethics on Business” I claim that central to any ethics is the relationship of the “ought” and the “can”. Any “ought” presupposes a “can”. Is it possible for a new business to act ethically or is it forced to concentrate on survival only and therefore cannot be expected to worry about acting in an ethical manner? Deon Rossouw in his book Business Ethics in Africa (42. Rossouw, 2002: 36) suggests that we could apply Piaget’s (20. Piaget, 1948) moral development theory to business as well, e.g.:
  o Survival morality – a pre-moral phase because it takes no cognizance of the interest of others.
o Reactive morality – a willingness to conform to the demands of society in order to gain social acceptance.
o Pro-active morality – the quest to do good through its activities, products and services.

According to this theory it is in order for a new business not to consider others if it is struggling for survival. I cannot see how this can be right. Any business, particularly a new one, is an agent dependent on others, e.g., customers, employees and creditors, and not to keep their needs in mind is likely to result in the demise of the business. If a new business does not care about its customers it will not satisfy their needs and eventually lose them; if it does not pay its creditors it will not treat them as ends in themselves and therefore it will, in the end, not be able to obtain the goods it needs to supply its customers; and if a new business does not care for its employees it will frustrate them and will not be able to trust them to help build the business. The majority of businesses that go insolvent are new ones. Their demise is usually due to poor planning of the new venture, undercapitalization and thus relying too heavily on bank and creditors’ money. As a result, the new business may find itself in financial trouble. This leads to delaying payments to creditors and using all sorts of shortcuts in an effort to make ends meet. Creditors do not appreciate being treated like this and they will curtail credit, making it even more difficult for the new business to survive. Customers are not serviced efficiently and become disenchanted with the new supplier. Staff feel insecure in their jobs and may not like what they see and hear. Thus, without proper planning and at least the minimum amount of capital the new business is doomed. It ought never to have been allowed to start because its failure will waste valuable resources and hurt others. I do not therefore believe in Deon Russouw’s “survival morality.” Even a new business must act ethically and should always comply with Kant’s doctrine never to treat others merely as means – this is a basic obligation. It is no doubt so that some of the other ethical duties spelled out on page 42 of this report are of a category that a new business “can” not comply with and therefore “ought” not to have to comply with, e.g., to help develop institutions or to support charitable organizations. For a credit insurer it is difficult
to know whether a new firm is acting morally because it is likely to be a minor risk in monetary terms that does not allow the credit insurer the time and expense to investigate the risk in great detail. But if the credit insurer becomes aware of serious unethical behaviour by the risk, he should not grant cover or withdraw existing cover, because an unethical business should not be supported for moral reasons and because it is clearly a higher risk for both the policyholder and the insurer.

• The opposite of a small, new business is the large, well established corporation that sees itself as so powerful that ethical behaviour either is considered an unnecessary and naïve effort or is only resorted to when it suits the organization (which is of course not ethical at all). This attitude has been dealt with in chapter 4 – “The Impact of Ethics on Business”. However, what is a supplier to such a business to do when he is treated in a clearly unethical manner by such a corporation (and it is usually the smaller, weaker supplier that is treated in this way because the important supplier will not accept such treatment and can usually force the purchaser into treating him with reasonable fairness)? This may well be a question of “can” and “ought.” Even the smaller supplier “ought” not to accept being treated in a manner that hurts his dignity – in the interest of self-respect and being true to his values. But on the other hand the small supplier “can” possibly ill afford not to do business with the large corporation, in which case his overlooking but not condoning the way he is treated should not be seen as unethical. Sometimes a large purchaser, who finds himself in a financially tight spot or wants to squeeze extra credit out of his suppliers, tries to deceive his suppliers through a totally disingenuous corporate structure that precludes an understanding of the financial standing/credit worthiness of the undertaking. Monies are shuffled from subsidiary to subsidiary and suppliers are told that the goods were sent to the wrong outlet; that they should invoice another group company; or they are advised that the cheque is “in the post”; or that some minor, obscure condition in the purchase contract has not been complied with and all this only in an effort to stretch supplier credit. This is a clearly unethical conduct. The credit insurer
cannot interfere in the relationship between the purchaser and the policyholder, but he should take note of tactics employed by the risk to delay payment and possibly downgrade the risk (which may have an effect on premiums charged for such a risk) even if it is financially in a sound position. Risks that employ murky, deceptive corporate structures should be viewed with great suspicion by the credit insurer.

- Contrary to popular assumptions, the poor can be a very profitable market, e.g., the micro lending industry. It takes considerable imagination, creativity and determination to develop a market infrastructure and suitable products for unsophisticated, poor people. Pricing and affordability are crucial issues. Because the amounts in which the poor deal are very small, transaction costs for financial services are usually disproportionately high. But South Africa’s four leading banks have succeeded in designing a product for the market of about 13.5 million poor, as yet un-banked people with the creation of the MZANSI account. With a MZANSI card a person can use any of the four big banks in the country at costs considerably lower than applicable to the banks conventional customers. Although this is a joint development, the four banks compete freely as far as the charges for the various banking services available to a MZANSI card holder are concerned. The “managed policy” as referred to on page 113 is a way to bring credit insurance to the small business.

Credit is a powerful means to free the poor from the cycle of poverty. It can be the kick-start for a new business. Credit oils the wheels of the economy. What must a credit insurer do to address the credit needs of the poor?

I believe that one must consider the following facts:

- The credit that can be underwritten by credit insurers is business-to-business credit.
- Business has the moral duty to survive, to earn profits and to create long-term wealth (as discussed in more detail in chapter 4 “The Impact of Ethics on
Business’). Its duty is not to act entirely selfless, in a manner that militates against its long-term wealth creation obligation. Business people can be expected to know this principle and respect it.

- Credit relies on trust (see chapter 7 “Trust”) and trust needs to be earned. A new business has to prove that it deserves credit if it cannot offer security. It has to begin by paying cash and so build a reputation. This may mean that it has to start on a very small scale. A record of cash purchases will be a basis for being granted small amounts of credit which will grow on the back of a good credit paying record.

- In addition to good training and the accumulation of experience, the corporate culture of the credit insurer needs to strongly promote trustworthiness, loyalty and commitment in its employees. This requires recognition of good work done, and giving authority to qualified underwriters together with matching responsibility. The staff needs to be motivated and proud of its employer. All this requires a motivating and enlightened human resources policy. Such a policy supports respect for the dignity and autonomy of the individual (treating employees not merely as means but as ends-in-themselves) and equitable remuneration that backs ethical behaviour. It also provides challenging and satisfying jobs with personal development and growth opportunities, and it requires an open and congenial working atmosphere.

- Quality in the work performed by underwriters is paramount. This needs to be accepted and fully supported by staff. The underwriter must be aware of the policyholder’s requirements. He, the underwriter, must have a good understanding of the policyholder’s business, particularly in relation to questions of credit. All credit limit applications by the policyholder must be dealt with promptly and in an expert manner.

- In addition to being professionals in underwriting credit risks, underwriters need to have good people’s skills so that they can deal sympathetically but firmly with
policyholders, debtors, information sources and other people they come into contact with.

- The insurer has to be constantly vigilant in order to detect fraudulent behaviour. An independent credit committee, which has to vet and track large risks, as well as good internal audit, can assist here. A strong corporate culture of openness, trustworthiness, participatory management and a well entrenched ethics policy will help in avoiding underwriting staff becoming involved in unsavory actions. Careful recruitment, good staff communications and enlightened human resource policies are also important tools to fight dangers of deception and double-dealing.

- Underwriters need to know when and how they can make information available to a policyholder in order to help the policyholder to understand certain decisions by the underwriter. As the policyholder could, due to an underwriter’s decision, lose large, lucrative transactions, it is understandable that the policyholder may feel justified in demanding reasons from the underwriter for the decision. On the other hand, the underwriter often makes his decision on the strength of information given in confidence. Revealing such information means breaching confidentiality and could lead to losing a valuable information source. Making such confidential information available to third parties may also harm the debtor, and the credit insurer could be sued for defamation.

- The credit insurer needs to have checks and balances in place to ensure that underwriters do not exceed their mandates. Building suitable blocks into the underwriting computer system can easily do this. It is obviously important that mandates are given in line with knowledge, experience and trustworthiness.

- The credit insurer must be careful with blacklisting certain classes of buyers. Well thought through, objective criteria that are ethical and fair need to be the basis for such action. Using race, gender, domicile or religion as a basis for blacklisting would be totally unacceptable. The same applies to a register of delinquent
directors or other business people. Such information can be an important underwriting tool.

- Under certain conditions the credit insurer could auction off available credit cover, but this would raise serious administrative difficulties where continuous, ongoing business is concerned as opposed to a once off contract.

- Clearly, the underwriter has to be prepared to listen to all parties involved, e.g., the policyholder, the buyer and all available sources of information. All information so collected requires critical evaluation before a decision is made.

- Underwriters need to be persons of integrity and the credit insurer has a duty to carefully select the people he places in these difficult and responsible positions.

- The credit insurer needs a first class risk administration and management system. Proper recording, controlling, evaluation and periodic re-assessment of the risks is necessary in order for the insurer to meet his business and ethical obligations to all his stakeholders.

- Spread provides the insurer with the basis of his risk absorption capacity. Thus the credit insurer has to strive for the best possible spread in numbers, sizes, industries and locations of his risks. Through the diversified portfolio of his risks, the credit insurer is able to accept the risks from his policyholders at premiums that are attractive to both parties. A credit insurer who sells both domestic and export credit cover is clearly better placed than one who provides only domestic or only export cover. The demand for credit insurance fluctuates vastly between different industries and this hampers the credit insurer’s aim for a perfect spread. Credit and country risks of a superior grade are less likely to be offered to the credit insurer, even though the terms for insuring such risks will be far more attractive than for poor grade risks. The insurer must therefore strive to structure his products in such a fashion that they induce the policyholder also to offer his
first class risks for cover. Careful risk portfolio management is an aid to balancing the credit risks to which the insurer is exposed. A well balanced and diversified portfolio is basic to survival and long term profitability of the credit insurer. Ignoring this important issue puts the future of the insurer in danger and is therefore unethical towards his shareholder and clients – an insolvent insurer cannot keep his promise as embedded in the credit insurance policy.


The insurer’s moral obligations towards his clients or prospective policyholders in country underwriting are similar to those described above.

The underwriter needs to be thorough and diligent in collecting the relevant information concerning the political and economic situation as well as historic and likely future developments of the country under consideration. The political and economic relations between the exporting and importing countries need to be kept in mind as well as any special circumstances such as legal, financial, licensing etc. regulations that may affect exports and the flow of payments in foreign exchange.

The information so gathered requires intelligent analysis and presentation in a country report that concisely and completely highlights the important issues. The report should also draw conclusions and make recommendations so that a decision by the country underwriting committee can be taken.

The country underwriting committee’s decisions will include political and economic risks grading. These gradings will dictate the terms and conditions on which risks on a particular country can be underwritten as well as the premium rate that will be levied on insured exports to that country.

International agreements, such as sanctions, restrictions or understandings agreed to within the Berne Union (the international association of export credit insurers) need to be complied with.
Country underwriting is clearly a complex job that requires specialist knowledge and skills. Large credit insurers would have people with economics degrees attending to this work. Smaller companies may make use of the services available from such institutions as the World Bank, the *Economist*, their own government etc.

Because the accumulation of many risks resulting from the exports by many of the credit insurer’s policyholders to the same country can result in very large exposures on any one country, careful, conscientious underwriting is crucial in order to avoid mammoth claims.

Meticulous work in this field is an ethical obligation toward the exporting community, the importing county, the credit insurer himself and his reinsurers.