CHARTERED INSTITUTE OF LOSS ADJUSTERS

DIPLOMA READING & LEARNING GUIDE FOR CUSTOMER SERVICE AND ETHICS — DP3

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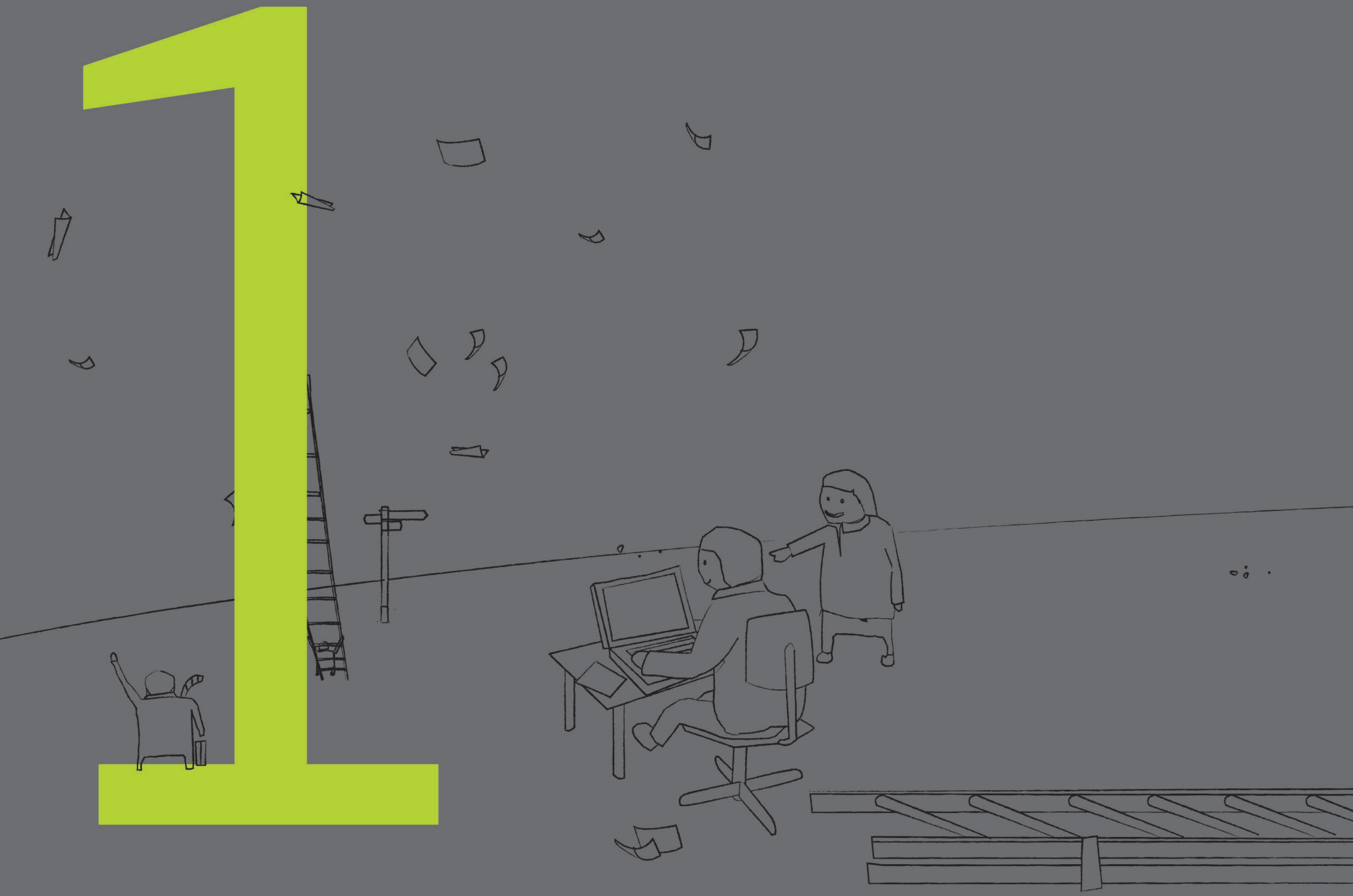

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INTRODUCTION TO CUSTOMER SERVICE

1. INTRODUCTION TO CUSTOMER SERVICE

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Introduction

Customer service is not a new idea; it has existed for centuries, for as long as people have been selling their products and services. It is now ingrained in our society with the popular adage ‘the customer is always right’, placing the customer at the heart of an organisation and recognising their importance. However, the way in which an organisation delivers customer service, and the expectations customers have of what service they should receive, has changed over time.

The purpose of this section is to provide a clear understanding of what customer service is, when it takes place, the different ways in which it can be delivered and who is responsible for delivering customer service.

1.1 Customer Service Defined

The Oxford Dictionary defines customer service in terms of the assistance and advice provided by a company to those people who buy or use its products or services. Zeithaml and Bitner, academic researchers in the field of customer service, define it as *“the service provided in support of a company’s core products”*. In its broadest sense, customer service is anything that we do for the customer that enhances his or her experience. It is any interactions that we have with a customer that form part of the service we provide.

These interactions are also known as ‘touch points’. Touch points are the moments when the customer comes into contact with the company, for example when they report an insurance claim or meet a loss adjuster. Each touch point is an opportunity to provide good customer service, for the customer to assess that service and for a relationship to be built between the company and the customer.

Activity

Think of two different customer service experiences that you have had recently. By ‘different’ we mean in terms of the types of product or service you were buying or using (e.g. a low cost item such as food at a supermarket, checking your bank balance or researching the purchase of an expensive item).

What were the touch points for each? What assistance or advice did you receive from the company? In what ways did the level of service differ?

1.2 When does Customer Service Take Place?

Customer service takes place before, during and after the purchase of a product or service. Marketers refer to these stages as the pre-purchase, purchase and post-purchase stages.

In an insurance context, customer service occurs:

- At the pre-purchase stage – helping the prospective customer to find the right insurance policy for their needs;
- at the purchase stage – helping the customer to buy and arrange payment for their insurance cover; and
- in the post-purchase stage – processing changes to the policy and, most importantly in our context, helping with an insurance claim.

As we shall see in Section 2, the delivery of good customer service is just as important in claims handling as the purchase of the original insurance policy. Indeed, many within the insurance industry consider the claims process to be the 'acid test' of insurance. This is when the customer uses, or consumes, the service they have purchased and the point at which they can fully evaluate it. In other words, this is the make or break point of insurance. Research has shown that claims that are well handled not only lead to a satisfied customer, but also to one who is likely to stay with that insurer. On the reverse, a badly handled claim is more likely to result in dissatisfaction and the customer taking their business elsewhere at renewal.

Activity

The claims handling process can also be divided into the same three stages: pre-purchase, purchase and post-purchase. Write down all three and give an example of how customer service takes place in each stage.

1.3 Forms of Customer Service

For customer service to take place, there needs to be an interaction between the customer and the company. The different forms of customer service can be classified by:

- The method of delivering customer service, e.g. face to face, telephone, letter, email or through mobile technology.
- The level of customer service. This is typically classified as high touch or low touch. High touch is where time is devoted to providing quality customer service; low touch is where very little or indeed no service is provided to the customer.
- The transparency of customer service, i.e. whether or not the customer can see the 'workings' of the customer service process. Customer service can be transparent – where everything is seen; or opaque – where customer service is not seen. A good example of a transparent customer service is Subway where the customer can see their sandwich being made, step by step.
- Good or poor customer service – an obvious but important addition to the list.

For most companies, the form of customer service they provide is not high or low, transparent or opaque. The service provided sits somewhere in between, for example on a scale with high touch at one end and low touch at the other. Companies need to decide what is the best mix for them to meet the needs of their market and where possible to differentiate them within their market.

These forms of customer service are also not fixed. Companies can move position within the different forms. This may be a deliberate move by the company to change consumer perceptions of the service they provide. Alternatively, the change may be as a result of external factors that cause consumers to view customer service differently. External factors can include changes in customer expectations, changes in competitor service or legislation.

Activity

How would you classify your company on each of the four forms of customer service?

1.4 Who is Responsible for Customer Service?

In the past, many companies had a customer service department that was responsible for customer service; some still do. However, customer service is not solely the responsibility of one department. It is the responsibility of everyone within a company, everyone who comes into contact either directly or indirectly with the customer.

Customers do not form an opinion of the quality of customer service based on their interaction with one person. It is a combined view based on their contact with everyone, and indeed everything, i.e. the touch points. Some aspects will be more important, for example the first impression based on the first touch point. Other interactions will be more influential depending on context, for example during times of stress or anxiety. The claims management service falls into this category.

1.5 Key Points to Remember

- Customer service is anything that we do for the customer that enhances his or her experience.
- Customer service is the responsibility of everyone.
- Touch points occur when the customer comes into contact with the company and it is at these points that their impressions of customer service will be formed.
- Customer service can be considered in four ways: method of delivery, level of customer service contact, the degree of transparency and the quality of that service.
- Customer service is not static, but changes over time either due to changes made by the company or changes that occur within the market and the environment in which the company operates.

2 WHY CUSTOMER SERVICE IS IMPORTANT

2. WHY CUSTOMER SERVICE IS IMPORTANT

Introduction

In Section 1, we defined customer service, but why is customer service important? In this section, we will outline the benefits that flow from good customer service and the problems a firm can experience when it provides poor service. However, before we look at these areas, we need to consider the legal and regulatory requirements imposed on firms to provide good customer service. This section therefore starts with a review of two obligations placed on insurance and loss adjusting firms. The first is imposed by the Consumer Rights Act 2015; this applies to all firms but has specific requirements for firms providing services. In addition, firms in the claims management sector need also comply with the Treating Customers Fairly (TCF) regulations imposed on financial services companies by the Financial Conduct Authority.

This section is structured as follows:

Contents

2.1 Consumer Rights Act 2015

The Consumer Rights Act 2015 became law on the 1st October 2015. Its aim was to simplify, strengthen and update existing law. It replaced three key pieces of legislation: the Sale of Goods Act, the Unfair Terms in Consumer Contracts Regulations and the Supply of Goods and Services Act.

As the Act includes the supply of a service, it applies to services such as those provided by loss adjusters. The Act states the following:

- Services must be performed with reasonable care and skill
- Information provided to the consumer by the organisation (written or spoken) is binding where the consumer relies on that information
- Where the price is not agreed beforehand, the service must be provided at a reasonable price
- Where a particular timescale is not set out or agreed for performing the service, it must be carried out in a reasonable time.

Customer service therefore features quite prominently in this Act in terms of the information provided about the service, the price, the timeliness of the delivery of the service and the way in which the service is performed.

If the service provided does not satisfy the above, the customer is entitled to the following:

- The service, or part of the service, that is inadequate has to be repeated at no extra cost to the customer, within a reasonable time and without causing significant inconvenience to the customer

- Or, where it is not possible to repeat the service or it cannot be done within a reasonable time and without causing inconvenience, the customer can claim a reduction in the price charged.

2.2 Treating Customers Fairly

The Financial Conduct Authority (FCA) is the regulatory body for the financial services sector. One of their goals is to ensure that customers are protected and get a fair deal. The actions that firms need to undertake are encompassed in the six outcomes below on how to Treat Customers Fairly (TCF):

- **Outcome 1:** Consumers can be confident they are dealing with firms where the fair treatment of customers is central to the corporate culture.
- **Outcome 2:** Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.
- **Outcome 3:** Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale.
- **Outcome 4:** Where consumers receive advice, the advice is suitable and takes account of their circumstances.
- **Outcome 5:** Consumers are provided with products that perform as firms have led them to expect, and the associated service is of an acceptable standard and as they have been led to expect.
- **Outcome 6:** Consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.

Source: www.the-fca.org.uk

Customer service is very much at the heart of this list. Firms are responsible for making sure that their customers are treated fairly and this responsibility also applies to every single employee working for or on behalf of that firm, including loss adjusters and claim handlers. It is important however to remember that the FCA regulations apply to retail customers and not those acting in a business capacity. However, it is becoming increasingly the case that insurers wish to demonstrate that they are treating all customers fairly, whether retail or business customers.

Activity

Identify the ways in which the TCF outcomes differ from the requirements of the Consumer Rights Act 2015.

2.3 The benefits of good customer service

Good customer service is vital to an organisation's success and long-term survival. Customers are important to a firm as they provide the income the firm needs to enable it to operate and make a profit or surplus. Customer service is the way in which a firm interacts with those customers.

Good customer service contributes to a firm's success and profitability in the following ways:

Customer loyalty

Customer loyalty occurs when customers choose to repeatedly use a particular company for a product or service over an extended period of time rather than buying from a competitor. For example, a policyholder who buys his/her travel insurance from the same insurer for several or more years can be considered to be a loyal customer. Customer loyalty is not however automatic. In insurance, a policyholder will commonly review their insurance each year when they receive their renewal and may or may not decide to renew with the same insurance company.

A customer who has received good customer service is more likely to stay with that company rather than feel the need to look around for a better price and will therefore become a loyal customer.

In addition, satisfied customers are less price sensitive. This means that a lower price from a competitor is less attractive to them compared to a customer who is dissatisfied with the service they have received. Of course, even satisfied customer can leave, but a loyal customer who has received good customer service is less likely to be tempted away by a lower price and untested promises made by a competitor.

Customer loyalty is beneficial to a company as it is expensive to find and secure new customers. For example, attracting new customers via a website requires (expensive) advertising. Complex business insurance products also require an underwriter to spend time reviewing the insurance requirements and providing an individual quote. This all costs the company money.

Finally, loyal customers are also good for companies as they are more likely to buy additional products and services from that company should they need them. For example, a loyal customer who is happy with the service provided by their insurer may place their motor and home insurance with the same company. This not only results in efficiencies for the company, but also increases customer loyalty even further as their relationship with that company grows and the effort required to move their multiple products/services results in inertia, i.e. unwillingness to take action.

Positive word of mouth

Customers who experience good customer service are more likely to talk positively to family and friends about their experience. This is called positive word of mouth (or WOM for short). WOM need not be face to face, but can also be electronic (eWOM).

WOM is similar to a conversation in that there is a sender (the person who is talking about their purchase and experience with the company) and the receiver (the person who is listening to what is being said)

WOM has a positive effect on the views and opinions that the receiver has on the product or company being discussed. In addition, recent studies have found that WOM also has a positive effect on the sender as they talk about their own experiences and feel that they are helping others by providing that information. In both cases, the sender and receiver will be more positive about the product or firm being discussed.

Positive WOM is valuable to companies as it is much more influential than other forms of marketing promotion. For example, studies that have compared positive WOM to advertising found that consumers were much more likely to believe WOM from a friend or family member compared to an advertisement. This is because family and friends are seen to be independent (i.e. not working or having a commercial interest for the company selling the product) and are therefore more trustworthy.

Activity

Write down three recent purchases that you have made where one was inexpensive, the second expensive and the third very expensive. Thinking back to the time before your purchase, when you were choosing what to buy, can you identify the role that friends and family played in your purchases? What information did you seek or receive and how did this information influence your final purchase decision?

Reputation

A company that provides good customer service will over time develop a reputation within the market for its customer service. This reputation may be developed due to positive customer WOM, industry knowledge, media coverage or industry awards. A positive reputation is a strong asset for a company.

A positive reputation for customer service can produce a halo effect. As the company is known to have a positive reputation for customer service, it will be assumed that it is good at doing other things too. For example, a company known for employee satisfaction will attract new employees to the firm.

A reputation for good customer service can also act as a ‘reservoir of goodwill’. This reservoir provides the firm with a buffer that can help to protect it in times of crisis. For example, when a firm with a good reputation for customer service experiences a corporate crisis, such as a very badly handled claim that appears in the media, customers will assume that this is an exception rather than the norm for this company and are likely to be generous in their views of this company. The reverse would of course be true for a company that has a poor reputation for customer service.

Sustainable competitive advantage

A competitive advantage exists when a firm consistently outperforms other firms in the same industry sector. There are different ways in which performance can be measured, although most often it is measured in terms of the profits the firm produces. Firms that are able to repeatedly outperform their competitors have a sustainable competitive advantage.

Good customer service can provide this competitive advantage. We have already noted that good customer service contributes to a firm’s profitability. Good customer service is also difficult for competitors to copy quickly as it requires a change in the culture of an organisation; it takes time for a company to build and establish a reputation. Good customer service is therefore a source of sustainable competitive advantage.

2.4 The Problems of Poor Customer Service

Many of the problems of poor customer service are the direct opposite to the benefits.

Customer switching

Customers who receive poor customer service are more likely to leave the company and go to a competitor. This is called customer switching. Switching is high where customers have a choice of other companies to choose from and the move is easy. Switching can also occur when contracts, for example loss adjusting panels, are up for renewal and the customer in this case is the insurer. Extreme examples of poor service can result in the customer switching mid-contract.

Negative word of mouth

We discussed earlier how influential positive WOM is to firms. Negative WOM is, however, much more influential than positive WOM. There are three reasons for this:

- The senders of negative WOM tell more people than those communicating positive WOM. It has been estimated that, on average, customers who receive poor customer service go on to tell 16 people, whereas those who receive good customer service tell just 9 people. Bad news does indeed travel more quickly!
- Negative WOM is much more influential as the recipients are more likely to remember it when compared to positive WOM. Negative WOM can prevent potential customers from becoming customers.
- Negative WOM is much more influential as the recipients are more likely to act on the information. In the case of poor customer service, this means that customers are more likely to avoid organisations that receive negative WOM than to use companies that receive positive WOM.

With the growth of social media, the impact of WOM has increased dramatically. The consequences of negative feedback posted on websites are greater in scale, highly visible and more immediate than offline WOM of the past.

Reputation and trust

Trust is important in the insurance relationship between a customer/insurer and a customer/loss adjuster. In the former, the customer needs to trust that the insurer will pay a valid claim should they suffer a loss in the future. In the latter, a customer needs to trust that a loss adjuster will assess their claim in a fair and equitable manner. A strong reputation for customer service helps to build this trust.

Where there is an absence of consumer trust, the consequences can be far reaching. In a recent study by the management consultancy service Accenture in the United States, 55% of customers were found to be more likely to commit insurance fraud due to a company's poor customer service. Poor customer service can therefore have a direct impact on company profitability.

Impact on employees

The impact of handling frequent customer complaints and working for a company with a poor reputation will have a negative impact on staff. Companies with poor customer service are more likely to have dissatisfied or demotivated staff. Staff turnover will increase as employees prefer to work for and be associated with companies with a positive reputation. In addition, the firm's ability to attract and retain new quality staff will reduce.

Financial performance

We have already touched upon the impact that customer service can have either directly or indirectly on the financial performance of the firm. However, it is worth restating these as companies often have to consider a choice between investing in customer service against other company needs. To summarise, customer service impacts financial performance in terms of lost business, the difficulty and associated high costs of attracting new customers, additional resources required to handle and resolve complaints, the increase and impact in fraudulent claims, and the associated costs of demotivated staff and staff turnover.

Activity

Find out how your company records and monitors customer complaints.

What has been the most frequent type of complaint over the past six months? What action is the company taking to put this right?

2.5 Key Points to Remember

- Some aspects of good customer service are not optional but are required by law under the Consumer Rights Act 2015 and the Treating Customers Fairly (TCF) regulations.
- The TCF regulations apply to retail customers and not to those acting in a business capacity. However, firms should demonstrate that they are treating all customers fairly, whether they are retail or business customers.
- Good customer service provides a company with a sustainable competitive advantage through customer loyalty, positive WOM and a good reputation.
- Poor customer service will damage a firm financially as a result of customer switching, negative WOM, damage to reputation and customer trust, and the negative impact on employees.

3

WHO IS THE CUSTOMER?

3. WHO IS THE CUSTOMER?

Introduction

Although we always talk of ‘customers’, they are not one large homogeneous group. The aim of this section is to identify the main types of customers and to consider how their needs, in terms of customer service, might differ.

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3.1 Internal and External Customers

Customers can be divided into two broad groups: internal and external, depending on their relationship with the firm. External customers are individuals or organisations who buy a product or service that the firm produces. An internal customer is someone who works within the firm and relies on others within that firm for goods or services. For example, a claims manager may rely on the services of an underwriter to help them to assess a claim. Business development managers may rely on the services of their accounts department to assist with payment plans. Many employees rely on their IT department to help with queries and to provide them with support in connection with their computer or laptop. Customer service is important to both internal and external customers.

Loss adjusters can have internal and external customers and can themselves be a customer.

Activity

Thinking about your own role, can you identify one internal and one external customer that you have? How do their expectations, in terms of the customer service you provide, differ?

3.2 Policyholders

Within the claims management profession, policyholders are the largest single group of external customers. Policyholders are the customers of insurance companies and can also be the customers of loss adjusters where the loss adjuster is employed by the policyholder directly.

Policyholders can be private individuals or businesses/organisations. These relationships are known as Business-to-Consumer (B2C) where the consumer is an individual policyholder, or Business-to-Business (B2B) where the business is a firm, company or other type of organisation. The needs of these two groups with respect to customer service can differ markedly.

Private individuals

Private individuals can be segmented according to their characteristics. Customer characteristics can influence customer expectations of customer service and their perceptions of the service they have received. Customers can be segmented in the following ways:

- Demographics: demographic factors include age, gender, education, income, occupation and cultural background. These factors enable companies to segment their markets and identify particular groups that share behaviours, for example Baby Boomers (born between 1946 and 1964) or the Millennials (born between 1980 and 2000). Due to changes in society norms over time, these groups will have different expectations and perceptions of customer service.
- Motivational factors: these factors explain why a consumer buys a product. A good example is car insurance. This is a legal requirement and for some customers is the only reason they purchase insurance. Others buy insurance because they want the protection an insurance policy provides. Attitudes to insurance and the service expected will differ between the two groups.
- Usage: consumers are traditionally placed into broad categories based on the frequency with which they purchase a product. Heavy users buy frequently and light users hardly at all. Insurance is typically an annually renewable policy, but the concept of usage can be applied to the claims experience. Consumers who are heavy users and have experienced more than one claim will have gained knowledge about the claims process, perhaps from different companies, and will have different expectations to those who have not made a claim.
- Vulnerable consumers: The Financial Conduct Authority (FCA) identified a range of consumer groups that may be vulnerable in a financial services context. The groups are detailed in the FCA's Occasional Paper Series No. 8 published in 2015. Some of the key groups they mention are the very young, the very old, people with mental illnesses and those with low numeracy and literacy skills. It is always dangerous to group consumers using such broad categories as not all people falling into these groups are vulnerable. However, there is a need for all service providers to be aware that some consumers may be vulnerable and will require additional levels of care.

Activity

How would you segment your customers? Which segment would you consider to be the most important and what specific needs does this segment have with respect to customer service?

Business

As with individual consumers, businesses can also be sub-divided into smaller segments:

- Size: this is perhaps the most important and frequently used basis on which to segment business customers. Sole proprietorships, microbusinesses (with no more than two employees) and small businesses often behave in a similar way to private individuals in terms of their decision making and expectations. Large firms are more likely to have insurance and/or risk managers who are knowledgeable about insurance and expect their claims to be managed in a professional and businesslike manner.

  Care must be exercised when using the term small business as small has different definitions in terms of the size of a firm. For example, the Department for Business, Innovation & Skills defines SMEs (small to medium-sized enterprises) as companies with less than 250 employees. Companies House defines a small business as employing less than 50 people and a medium business as having less than 250 employees.

- Industry type: companies can be classified according to the industry in which they are based. The Standard Industrial Classification (SIC) is a four-digit code, originally developed in the United States in the 1930s and later adopted by the UK. This provides a broad basis for grouping firms into industries. Different industries develop their own norms of behaviour in terms of concepts of timeliness, ethics, professionalism and expectations of customer service.

Groups

Groups are most frequently recognised in a B2B context as a firm typically has many people who are involved in a decision to purchase an item. Decisions within firms are made through hierarchical reporting lines. However, group decisions also occur in a B2C context as people do not always make decisions on their own but as part of a couple, a family unit or as friends.

In its simplest form, a group will have an initiator who identifies the need to buy, an influencer who specifies requirements and assesses information about the product to buy, a purchaser who makes the purchase, and a user who actually uses the product purchased. Each will vary in terms of the knowledge they have, the level of contact with the company and the customer service they received, their expectations, and the influence these factors have on their decision to buy. It is important to understand these different roles so that the different customer service requirements are clearly identified and delivered to the right person.

3.3 Employees of the Firm

Internal customers are easy to overlook as customers as they do not buy the firm's product or services. They are however important to the success of a company. Poor internal customer service ultimately results in poor service to external customers. All employees need to work together as a team.

The management consultant Karl Albrecht has written widely on the importance of the internal customer. He proposed a step-by-step internal customer service audit as follows:

1) Identify and prioritise your internal customers
2) Identify their need(s)
3) Identify which needs are most critical
4) Verify 3) and 4) with your customer(s) and amend if necessary
5) Conduct research (e.g. interview or survey) to measure your performance on the critical needs of your priority customers.

Activity

Undertake the internal customer audit for your department or team and identify your priority customers and their needs.

When undertaking an internal audit, it is important to keep in mind why the audit is necessary. A company that focuses exclusively on its external customers is failing to see the bigger picture and risks overlooking the link between internal and external customers. It is important to ask the question: how does this internal customer's service contribute to the customer service delivered to external customers?

3.4 Other Stakeholders as Customers

A stakeholder is anyone, any group or any organisation that has an interest or concern in a company. The number of entities that can be considered to be a stakeholder is therefore large. Typical examples include government, professional bodies, shareholders, suppliers, unions and the community in which the company operates.

Not all stakeholders are equal in terms of their importance to the firm and this importance can change over time and by situation. In addition, a stakeholder can be a customer, a supplier or have another form of relationship with the firm. If we think about this in the context of a claim, we can identify a range of other stakeholders, for example the fire service, the manufacturer of a faulty part, a forensic expert, etc. This list can be large or small depending on the complexity and size of the claim. One important thing to note here is that stakeholders do not always occupy the same position and may move from supplier to customer depending on the nature of the claim you are handling.

3.5 Key Points to Remember

- Customers can broadly be divided into internal and external customers.
- Loss adjusters can have external and internal customers and can themselves be a customer.
- External customers are not one homogeneous group but fall into different groups with different customer service needs.
- External customers can be grouped as Business-to-Consumer (B2C) or Business-to-Business (B2B).
- Internal customers are important because poor internal customer service ultimately results in poor service to external customers.
- Firms have a range of other stakeholders who may also be customers.

4

SERVICE QUALITY

4. SERVICE QUALITY

Introduction

In the preceding sections, we defined customer service as the assistance and advice provided by a company to those who buy or use its products or services. This is a simple, straightforward view of customer service but is quite narrow. Other factors can also have an impact on customer service and customer satisfaction. We need to take account of these additional factors if we are to identify exactly why customers are satisfied with the service provided or what the company can do to improve its customer service.

In this section, we will break down the idea of customer service into more detail by looking at service quality. Service quality takes into account a much wider view of what makes customers satisfied within professions such as insurance and loss adjusting. Service quality also provides an instrument that can be used to measure service quality. This enables service quality to be assessed and compared more easily, for example to see how a firm performs year on year.

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4.1 Measuring Service Quality

If we wanted to ascertain how good an organisation is at delivering customer service, we could simply ask customers ‘Have you received good customer service from X company?’ with a choice of answers ‘yes’ or ‘no’. Or we could ask ‘What do you think of our customer service?’ with a range of answers on a scale from ‘very good’ to ‘very poor’. This would provide a good overall measure. However, the answers to these questions would not tell us why the service was good so we could keep doing the right things or, if the service was poor, what the problem was or how to fix it.

There is therefore a need to break down customer service into smaller parts. We can then ask questions and measure each of the smaller parts to identify what the company is doing well and identify the precise areas to improve. Researchers have spent a lot of time working on this and have identified a range of different service quality models. In this section, we will examine the most popular model: SERVQUAL.

4.2 SERVQUAL

SERVQUAL is an abbreviation of the words ‘service quality’. This model was designed by the researchers Zeithaml, Parasuraman and Berry in the United States in the 1970s. Although it is more than 40 years old, the model is still used widely today.

The most common form of SERVQUAL has the following five parts, which together make up the word RATER:

R Reliability

A Assurance

T Tangibles

E Empathy

R Responsiveness.

Even if we are not going to use this model to measure service quality, it is useful to be aware of the different items SERVQUAL contains as it provides us with a much wider understanding of what contributes to customer service and customer satisfaction.

Reliability

Reliability is about consistency, i.e. about doing things right the first time. It is about delivering on promises made to the customer. Examples include meeting deadlines, such as phoning the customer back within 24 hours after promising to do so, and maintaining full and accurate records of a claim and the customer's details (their name, address, etc.).

Activity

When handling a customer's claim, what in your opinion is the most important thing to get right first time and why?

Assurance

Assurance exists when customers have confidence in the firm to provide the service that they expect. Assurance is provided when employees are knowledgeable about their job and have the necessary information to enable them to respond to their customers' questions. For example, a customer will have confidence when their questions about basic insurance terms included in their policy are answered by their claims handler in a concise and easy to understand manner.

Activity

Thinking back over your career, what claims-related question have you been asked by a customer that you did not know the answer to?

If you were asked that same question today, would you know the answer? Can you explain that answer in words that most customers will readily understand?

Tangibles

Tangibles are the physical items that can be seen and touched. In addition to the professional appearance of staff, tangibles can also include company facilities when seen by the consumer (e.g. the office where you work – is it clean, tidy and ordered?), any tools or equipment used as part of your job (e.g. laptops) and the paperwork that you issue (e.g. letters, contracts etc. – are these easy to read and understand?)

The appearance of tangibles communicates a lot of information to customers about your organisation and about you. It can also influence whether the customer feels positive or negative towards you and your firm as it creates an impression about the service you are likely to provide.

Activity

What tangible items do your customers see when they make a claim? List all the items you can think of and then consider what the appearance of these items communicates to your customers.

Think about the colours used and the physical appearance: is it modern or traditional, professional or unprofessional in appearance? Are they pristine and well maintained or are they older and showing signs of wear? What conclusions would you draw about these tangibles if you were the customer?

Empathy

Empathy is having the customers' best interests at the heart of the company. It is the process through which we attempt to step into the shoes of someone else to understand a situation from his or her point of view. In a service context, it relates to how well the company understands the customer and their needs and how it responds, treating each customer as an individual. Examples of empathy would include staff that listen to their customers' problems and try to provide solutions.

Activity

Imagine you are handling a claim under a household policy which requires the policyholder and her family to be placed into alternative accommodation for a short time. How would you handle this claim? Would you handle the claim differently if one of the children has Asperger syndrome and finds it difficult to cope with change?

Responsiveness

Responsiveness is about timeliness and willingness to help. Examples include the time it takes to answer the telephone or to confirm details in a letter or email. Is your company quick to respond to customers and willing to help them where they can?

Activity

Many firms have service level agreements (SLAs) to ensure that all employees provide a standardised level of service. What SLAs does your firm have for answering telephone calls and responding to emails?

4.3 Gaps in Customer Service

SERVQUAL is often called the 'gap' model. This is based on how it is used in practice. SERVQUAL identifies a gap between the service quality the customer expects to receive and the service quality they think they have received. To identify this gap, we use the RATER items.

SERVQUAL is usually implemented using a survey. Each of the five RATER items are further divided into about three to five questions and the customer is asked to rate the service provided. An example of the type of question and the way in which that question is presented to the customer is provided below for the RATER item Reliability:

	Strongly Agree 1	Agree 2	Neither agree nor disagree 3	Disagree 4	Strongly disagree 5
When my insurer promises to do something by a certain time, they do so					

This question is asked three times:

1) What level of service does the customer expect to receive (known as expectations)?
2) What level of service did the customer receive (known as perceptions)?
3) How important is this service to the customer? (known as importance, see 4.5 below).

A score is produced by taking the customer expectations score (from Question 1) and subtracting the score for customer perceptions (Question 2).

Customers usually give a different score for expectations and perceptions as our expectations are typically high, so there is often a gap. A comparison of the scores for expectations and perceptions reveals how satisfied customers are with the service provided to them:

Where perceptions are equal to expectations = satisfied customer

Where perceptions exceed expectations = delighted customer

Where expectations exceed perceptions = dissatisfied customer.

Firms can look at the individual scores for each question to see where they performed well and where they need to take action to improve their scores. They can also combine the scores to produce a total for each of the five RATER items, or they can combine the RATER scores to produce one figure for overall service quality.

4.4 How Important is the Gap?

In 4.3, we noted that a SERVQUAL survey has three questions. The third question asked about importance. This question is required as not all of the RATER areas are viewed as equal in importance by customers. For most service companies, reliability is the most important and tangibles the least, but the order of importance will vary from industry to industry and firm to firm. The order of importance can also vary by departments within an organisation.

When analysing the gaps, we also need to know which aspects of service are important to the customer before an organisation invests time and money trying to improve its score. For example, a poor score in an unimportant area may not require any action to be taken to correct it, whereas a poor score in an area that the customer considers very important will require possibly immediate corrective action.

4.5 Benchmarking

One measurement of service quality on its own will tell a company how its customers view the quality of the service it provides, but the information will have greater meaning if it can be compared to other scores. These other scores are benchmarks. The most common are:

- Over time – SERVQUAL scores can be compared month by month or year on year to see whether the firm is improving. This is particularly important where the firm makes changes as the impact can be monitored to see whether the changes have had the desired effect.

- Different organisational units – most firms have different departments, locations and business units. Firms can compare their SERVQUAL results across the different parts of the firm. Such comparisons can have a positive effect by creating internal competition and thereby raising service quality standards.
- Competition – ideally companies would compare their SERVQUAL results with those of their competitors. This data can be difficult but not impossible to obtain. Firms can, for example, commission research agencies to conduct this research on their behalf.

4.6 Key Points to Remember

- SERVQUAL has five RATER items: Reliability, Assurance, Tangibles, Empathy and Responsiveness.
- SERVQUAL measures the gap between customer expectations and perceptions.
- An organisation needs to know how important each RATER item is to its customers so it can focus its resources on correcting any problems in those areas first.
- Firms need a benchmark to help them to put their SERVQUAL score into context.

5

MANAGING CUSTOMER SERVICE

5. MANAGING CUSTOMER SERVICE

Introduction

In Section 4, we looked at how to measure service quality using SERVQUAL. This model is based on the identification of a gap between what the customer expects in terms of customer service and their perceptions of what they received. In this section, we will look at how firms can close this gap. To do this, we need to understand how customer expectations and perceptions are formed.

Contents

5.1 Managing Service Expectations

In order for a customer to form an expectation in their mind of the level of service they might receive, they will need to draw on information that they already have. This information can be gained from their own past experience, information given to them by friends and family (WOM) or promises made either explicitly or implicitly by the firm.

Past experience

We use past experience to help us shape our expectations of what is likely to happen in the future. This is all part of how we learn.

Past experience has a strong influence on future expectations. Therefore, customers who have made a previous claim on their insurance policy will think back and draw on that experience should they have another claim. If the claim was well handled, the customer will most likely be positive about how their current or future claims will be handled. If they had a bad experience, this will lower their expectation of the service they expect from the claims handler. This can result in a positive outcome as it is more likely that perceptions of the claims service will this time exceed expectations. However, this may not always be the case. A bad past experience can also result in negative feelings that the firm must first overcome before the customer is willing to acknowledge that the service they receive is good.

The customer's past experience does not necessarily have to be with the same company; it could have been a claim that was handled by a competitor. The experience they recall may not even have been an insurance claim, but could be another experience with an insurer, such as a policy renewal, payment or mid-term adjustment. Indeed, the past experience does not necessarily have to be linked to the same type of product or service or even be from within the same industry sector. Customers may draw on their experiences with other service providers, such as retail stores or utility companies, to help them form an impression of what they can expect of the claim process and service levels. This is becoming more common as insurance is now provided by well-known high street brands and customers expect the same level of service quality in all their transactions and services.

Word of mouth

In section 2, we examined how word of mouth (WOM) can influence the decisions that consumers make in terms of which companies to buy from. WOM also has an impact on service quality expectations. Claimants will relay their experiences to friends and family and this will shape the expectations of others.

Awareness of competing brands

A brand is not just a name, logo, catchphrase or jingle, although these are a part of what physically represents a brand. A brand in its simplest form is everything that the name conjures up in your mind about that organisation or product. This includes an expectation of the level of customer service that you expect to receive.

Customers may be aware of competing brands through their own past experience, WOM from friends and family, or other sources such as local and national news stories in printed or online media or television consumer programmes.

Brands also communicate explicit promises, e.g. through advertising tag lines, and implicit promises through the brand values.

Explicit promises

Explicit promises are promises that are direct and clear. For example, advertising makes explicit promises to the consumer. Aviva promise to 'take care of what's important', McLarens state that 'quality is at the heart of everything we do' and Cunningham Lindsey declare that they have 'the right people, right place, right time'. These are all explicit promises that the customer will interpret and expect to be kept.

Explicit promises can appear on printed material (such as advertisements and company brochures) as well as in electronic format (such as a company's website). In addition, any verbal statement that an employee makes to a customer may also be interpreted as an explicit promise, for example if you promise to return the customer's call in 24 hours or to pass on the details of their claim to your manager.

Explicit promises, such as advertising and other marketing activities, are directly controllable by the firm. The most important point to remember is not to overpromise. This may well attract customers to the firm, but their expectations will not be met and negative WOM will result.

Activity

Find a copy of an advertisement, brochure or website for your own organisation and one for a competitor. Read through each and identify the explicit promises they each make. How do these promises compare? Do you think each company delivers against its explicit promises?

Implicit promises

Implicit promises are implied or expressed indirectly. Consumers glean or deduce information from cues that may or may not be intentionally provided by the firm. Implicit promises are often subjective as different consumers may draw different conclusions for the cues. A good example of this is with tangibles. We discussed the power of tangibles in Section 4. Here, we are concerned with the information that tangibles communicate. The most powerful tangible is price. This communicates to the customer information about the extent of insurance cover and/or the quality of service they will receive in the event of a claim. Where the consumer considers the price to be high, their expectations of the service they should receive will also be high. However, the key question here is what constitutes a high price in the consumer's mind.

Activity

In the airline sector, consumers can choose between a range of different airlines, ranging from low cost airlines to those priced more expensively. Even if we have not flown with a particular airline, we form an impression of the type of service we will receive based on the price.

Imagine two new airlines, one with the brand Harrods and the other with the brand Aldi. What would you expect to be the key differences in the in-flight service provided by each?

5.2 Managing Customer Perceptions

Customers have a role to play in customer service as they participate in the interaction and can therefore influence their own perceptions and satisfaction of the service.

Consumer emotions

The emotional state of a consumer is one of the biggest factors that has an impact on their evaluation of the service they receive. Consumers with a positive frame of mind will be more positive about their experience and less critical when making judgements. Staff can influence the emotions of the customer through their own social interactions. For example, a smile, increased eye contact, displays of gratitude and extending a greeting can all result in an increase in customer positive emotions and, in turn, a more positive customer experience.

Trade-offs on product and service features

All products and services have a range of features, such as price, availability, payment plans and, for insurance, the level of excess, extent of cover, etc. Customers rate product features, and some will be more important than others. In addition, customers also make trade-offs between features. For example, low customer service is more acceptable for a low priced product. It is important for companies to understand how their customers rate the features their products and services offer and what the trade-offs are. Variations in both can help to manage customer perceptions.

Equity and fairness

Customers do not consider their own experience in isolation, but will also evaluate their experience against the experience that other customers have (or may have) received. Customers want to assure themselves that they have been treated fairly compared to other customers. Some service settings are transparent, for example queuing, and in these settings fairness can be easily and quickly evaluated. Where comparisons are not directly available, customers will use their perceptions of fairness and/or consider other cues. For example, the customer may ask themself whether they have been treated fairly based on what they paid.

The influence of others

Customer perception can also be influenced by friends, family, co-workers and other consumers. Shared opinion on the quality of the service received will influence the customer's perceptions. It is possible that a satisfied customer who relays his experience to a friend may change his view on that experience if his friend considers the service he received to be poor.

Attributions for service success or failure

When a customer experiences customer service that is much better or much worse than they were expecting, they look for reasons to explain this difference. Attribution is the act of placing that responsibility. For example, if an insurance claim payment was not paid on time, the customers will consider where the blame lies. Was the delay due to a genuine mistake, was it outside of the firm's control or was it poor service? The answer decided upon will impact the customer's perception of that service. In most cases, the customer is unlikely to consider themselves to be at fault even when the evidence points to the contrary.

5.3 Closing the Gap

In Sections 5.1 and 5.2, we examined how firms can close the gap by looking at how they can manage customer expectations and customer perceptions. The gap can, however, be closed in five ways and managing customer expectations and perceptions is only one of them:

1) Customer gap. This is the gap between customer expectations and customer perceptions. Understanding and managing customer needs and expectations will close this gap.
2) Knowledge gap. This is the gap between management's knowledge of consumers' expectation and reality. To close this gap, the firm will need to undertake research to learn and understand their customers' requirements.
3) Policy gap. Here, managers understand what the customer wants but fail to deliver it in practice. Customer complaints may provide an insight into this problem and how to correct it.
4) Delivery gap. This gap occurs when the firm has correctly specified the right service for the customer but the employee fails to deliver on this service. Staff training and development can reduce this gap.
5) Communication gap. We considered this gap earlier under explicit promises. This gap is the result of overpromising by the firm.

5.4 Customer Complaints

A key point to remember when managing customer service is that the level of complaints is a poor indicator. Many customers do not complain to the firm, but simply walk away to their competitors and on the way tell their friends and family. Research with customers has found that only 5% of unhappy customers complain, so although complaints provide valuable information, they are only the tip of the iceberg in terms of identifying customer satisfaction.

All firms should have a clear customer complaints policy, which should loosely follow the following six steps:

1. Listen to the customer to identify the problem
2. Ask questions to clarify the problem in a caring way
3. Empathise with the customer to demonstrate you understand
4. Apologise without blaming anyone

5. Ask the customer what they would like you to do to solve the problem
6. Solve the problem.

Where possible, problems should be resolved without passing them on to another person. This not only saves the firm time and money, but also helps to improve customer satisfaction.

Activity

Find a copy of your firm's customer complaint handling policy. Identify how it compares to the above six steps.

5.5 Key Points to Remember

- Firms can close the gap by understanding how customer expectations and perceptions are formed.
- Firms can influence customer expectations, for example through their explicit and implicit promises.
- Firms may understand the cause of the gap, but need also to ensure this is correctly translated into action in terms of policy and delivery to improve the service.
- Customer complaints are a poor indicator of a firm's customer service.

6

CHALLENGES AND OPPORTUNITIES FOR CUSTOMER SERVICE

6. CHALLENGES AND OPPORTUNITIES FOR CUSTOMER SERVICE

Introduction

In the preceding sections, we have demonstrated how important good customer service is to an individual firm and the loss adjusting profession as a whole. We have also considered how service quality can be measured and how firms can manage the customer service process. In this final section, before we leave the topic of customer service and move on to consider ethics, we will briefly look at some of the key challenges and opportunities to providing good customer service.

Contents

6.1 Legal

At the beginning of this book, we examined how the Consumer Rights Act 2015 and the FCA's Treating Customers Fairly regulations offer protection to consumers. These legal requirements are the baseline for firms when formulating the levels of customer service they provide to their customers.

6.2 Industry Reputation and Consumer Trust

We examined trust at a company level in Section 2, but the reputation of an industry also impacts the individual firm.

Reputation and trust in the financial services sector as a whole was damaged by the recent recession, subsequent credit crunch and high profile cases of misselling. Many within the industry, including loss adjusters, insurers and industry professional bodies, have been working together to restore consumer trust and there are signs that this is now happening, as measured by the Edelman Trust Barometer. However, trust remains perhaps the key challenge for the sector going forward. Consumer knowledge of financial services is limited, and therefore any misdeeds within, for example, the banking sector will have an impact on the insurance and loss adjusting sectors.

In Section 2.4, we considered the negative consequences of low levels of consumer trust. All firms need to work hard to repair consumer trust, even when they may not have been party to the cause of the loss.

6.3 The Evolving Consumer

Customers are constantly changing in terms of the service they expect. If we were to compare customer expectations within the same group 10 or even 5 years ago, we would identify clear differences in expectations. These include:

Response times

The customer's definition of what is fast, or more importantly what is slow, has changed. Customers expect near immediate response at all times and are becoming less patient and less willing to wait for a response. Response times will differ by customer segment and according to the way in which they make contact with the firm. For example, in the case of social media, expectations are high. Industry experts advise that customers using Facebook expect a response within 24 hours, whereas those using Twitter expect a response within 2 hours. Firms need a clear strategy on how they will meet these growing expectations.

Personalisation

Customers expect products and services to be tailored to their needs. They want choice. They expect companies to remember who they are and whoever they speak with to have immediate access to their information and to provide a seamless service. In addition, in an age of 'cut and paste' and spell-checkers, customers expect accuracy in the documents they receive and in the information held in customer records.

Empowerment

Today's customers have access to a wide array of information via the internet. Whatever they need to know is available in a couple of clicks. As a direct result, customers feel empowered. They have a strong sense that the 'customer is always right' as they provide feedback online about their purchase or experiences. They expect to be listened to and to have their feedback acknowledged.

Activity

Review the customer feedback that your firm has received over the past month. Are there any patterns in the type of feedback received? How did your firm respond to this feedback?

Product knowledge

Many customers lack knowledge when it comes to financial services such as insurance and related services. When they compare insurance products, the key factor is often price rather than cover or service. There is growing concern that customers may be buying the wrong product or are underinsured. Both outcomes can have a negative impact on customer perceptions of the service they receive. The insurance industry as a whole has attempted to improve customer knowledge by simplifying products, educating the consumer about insurance and providing greater transparency on, for example, pricing. Loss adjusters should also embrace these initiatives, which will in turn help manage customer expectations.

6.4 Technology

The way in which people buy insurance, the way in which customer service is delivered and the way in which customers interact with firms is rapidly changing. There are new ways of doing business in terms of producing the product, servicing the customer and communicating with the customer. The range of channels can include physical locations, webpages, social media, live web chats, mobile applications and telephone communication to name a few.

The use of omni-channels, whereby companies use different channels to interact with the customer, present both advantages and challenges. The key advantage is the choice afforded to the customer in terms of how and when they interact with the firm. However, this choice also presents the challenge of meeting the needs of a diverse range of customers and providing a high standard of customer service across all the channels to a consistent standard. Omni-channels have resource implications for companies as they need to respond to customers contacting them through each channel in a timely manner. For example, if social media posts remain unanswered, this can harm the reputation of the company through negative word of mouth.

Activity

What channels does your firm use to communicate with its customers? Select two and consider whether your firm is providing a consistent level of service to the customers using each channel. If not, why is this the case?

6.5 New Entrants to the Insurance Market

In the past, insurers provided insurance, retail stores provided goods and clothing, and supermarkets provided food. Today, both retail stores and supermarkets provide a range of financial products including insurance.

When new entrants such as Marks & Spencer, Tesco and Virgin entered the insurance market, they brought with them new standards and norms from their own industry sectors. Customer service in retail had been very different to the insurance sector and this changed the expectations consumers had of claims handling. Why should the customer service they receive when shopping for clothes be any different to that of insurance and claims handling? All these services are provided by the same brand as far as the customer is concerned.

Activity

The Institute of Customer Service undertakes a semi-annual survey of customer satisfaction across 13 different industry sectors:

- Automotive
- Banks and building societies
- Insurance
- Leisure
- Local public services (e.g. fire service, library, council)
- National public services (e.g. NHS, post office)
- Retail (food)
- Retail (non-food)
- Services (e.g. AA, Autoglass, DHL)
- Telecommunications and media
- Transport
- Tourism
- Utilities (e.g. gas, electricity).

Which sectors would you put in the top and bottom five and why?

Where would you place the insurance sector and why?

Click on the link below to see whether you were right:

https://www.instituteofcustomerservice.com/media/image/customer-satisfaction-a3-1334.jpg

6.6 Key Points to Remember

- The legal requirements are the baseline for firms when formulating the levels of customer service they provide to their customers.
- The reputation of the insurance industry has an impact on consumer trust at firm level.
- Customers are constantly changing in terms of the service they expect.
- Technology is rapidly changing how firms interact with their customers.
- New entrants from different industry sectors have brought with them new standards of customer service.
- No news is not necessarily good news where customer service is concerned.

CILA

THE CHARTERED INSTITUTE
OF LOSS ADJUSTERS

Chapter 2 Ethics

1

ETHICS

1. ETHICS

Contents

Introduction

Ethics concerns the guiding principles governing right or wrong conduct and is often reflected explicitly in opinions, actions and behaviour.

This exists at many levels, e.g. individual, family, group, organisational, industry, professional and national. It has particular relevance to the way in which individuals and companies conduct their business. It also has relevance to regulation and self-regulation in industry and professional contexts, and therefore the extent to which people and organisations can conduct themselves ethically without regulations, laws or intervention.

Activity

How does ethics affect your interaction with colleagues in your job?

Of course, laws have been enacted and are constantly being developed to try to ensure that behaviour remains within the bounds of what is considered acceptable in society.

Culture is reflected in the way people think and behave. It relates mainly to groups of people (e.g. families, groups of friends, sports or work teams, organisations and nations).

Values are strongly held beliefs or views, which are often developed over time through experience and learning and can be difficult to change. They can be held individually or shared and are central to culture.

Morals are the beliefs of a group or individual as to what is right and wrong.

1.1 Ethics

Ethics is closely related to culture, values and morals. Culture, both in an organisation and the wider community or society, can exert a very powerful influence on what people believe, their attitudes, their principles, how they should behave and how they actually behave.

Ethical standards that are accepted in society, organisations or professions can be described as ethical norms. Ethical norms are expectations or standards of behaviour in society (for individuals, groups, organisations or communities). Some may be legally enforced and others simply concerned with treating people fairly and with respect. Similarly, they may be recorded in writing (e.g. rules or codes of conduct), or may be implicitly understood or even unspoken. For example, in some cultures, it is customary and expected that respect is given to older people.

Ethical standards are not always universal and also can change over time (e.g. as society changes and in relation to social trends) and in different environmental contexts (e.g.

at times of war or crisis). What was considered as socially acceptable in the past is not necessarily the same today (e.g. slavery, child labour).

There are three main schools of thought about the nature or source of ethical norms (see Section 2 for more detail) and the extent to which they have global or cross cultural relevance:

- Ethical Universalism
- Ethical Relativism
- Ethics and Integrated Social Contracts theory.

These three theories differ as to the extent to which ethical norms and standards are relevant across cultures, countries, industries or individual organisations, i.e. whether they are global or local, universal or specific.

There is some evidence that ethical standards are to an extent developing across the world. This trend has been supported by the rapid development of IT, the internet, speed of and access to modern communications, education, increased overseas travel, inter-country mobility, the impact of global companies, cross-border strategic alliances and global supply chains.

1.2 What is Ethics and why is it so Important?

Ethics is the application of general ethical principles to the actions and decisions of businesses and the conduct of their personnel. – Thompson, Strickland, Gamble, Peteraf, Janes & Sutton.

Ethics concerns the way in which organisations conduct themselves, or how they should conduct themselves, in their strategic approach and operations, and in particular their relationships with key stakeholders with an interest in, or influence or dependence on, their activities and performance (e.g. clients, customers, shareholders etc.).

In essence, ethics is based on general ethical principles as accepted in society in terms of what is right or wrong, good or harmful, acceptable or not acceptable, moral or immoral (e.g. dishonesty, bribery). Whilst society and social norms tend to dictate what is acceptable behaviour in business practice, the actual relevance of these can vary within the different areas of industry, business, professions and countries (e.g. the importance of avoiding inducements or bribery, confidentiality in the loss adjusting industry and confidentiality in the medical profession).

The dominant internal culture of a specific organisation can have a major influence on the ethical behaviour and standards of an organisation's staff (as demonstrated in the Enron case discussed in Section 6).

1.3 Ethics and Stakeholders

Ethics is particularly relevant to an organisation's relationships with its key stakeholders.

Stakeholders are any groups or individuals who have a stake, interest in or expectation of an organisation, its activities, performance or its operations. This can include a number of interested parties, e.g. employees, shareholders, sources of funding such as banks, customers, professional bodies, regulatory bodies, HMRC, competitors and even the local community (e.g. the impact of pollution from a company on its locality). The relative interest of stakeholders in an organisation can change over time and sometimes quickly, such as where a company suffers product failure or has adverse publicity.

The stakeholders of a company can be internal or external and sometimes both, such as trade union or professional body members.

Another key aspect of stakeholder relationships concerns the level of power stakeholders have to influence an organisation in a specific situation or strategic decision. This could include the influence of institutional shareholders in a company's decision to be involved in a merger, or the decision of the Monopolies and Mergers Commission to block a proposed merger.

This brings in corporate social responsibility and corporate governance, which we will cover in Sections 4 and 5. So, which of a wide range of stakeholders should or is it realistically possible for an organisation be responsible to?

In reality, it is not possible for an organisation to satisfy the interests of all its stakeholders and it should decide and try to prioritise which stakeholders are most important to its success and survival, or those with the most power to influence the organisation.

It is quite common for different stakeholders in a specific situation to have conflicting interests or expectations, e.g. a conflict of interest in a loss adjusting situation.

From a wider perspective, there are many examples of conflict of stakeholder interests, e.g. the recent proposed Navitus Bay offshore wind farm development in Dorset, which attracted a high level of interest, attention and argument, with strong views expressed by the interested parties for and against the project going ahead. Similarly, on a national scale, the recent UK EU referendum raised a clear difference and considerable conflict in stakeholder views and interests.

Looking at specific stakeholder groups, customers are important to most organisations. Therefore, aspects such as customer service and maintaining good relationships are essential aspects of running a successful modern business, particularly in a competitive marketplace where it is hard to gain but easy to lose customers.

Activity

List the key stakeholders in your job. Which are most important and why?

Ethics have become increasingly important in recent years for many reasons, such as increased stakeholder scrutiny (e.g. from customers, regulatory bodies and the media), the increasing focus on the Corporate Social Responsibility (CSR) of organisations, the impact of communications/internet/social media, education and the highly publicised non-ethical behaviour of some large organisations (e.g. Enron).

For many professions, e.g. accountancy, insurance, finance, legal, medical and media, standards of ethical behaviour have become a key focus of attention in recent years.

The accountancy profession was forced to take a critical look at itself and its practices in the aftermath of a number of high profile corporate scandals.

For the media industry, the press in particular have come under scrutiny in relation to its controversial conduct regarding invasion of privacy issues including the illegal activity of phone tapping.

The financial services industry has been in the public spotlight for a number of years and has been subject to various regulatory pressures, with the Financial Conduct Authority (FCA) being given increased powers to make organisations reform their practices, to fine them and to make them open to massive compensation claims and payouts.

Not surprisingly, where the professional and ethical behaviour of industries and organisations has been brought into question, this has often led to government intervention or new legislation, increased regulatory controls and closer scrutiny from interested stakeholders, and recognition within some industries and professional bodies of the need for better and more effective means of self-regulation (codes of conduct and professional guidelines).

Activity

Do some quick research to find out about any new regulations affecting the conduct of the financial services industry in recent years.

1.4 Ethical Issues and Ethical Risk

Many organisations have become aware of ethical risk in relation to the way in which they operate and conduct their business, and have identified key areas of ethical issues and potential risk that need to be managed carefully and with diligence.

For the loss adjusting industry, managing ethical risk is very important and is likely to include:

- Dealing with conflict of interest
- Claims management
- Confidentiality and disclosure of information
- Beneficial interests.

Activity

Look at CILA's Guide to Professional Conduct and identify examples of where conflict of interest can arise in loss adjusting.

It also means that companies in this industry must not only be ethical in practice, but must be seen to be conducting their business ethically by its key stakeholders, e.g. in terms of integrity, fairness, objectivity, reputation, image, etc.

1.5 Key Points to Remember

- Ethics affects all people and organisations, shaping the way they think, live, work, conduct transactions, do business, negotiate, agree and form relationships.
- It affects all types of organisations from one-man businesses to global companies, and governments.
- Ethical norms have a strong influence on how we behave.
- Ethics has always been important but has come under increased scrutiny in recent years as organisations need to be more accountable to key stakeholders.
- The relationship between an organisation and its most important stakeholders is central to its survival and success.
- For most organisations, doing business means ethical risk and potential damage from influential or powerful stakeholders. Therefore, recognising ethical issues and managing ethical risk has become increasingly important for organisations. This is particularly relevant to the insurance industry and loss adjusters.
- Ethics underpins standards of business practice and decision making, e.g. in settling insurance claims.
- Ethics is closely related to the culture, values and purpose of a firm.

2

ETHICAL THEORIES AND BUSINESS PRACTICE

2. ETHICAL THEORIES AND BUSINESS PRACTICE

Contents

2.1 Theoretical Roots

The roots of ethics go well back into history and in the twentieth century have origins in economic theory (e.g. JK Galbraith from the 1950s onwards), social theory and in political ideologies (e.g. capitalism and socialism). Also, most religions are centred on or have reference to ethics, morals or codes of behaviour.

More recently, ethics began to be widely discussed by academics, business consultants and business practitioners, in the US in the 1970s and in Europe in the 1980s.

This section outlines the theory and principles of ethical practice that you should apply as an adjuster.

2.2 Key Theories

There are three underlying schools of thought regarding the extent to which ethics, in terms of what is right or wrong, is a global or local phenomena. Do universal or different ethical standards apply across the world, in different cultures and in different organisations, or do they vary?

The school of ethical universalism takes the view that a common understanding does exist across the world and cultures in the most important concepts of what is considered right or wrong (e.g. truthfulness, honesty and integrity). This means a world with universally understood ethical principles and basic moral standards that are shared and practised throughout. From a practical or business perspective, this would be helpful and would make conducting business transactions, negotiations, agreements and developing relationships less complex and risky.

The school of ethical relativism offers a contrasting view that there are many or multiple sets of standards or ethical norms across the world, which reflect and relate to different societies, cultures, ways of living and of conducting business. Therefore, there are significant cultural, national or regional differences and ethical norms which vary across the world, and what is considered as ethical behaviour in one location or society is not necessarily the same elsewhere.

From a business perspective, this view implies increased complexity and risk and makes life harder for organisations. Particular examples of ethical differences relevant to business practice are attitudes and behaviour in relation to:

- Bribery and inducements
- child labour
- working hours

- the role of women at work
- consumer protection.

Considerable and well-supported research has been conducted in the area of national cultural differences, in particular Hofstede's *Cultural Dimensions*. Hofstede's studies, developed over many years, put forward a strong view supporting the extent of significant national cultural differences, which are still held to be influential in today's world.

Some of the key national cultural differences described as *cultural dimensions* include:

- Power distance (e.g. the relationship and distance of authority and differences in power between managers and employees)
- uncertainty avoidance (e.g. attitude to risk)
- individualism/collectivism (the tendency to work as individuals or in groups, or to make decisions individually or as a group seeking consensus of agreement).

Some of the country differences highlighted by the study included:

- High power difference, e.g. Latin American countries, Greece and Turkey
- low power distance, e.g. the USA, UK and Germany.

In terms of uncertainty avoidance, Japan was high and the USA low.

Also for individualism/collectivism, Japan and many other Asian countries showed high levels of consensus, whereas the USA a high level of individualism.

The impact of these differences on organisations, businesses and people are wide ranging, and may affect motivation, attitude to work, performance and rewards, management styles and leadership, communication styles, decision making, negotiating, and building relationships.

Activity

How do you think uncertainty avoidance could affect reaching a loss adjusting agreement with a claimant?

In summary, the Hofstede view would tend to support the theory of ethical relativism (also referred to as ethical diversity, see Section 4).

The cultural differences can also be reflected in areas of consumer business, such as very different attitudes to providing tips or gratuities, levels of consumer protection, return of faulty goods etc., and also in marketing methods and advertising campaigns.

Another key factor is language. Whilst English is probably the main business language in the world, companies have to be careful how they use or translate certain words, messages and brand names as these can have different meanings or be lost in translation.

The effect on companies, particularly those conducting business overseas or with overseas partners, is that it makes for a complex world. This does not just affect large global companies, but it can also impact on small medium enterprises (SMEs), many of which are involved in global supply chains that cross different national and cultural boundaries and encounter a range of ethical standards and business practices.

The ethics and integrative social contracts theory aims to bridge the gap between the two extreme views of ethical universalism and ethical relativism. It suggests that collective views on ethical principles and behaviour of individuals, groups and organisations form a common understanding that provides a basis to what is called a social contract which they are contractually obliged to follow.

This refers to first order ethical norms, which can be seen as universal and ethically essential (e.g. integrity and honesty), and to second order ethical norms, which can be more local and reflect cultural and regional differences. In terms of ethical behaviour, first order norms should take precedence to second order norms. Therefore, local norms can be stricter but not less stringent than universal norms.

Activity

Which of the above three theories of ethics do you think is most applicable to your area of loss adjusting?

From the 1970s onwards, the academic and business consultant, Archie Carroll, significantly expanded the area of interest in ethics both from an academic and practitioner perspective and developed a number of theories and models to be applied to organisational situations. In particular, *The Pyramid of CSR* (1991) focuses on the relationship between the economic, legal, ethical and philanthropic responsibilities of an organisation. In this model, the level of organisational responsibility moves from basic (economic) to higher (philanthropic):

Level of Responsibility (from basic to higher levels of responsibility)

Economic > Legal > Ethical > Philanthropical

- Economic refers to the funding, profit and financial accountability and sustainability of the organisation.
- Legal refers to conducting activities or business within legal requirements (e.g. in English law, this means in accordance with statutory laws, as passed and agreed by Parliament, and common law or case law, which develops over time and is based on the principle of precedent.
- Ethical refers to complying with or meeting ethical norms or standards (e.g. as in society, a profession or industry).
- Philanthropical refers to behaviour and activities showing responsibility or accountability to society, customers, employees and other stakeholders which exceed and are over and above the previous three levels of responsibility, particularly where there is no obvious gain to the providing organisation (therefore giving without gain).

The theory relates not just to what organisations do but also to their motives for doing it.

Activity

Following Carroll's theory, in terms of the ongoing survival and success of a firm, is it more important for the firm to meet its legal or economic responsibilities?

Much debate surrounds the relative importance of and the interrelationship between the levels of responsibility, particularly economic and legal responsibilities. Also, in recent times, the motivation behind CSR-related activities of organisations has been questioned (e.g. is CSR just PR, or is CSR another form of marketing?).

2.3 Ethics and Corporate Social Responsibility (CSR)

Closely related to ethics, the concept of corporate social responsibility may be defined as:

The commitment by organisations to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families *as well as the local community and society at large* – Johnson, Whittington, Scholes, *Exploring Strategy.*

CSR is not new, and has been subject to much debate and disagreement by business practitioners, consultants and academics for a number of years. For example, an eminent American economist and business consultant Milton Friedman (1970) expressed a strong view that the primary responsibility of a company is to its shareholders: *"the business of business is business … and the only social responsibility of a business is to create a profit"*. In other words, he believed that businesses should not be focusing their efforts and resources on non-profit making activities, and to do this would be against the best interests of their shareholders.

Conversely, in the 1980s, a view began to develop and gain momentum in the western world that organisations should take a wider and more socially accountable view of their responsibilities. A major proponent of this view was R Edward Freeman (*Strategic Management: A Stakeholder Approach*, 1984). This approach has become widely known as stakeholder management, which is now seen as central to the strategic survival and development of most modern organisations.

Many other proponents of the wider responsibility view include Charles Handy who in 2002 wrote: *"The purpose of a business … is not to make a profit. It is to make a profit so that the business can do something more or better. That "something" becomes the real justification of the business."*

2.4 Who should Organisations be Responsible to?

To develop this further, it is often argued that:

1. Just looking after profit and shareholders' interests can actually be bad for a business, e.g. bad publicity can lose customers, clients or suppliers and damage relationships with other stakeholders.
2. Conversely, recognising and satisfying wider stakeholder interests can be good for a business, e.g. good reputation, positive image etc. This can be described as *enlightened self-interest*.

"Companies have to be socially responsible or shareholders pay eventually." – Warren Shaw, former CEO of LGT Asset Management.

Here, the short-term versus the long-term perspective is also relevant as well as the short-term profit or longer term success in business, e.g. the possible importance of repeat business or developing good working relationships with suppliers, customers, clients and contractors.

Activity

How do ethics affect customer service?

This comes round to the argument again as to what extent CSR activities are driven by ethical or economic (or business) interests.

2.5 Different Views of CSR

What constitutes CSR is often viewed differently in different countries, regions or cultures. For example, in most western countries, it may be viewed as actions, behaviour and commitment beyond legal requirements, whereas in parts of Asia it may simply be meeting legal requirements. An example of this is health and safety at work, which in most western countries is a legal requirement, whereas in some countries (e.g. Africa) this is not necessarily the case. Different national cultures can also have intrinsic values that relate directly to social responsibility (e.g. Buddhism, Confucianism).

Activity

Your company is dealing with a claim that involves parties from two companies from culturally different parts of the world. How would you deal with this?

2.6 CSR Issues and Challenges

Over the last 20 years, CSR issues have emerged in a number of areas and have affected many organisations, particularly global companies operating across national and cultural boundaries and any other organisations with high stakeholder visibility. Issues have included:

- working conditions/employee safety
- executive pay
- supplier control/coercion (e.g. late payment made to small suppliers)
- consumer health (e.g. smoking, alcohol, obesity, gambling)
- product failure
- environmental pollution
- carbon emissions/global warming
- tax evasion (e.g. controversies around Google, Apple and other global companies)
- market control … and many others.

Activity

Find a recent example of major product failure. What were the costs to the company involved?

Many organisations talk about CSR, their policies and activities, but implementing them can be more difficult. Consider a global company such as Nike or Shell – they will have CSR policies but making them work in countries with different ethical standards, laws or levels of corporate governance can be problematic. Nike among others was heavily criticised in the past for its alleged supply chain involvement in child labour, sweatshops, etc. in some Asian countries. However, it can be difficult to control suppliers in other countries with lower wage levels and standards of employee safety and care, as well as different labour laws.

2.7 Key Points to Remember

- The extent to which ethical standards or norms extend across nations or cultures is a question of much debate. However, it is clear that ethical differences do exist and these need to be considered when conducting business.
- There are two extremes in terms of the shareholder versus stakeholder view of CSR, i.e. the profit-focused view of Friedman and the wider stakeholder perspective of Freeman.

- Carroll's pyramid theory raises questions concerning the range, nature and extent of organisational ethical responsibility and also importantly the motivation behind ethical behaviour (or lack of it).
- CSR is a common topic in companies, boardrooms and published company reports, and whilst some global organisations may try to set and implement corporate global standards, it can mean different things across the world.

3

ETHICAL DECISION MAKING AND CSR

3. ETHICAL DECISION MAKING AND CSR

Contents

3.1 Ethical Decisions

Organisations are often faced with and have to make ethical judgements and decisions. This can be difficult and may involve ethical problems, dilemmas and risk (e.g. dealing with conflict of interest).

The importance of the decision will depend on the situation and the level of responsibility we have in that situation, and to the risks and consequences involved.

Activity

How did you decide to become a loss adjuster?

For organisations, decisions can be either day to day/operational or they can be major or strategic decisions that are likely to have a major or long-term impact on the company and its future.

Making decisions can be difficult. They can be made proactively, usually where there is a choice of alternative actions and time to consider the options (such decisions can also be planned), but decisions are often made reactively, e.g. when under pressure or faced with an unexpected problem, challenge or awkward situation.

Often, difficult or risky decisions are shared or discussed with others involved such as work colleagues, senior staff, or friends or family.

Activity

Think about your loss adjuster role. How do you make difficult decisions?

Ethical decisions concern the choices faced by individuals or organisations that are seen to be right and fair and that lead to an agreed outcome or resolution that is acceptable to all parties involved.

A key question is fair to whom? The right decision in a particular situation, and who should make it, can be particularly difficult if different stakeholders have differing or conflicting views about what is ethical or fair in a particular situation or if there are conflicts of interest (e.g. minimum wage, consumer protection, provision of state benefits etc.).

Activity

Consider a claim where the insured tells you he will accept settlement of £85,000, but you are aware that insurers are prepared to pay £100,000. What factors should you consider to reach an ethical resolution?

3.2 Factors Affecting Ethical Decisions

These factors can be internal or external but are usually a combination of the two.

External factors include social norms, industry standards, regulatory bodies, professional bodies and codes of conduct and other potentially influential stakeholders including press/media, government, non-governmental organisations and pressure groups (e.g. Greenpeace).

Internal factors include values, culture, organisational purpose and mission, management style, HR factors, staff capability and training levels, management/staff levels of motivation plus internal stakeholders including management, employees.

Factors such as trade union membership or professional bodies (e.g. CILA) are externally derived but are present within organisations. Similarly, shareholders could be both internal and external (e.g. employee shareholders, family shareholders).

3.3 Ethics and Organisational Culture, Values and Purpose

Organisation culture is not something that can be seen, but it can have a very powerful influence on what an organisation does, its key decisions and how it can be managed. Its presence is felt through values, attitudes and behaviour.

There are many definitions of culture but, referring to the nature of organisational culture, Charles Handy coined the phrase: *"The way we do things around here"*. This has a strong focus on how behaviour becomes normalised and established over time in a group or organisation, almost like unwritten or even unspoken rules.

It is also important to distinguish between internal or organisational culture and external culture such as national or regional differences or cultural influences in society. However, external culture can influence organisational culture through national cultural differences, social attitudes to work, etc.

Another important feature of culture is that it often strengthens over time, particularly with groups of people or organisations). This means it can become ingrained and difficult to change, which is a common problem when change management is required in an organisation.

The key elements of culture are values, beliefs, attitudes, traditions, accepted ideas and practice and, as Charles Handy pointed out, ways of doing things.

Ethics also affect an organisation's decision making process in terms of its attitudes to risk and who is involved in making the decisions. When we look in Section 6 at the Enron scandal and corporate collapse, it is evident that the culture of the company appeared to largely ignore the impending risks of its irregular accounting practices and fraudulent activities, and it seemed to think it was bullet proof in terms of its lack of responsibility to its key stakeholders.

The ethical views and decisions of an organisation are also likely to be affected by the fundamental purpose of the organisation, its strategic intentions, mission and objectives (e.g. profits, customer care, providing a good service, technological advancement, etc). This is also closely connected to the values, culture and ethical stance of an organisation.

Activity

How would you describe the culture in your firm? What's most important in terms of values in conducting your business?

3.4 Who Decides What is Ethical?

This decision depends greatly on the individual organisation, its culture, values and management style, its position in the marketplace, its area of activity and business, the environmental influences on it at that point in time, and in particular the power, influence and interest of its key stakeholders. In some professions, ethical standards and good practice can be guided by the professional body itself (e.g. the CILA's *Guide to Professional Conduct*), but ethical dilemmas can still emerge for organisations at operational level.

Ethical decision making can be seen as a general pattern or standard of behaviour (e.g. good practice in a firm or industry), but it is often required in specific situations such as a claim or dispute situation. This has clear relevance to loss adjusting firms which will follow ethical policies at company level (e.g. statements of good practice) but will still need to ensure that individual staff can operate effectively and ethically in practice and ethically in specific situations they are dealing with. This may also mean loss adjusters referring to senior colleagues or line managers when handling complex situations, particularly where ethical risk is involved.

The long-standing debate concerning regulation versus deregulation (in particular industries and areas of business) relates closely to standards of ethical behaviour. In recent years, the focus has been on the media, financial services and energy industries.

Activity

How would you resolve a claim situation involving two parties with very different ethical standards?

3.5 Key Points to Remember

- Ethical decision making can be difficult and problematic for individuals and companies.
- Values, culture and ethics are closely connected (values concerns what people believe is right or wrong, acceptable/not acceptable).
- Organisational culture underlies the behaviour of organisations, how their relationships with key stakeholders are managed and how they make decisions.
- How ethical decisions are made and by whom are particularly important to the insurance industry and loss adjusting firms.
- Ethical guidelines can be helpful, but the ability to deal flexibly with specific situations is very important.

4

ETHICAL DIVERSITY, ETHICAL BEHAVIOUR AND DEALING WITH UNETHICAL BEHAVIOUR

4. ETHICAL DIVERSITY, ETHICAL BEHAVIOUR AND DEALING WITH UNETHICAL BEHAVIOUR

Contents

4.1 What is Ethical Diversity?

One of the underlying problems and challenges for organisations striving to make ethical decisions and to operate socially responsibly is that whilst the theory of ethical universalism has some relevance, ethical behaviour or standards are often not universal. In reality, what constitutes ethical behaviour or standards can vary greatly between countries, regions, industries, organisations, groups and individuals. This is closely related to culture and values and is often known as ethical diversity (which relates closely to the theories of ethical relativism and the integrated social contracts).

Hofstede's studies on national culture suggest many differences between nations which have developed over time and have a direct impact on the way people think and behave and the way they build relationships, and conduct purchasing and business transactions.

There are counter arguments that suggest that modern global influences are eroding some of these national differences, for example through the impact of the internet, IT, social networking, global fashions, eating habits (*McDonaldisation*) and social trends. However, a further argument is that, despite globalisation, national differences are increasing, e.g. through the growth in nationalism and independence of countries and regions. In fact, there are now more countries in the world than 40 years ago.

4.2 Ethical Diversity and Stakeholder Complexity

The potentially wide variation in ethical perception and standards is likely to be particularly problematic for organisations operating on a global or transnational scale, as well as for those dealing with a range of different stakeholders with different interests and expectations, which can involve stakeholder conflict. For example, the insurance industry and loss adjusters in particular are in the focal position of trying to represent the interests of two or more parties.

Loss adjusting firms can be seen to be operating in a supply chain, looking to satisfy the interests and expectations of insurance company clients and claimants, ideally looking for a balanced outcome or settlement that is perceived as fair and equitable to all the parties involved, often in a conflictual and emotional situation where loss and damage is involved.

It may require dealing with stakeholders with different and sometimes conflicting interests, who may have different views of what is ethical or fair, both in general and specific situations.

4.3 Drivers of Unethical Behaviour in Companies

Reasons for unethical behaviour can include:

- Weak management, e.g. poor quality of management that lacks control and clear leadership.
- Faulty oversight by directors or senior management. Being out of touch with the operations of a business can be the result of a hands-off approach from the top. There is sometimes a gap, particularly in large organisations, between senior or strategic level managers and managers and staff at operational level. This can also mean a real difference between policy and practice. Internal communication and reporting structures can be very relevant in such situations.

  In the recent investigation by the Press Commission into the alleged phone tapping activities of News Corporation (TNC) staff (particularly at the News of the World newspaper), senior executives of the company, including Rupert Murdoch, claimed that they were not aware of any illegal activities taking place in the company. If so, this was a case of faulty oversight by the directors of the company.

  In contrast to the TNC situation, in the Enron case (see Section 6), it appears that most of the company's senior management not only knew about the illegal and unethical activities in the company, they actually instigated, endorsed and encouraged this behaviour. In fact, this behaviour became a key element of the culture of the company.
- Poor and ineffective corporate governance structures and processes. These are formal systems of defining accountability and responsibility to internal and external stakeholders (see Section 5).
- Pursuit of self-interest or personal gain. This is where directors or senior managers put their own interests before those of the company they are employed by. These may be personal, financial, promotional or career interests.
- The culture, values and purpose of the company. These factors relate to management style and the objectives of the company. Also relevant are the stakeholders that the company sees it has most responsibility towards, e.g. its shareholders, managers, clients, employees or clients. This relates directly to ethics and social responsibility, such as Carroll's pyramid model.
- Pressure on managers to meet targets, performance levels, etc. This can come from both internal and external drivers. It can relate to the management style in the company or to situations where subsidiary companies are under performance pressure from a parent company or from other influential stakeholders, such as city analysts or major investors, to produce good financial results. Another source of external pressure comes from competitors. All these factors can lead to short-termism.
- Short-termism is where companies or employees focus on short-term gain rather than longer-term benefit or development. This could apply to seeking short-term profits rather than longer-term development and success, or to building relationships and trust with key customers or clients. Studies suggest that, in countries such as the USA and the UK, a relatively short-term outlook and approach to business and business development prevails, compared to a longer-term, more sustainable view in countries such as Germany, Japan or Sweden.
- The agency problem. This is where there is a separation of control between the owners and managers of a business, which raises the issue of whether the managers have the same interests and motivations as the owners. It is also known as the agency/principal issue. It has increased in many parts of the world as the nature and structure of ownership of organisations change.

It is also important to note that unethical behaviour can and has occurred in most sectors, including private, public, not for profit and, with recent examples, the very competitive charity sector. This includes the collapse of Kids Company and also questionable practices of other charities concerning pressurised methods of funds collection and inappropriate use of funds.

4.4 Reasons for Ethical Behaviour in Business

There are two main areas to consider: the moral and the business case.

In the moral case, organisations should be, and should be seen to be, acting within or above ethical norms. This has strong relevance to the image, reputation and status of the business. The speed and viral nature of modern communication can be very supportive or very damaging to a company. It is much harder nowadays to hide unethical behaviour and the risk of exposure is high.

In the business case, a good moral or ethical status or reputation can positively impact on customer or consumer perception of a product or service, on business relationships, gaining and retaining key clients, and contracts and suppliers. Conversely, actual or perceived unethical behaviour or misconduct can have the following negative impacts:

- loss of business, customers (e.g. as recently with Barclays high street banking) and contracts. This can be accelerated by negative word of mouth with both consumer (B2C) and business to business (B2B) customers.
- damage to other key stakeholder relationships. For example, in 2009/10, following loss of reputation, Tiger Woods lost $22 million in sponsorship and endorsements, which included Nike and Gatorade sports energy drinks. It is claimed that this had a knock-on loss effect of millions of dollars for the shareholders of those companies.
- penalties. Companies can face severe government or regulatory authority fines and be required to make financial payouts to affected customers. For example, according to the Guardian, the compensation, fines and legal costs payable by the UK financial services industry for PPI misspelling have totalled £75 billion since 2011, with the four major banks estimated to be liable to pay another £19 billion by the end of 2017.
- imprisonment for executives (e.g. financier Bernie Madoff received a 150-year prison sentence in the US). Most of the senior Enron executives received prison sentences for conspiracy and fraud.
- professional body fines or penalties (e.g. as per the CILA Charter).
- legal claims and lawsuits. These could be civil claims for damages, negligence, etc.
- negative impact on the share price of a company (therefore a cost borne by shareholders) which can have severe consequences on a company's financial health and status. For example, in the face of the growing corporate scandal, Enron's share price fell from a peak of US$90 in August 2000 to virtually zero in 2001.
- internal costs to the company, e.g. legal representations, HR costs including retraining, loss of key staff, difficulty in attracting talented staff, demotivation/low morale of staff, cost of change management programmes, etc. Other internal costs could include the expense of setting up compliance systems and processes or employing external systems auditing or consulting companies.

Factors such as media focus or attention can also damage an organisation both from a moral and a financial perspective (e.g. impact on reputation, integrity, reliability, and product and service quality). This can be difficult to defend or counter, particularly for smaller companies with fewer resources and less clout.

Reputation is a major intangible resource for companies that is often key to success. Loss or damage to it can be a serious blow. The tangible or financial value to a company of good reputation or image can be difficult to quantify. However, when it is lost, the financial cost or loss is often very clear in terms of lost business, reduced revenue and profits, fall in shareholder value, reduced credit ratings etc. Benjamin Franklin, American Statesman, Investor and Philosopher, summarised reputation as follows:

"It takes a good many deeds to build a good reputation and only one bad one to lose it."

In many aspects, the moral and business case interrelate, which is why a good ethical, socially responsible status makes good business sense. This can be described as enlightened self-interest.

> **Activity**
>
> *Look at CILA's Charter. What can happen to loss adjusters who breach CILA's Professional Conduct Guidelines?*

4.5 How can Organisations Deal with Unethical Behaviour

Unethical behaviour may be exhibited by insurance companies, clients, loss adjusters or claimants.

In terms of the internal management approach of a firm, the culture, values, recruitment, training policies and staff capability in managing relationships all have relevance. The ability to deal with potential conflict of interest and the potential stress involved are also relevant.

To manage relationships with clients and claimants, clear communication of good practice, principles and professional conduct supported by approaches to encourage ethical behaviour are important (e.g. emphasising the benefits of an agreed acceptable outcome to the adjustment and agreement process).

Organisations should develop means of deterring or discouraging unethical behaviour, such as penalties or sanctions for breach of warranty or breach of professional conduct.

> **Activity**
>
> *How does your firm decide what is ethical or unethical behaviour? Who would normally decide?*

4.6 Building Ethical Organisations and Ethical Behaviour in Practice

The following factors can help an organisation become more ethical and ensure ethical practice, particularly in the loss adjusting industry:

- Having a clear view of areas of potential ethical issues and risks
- Being aware of potential ethical differences and stakeholder conflicts
- Developing clear values and putting them into practice in the culture of the organisation
- Managing the expectations of key parties
- Dealing as equitably as possible with conflicts of interests

- Having clearly understood policies and processes for claim management, dealing with conflict of interest and maintaining confidentiality
- Establishing clear routes of internal communication and reporting structures (e.g. knowing when to refer to a senior or line manager)
- Practising communication and openness with clients and claimants, within the bounds of confidentiality, and explaining the rationale and reasons for a decision
- Being able to provide clear evidence (e.g. to internal and external stakeholders) of internal critical self-examination or internal audit of ethical practice
- Demonstrating ethical leadership and ethical principles in practice
- Effecting change management where required
- Training (e.g. dealing with potential conflict, tact, interpersonal skills and legal knowledge)
- Working within and to the guidelines as provided by the CILA *Guide to Professional Conduct*.

A final point here relates to the growing problem of cybercrime, which has particular relevance to organisations dealing with, storing and communicating confidential information. Clearly, this applies to the insurance industry and to loss adjusting firms where confidentiality and disclosure of information are critical aspects of the business. Therefore, attention to this issue is vital.

Activity

Refer to CILA's guidelines and provide two examples of potential conflict of interest.

4.7 Key Points to Remember

- Ethical standards are likely to vary across different people, companies, industries, countries and cultures; it is not a level playing field.
- Different stakeholders and interested parties can have contrasting or conflicting expectations of an outcome. Stakeholder situations can be complex and often involve conflicts of interest.
- Unethical behaviour in organisations can be caused by many factors, but it often relates to weaknesses in management control and processes and ineffective corporate governance structures.
- Dealing with unethical behaviour requires clear policies and communication, and the flexibility to deal with specific situations is essential.
- Both internal and external visibility of good ethical policies and practice are vital for the insurance industry and loss adjusters in particular.

5

GLOBAL ETHICS AND CORPORATE GOVERNANCE

5. GLOBAL ETHICS AND CORPORATE GOVERNANCE

Contents

5.1 What is Corporate Governance?

Corporate governance concerns who an organisation primarily serves and how its managers should be accountable and be held responsible for this. For example, in the UK, company directors have legal responsibility and potential liability for the actions of the company.

"Corporate Governance is concerned with the structure and systems of control by which managers are held accountable to those who have a legitimate stake in an organisation." - Johnson, Whittington, Scholes – *Exploring Strategy.*

We can see from the above definition that corporate governance concerns the relationship between an organisation and its stakeholders, and also that it requires formal systems, controls and processes within the firm to enable effective and accountable governance to take place. This can include a governance statement that outlines the governance structures for the organisation.

Corporate governance has become increasingly important in recent years and relates to and affects all types of organisations.

5.2 Driving Factors

The increased focus on corporate governance has been driven by many factors including:

- The trend of separation of ownership and control in many organisations (known as the agency problem or the principal/agency issue)
- The growth in strength of the view that organisations should take into account, and be accountable to, wider stakeholder interests
- The impact of IT and the speed of communications, which has made it harder for organisations to hide unethical practices or activities, together with the increased risk and potential costs and damage of exposure
- The number and impact of high profile corporate scandals in the last 20 years
- Increased regulation, plus greater emphasis on industry and professional guidelines and codes of practice.

We can see that the drivers are a combination of both internal and external factors. These include the need to increase external visibility of the activities of organisations, the pressure to comply and be accountable, and recognition within companies of the need (as a minimum standard) to comply and to reduce risk and potential damage.

Stakeholder complexity, global differences and ethical diversity again become relevant because formal approaches to governance structures are not standardised but vary across the world. The question remains as to which stakeholders an organisation should be accountable to, or most accountable to.

Activity

Which stakeholders are most important to the governance of your firm?

5.3 The Chain of Governance

This describes or identifies the groups of different stakeholders directly involved in and having an influence on an organisation's governance structure, as well as how the different parties in the chain interrelate with each other.

The chain of governance in each individual organisation depends on various factors including:

- The type of organisation (e.g. service, manufacturing)
- The geographical coverage of the organisation (e.g. local, regional, global)
- The business sector (e.g. profession or industry)
- Size of the company, with large organisations likely to have a longer and more complex chain of governance
- The company's supply chain and particularly its relationship with suppliers, distributors, agents, brokers, etc.
- The way the company operates (e.g. all key activities in house, or using outsourcing or subcontracting of activities). Outsourcing can be very cost effective, but it can add complexity to the formal responsibilities of a company in terms of governance and legal aspects. Similarly, with collaboration agreements, joint ventures, strategic alliances, franchising and licensing agreements, there is likely to be a gap between ownership and control.
- Its ownership (e.g. private or public ownership, or joint ownership such as joint ventures or collaborations).

Different types of ownership include:

- Public, private or not for profit sector organisations. Private companies tend to be owned by their shareholders, and public companies by the government or government agencies. Many countries still have state-owned corporations (e.g. many major oil and energy companies in the world are state owned). Additionally, some organisations are combinations of public and private ownership or are partly privatised (e.g. dental practices in the UK may be part NHS funded and part private).
- Larger private sector companies, either privately owned or with shares that can be openly traded. Privately-owned companies are not always small (e.g. Virgin is one of the largest private companies in the UK).
- SMEs, often family owned or owned by an entrepreneur who set up the business.
- Subsidiary companies. Many firms, large and small, are owned by a larger parent company or are part of a conglomerate. They are often managed as separate business units (e.g. the Virgin group).
- Family-owned businesses (these are often small businesses or SMEs, although there are large family-owned business throughout the world, such as Wal-Mart and Benetton).

- Professional partnerships (e.g. accountants, insurance brokers, medical practices, solicitors and business consultants). They are often owned by the senior partners in the practice.

Activity

Are universities in the public or private sector?

5.4 Governance Structures

Whilst approaches to governance and governance structures vary across the world, they generally fall into two main classes: the shareholder model and the stakeholder model.

Structures can also be affected by the type of organisation, the sector it operates in and its ownership. There can be major differences between the public and private sector.

Reporting structures are an important aspect and can typically include accounts, analysts' reports, company briefings, budgets/targets and operating reports.

The shareholder model of governance is most relevant to the US and the UK, where it is common for the shareholding of a company to be quite widely dispersed, with lots of shareholders, including many small investors. The prime focus is on generating wealth for the company and its owners rather than the wider interests of other stakeholders such as employees. However, it could also be argued that the success of an organisation is likely to benefit its employees.

Shareholder loyalty is often not high and, for many investors, shares can be easily bought, sold and traded without consideration of the potential impact on other stakeholders. Therefore, an interest in the organisation can be largely financially driven and be a short-term rather than a longer-term interest.

In contrast, the stakeholder model of governance relates to a wider stakeholder view of wealth creation and the successful development of an organisation. In this case, the management involves and takes more account of wider stakeholder interests in the performance of the company. Whilst this includes shareholders, it can also encompass other investors/sources of funding, such as banks, employees, union representatives, etc.

Historically, economies such as Japan, Germany and Italy tend to follow the stakeholder rather than the shareholder model of governance. This has relevance also to national cultural differences (see the Hofstede studies), which are often reflected in closer and often more long-term relationships between companies and their sources of funding.

There are advantages and disadvantages of both models of governance. The main advantage of the stakeholder model is that it can offer long-term stability to companies, such as through funding and investment for new product development or production facilities, which can support more sustainable company growth and development. A disadvantage is that companies can be subjected to more interference by a wider range of stakeholders, which can also slow down the decision making process.

The shareholder model would normally benefit shareholders, e.g. through a higher return on their investment. Criticism of the model centres on its shorter-term view of a company's priorities.

Activity

Find out how governance is structured in your company and the key processes involved.

5.5 Governance – the Global View

As already indicated, different governance systems are prevalent in different areas of the world and can relate to local culture and historical practice. However, governance has come to the fore globally, supported by international pressures (particularly with the increased globalisation of business), and there appears to be a global trend towards the shareholder model. This includes countries that have traditionally shown a wider stakeholder approach, such as Japan where there are pressures for change with an increase in institutional and overseas investment, and India where there are social changes in the ownership, structure and control of companies as the pace of modernisation increases.

Other trends that have supported the focus on governance structures include government action in many countries in an attempt to improve and tighten up areas such as accounting standards and auditing independence. These are key areas of concern that have emerged from some of the major corporate scandals. Of course, governmental action has related to a number of large international companies (including accountancy firms), which has also added to the pressure for a level of uniformity in global governance standards.

Activity

Why is corporate governance important to loss adjusting firms?

5.6 Key Points to Remember

- Corporate governance concerns both the legal and ethical responsibilities of a company to its stakeholders, whereas CSR (in many countries) is seen as over and above legal responsibilities.
- It is formal rather than voluntary accountability and requires clear and effective systems and processes to be put in place by a company.
- In recent years, the focus of responsibility and accountability of companies has increased.
- There is no global standard for corporate governance.

6

ETHICS, CSR AND WHISTLEBLOWING

6. ETHICS, CSR AND WHISTLEBLOWING

Contents

6.1 Introduction to Whistleblowing

Whistleblowing is a term that came into use in a business and organisational sense largely in the 1990s. It was particularly brought to the attention of many key stakeholders by the exposure of the unethical and illegal activities of some large US corporations (e.g. Enron, Tyro, WorldCom, Lehman Brothers and Madoff) often involving financial irregularities and large-scale fraud.

6.2 Who are Whistleblowers?

Whistleblowers are normally individuals (although they can be groups) who become aware of covert, unethical, illegal or unfair practices being conducted in or by an organisation (usually the organisation in which they work/ed) and who are prepared to disclose or expose this internally, or if necessary externally to other influential and interested parties or stakeholders (e.g. professional or regulatory bodies, government agencies, the press/media, shareholders, customers etc.).

Whistleblowers can also be groups or individuals within an organisation who are dissatisfied with the way it is being managed or run, who would like to see changes or improvements and who are prepared to voice their ideas, views or objections within the company and make a visible stance.

6.3 What's in it for Whistleblowers?

A whistleblower's motivation may be moral consciousness, strong personal values and beliefs, ethical standards, or concern or dissatisfaction about the negative impact of the firm's activities on stakeholders (e.g. with Enron, it was large-scale defrauding of shareholders).

Whistleblowers can face considerable personal risk in pursuing exposure, such as legal action, loss of employment and earnings, reduced promotion or employment prospects, etc. There may be a lot at stake and understandably many individuals with concerns may decide to keep the knowledge to themselves rather than risk damaging their prospects for their ethical principles.

6.4 Impact of Whistleblowing

While whistleblowing is still a controversial area, it has had a significant impact on the ethical and CSR approach of organisations and how they are perceived and scrutinised by interested parties/stakeholders. It has also focused attention on the accountability of organisations and encouraged transparency of internal and external activities. It also questions the extent to which industries are capable of ethical and legally acceptable self-regulation and whether there is a need for increased external regulation.

6.5 What Happened at Enron – the Events, Impact and Relevance

The Enron scandal is often seen as the tipping point that accelerated global interest and focus on the related areas of ethics, CSR and corporate governance. Enron was a globally operating organisation with a high reputation. Whilst not the only high profile corporate scandal, the events and subsequent fallout had far-reaching political, financial, legal and social implications.

The events – up until the scandal, Enron appeared to be a very successful US-based corporation operating in the electricity, natural gas, communications and pulp/paper industries. The company employed around 20,000 staff prior to 2001, with subsidiary operations around the world (including in the UK). The status of the company was evident by it being named by Fortune magazine as *America's Most Innovative Company* for the years 1996 to 2001.

However, behind this façade of great success, Enron had been conducting many of its activities, and in particular its financial practices, illegally and unethically for a number of years, at least back to the early 1990s.

The impacts – For Enron, the immediate consequences included loss of reputation and a sharp decline in its share price and therefore the valuation of the company. This quickly led by 2001 to bankruptcy; this was the largest in history, only surpassed by WorldCom in 2002 and Lehman Brothers in 2008, which also concerned financial wrongdoings/ irregularities and fraud.

Enron's accountancy firm, Arthur Anderson, in addition to its role in not effectively auditing Enron's accounts, was found guilty in 2002 of obstruction of justice (which apparently included destroying key documents pertaining to the Enron audit). The firm was barred from auditing public companies and quickly went into dissolution. It was effectively destroyed by its involvement in the debacle and has failed to recover on any scale.

Most of Enron's key executives faced criminal investigations and served or are serving prison sentences. In 2006, two of the senior executives (Skilling and Fastow) faced charges of conspiracy, fraud and insider dealing and were subsequently imprisoned.

This unprecedented event caused a major shock in the financial and corporate world and brought significant changes in terms of laws, regulation and vigilance relating to companies and accountancy firms.

In terms of legal impact, the US government quickly brought in new legislation – the Sarbanes-Oxley Act of 2002. Additionally, the regulations surrounding accountancy and auditing practices were reviewed and tightened, particularly in terms of accounting firms' auditing activities being clearly independent from their clients.

What did Enron do wrong?

It eventually emerged, primarily through the internal whistleblowing activity of Sherron Watkins, that senior executives in the company had deliberately manipulated the company's finances to create an unrealistic, misleading and inflated view of its financial condition. In particular, it misled its shareholders, although other stakeholders including employees, suppliers, contractors, etc. were also subsequently affected.

Throughout the 1990s, the company had developed and conducted irregular accounting procedures, also closely involving Arthur Anderson, who were one of the world's leading accountancy firms at the time.

Enron used a range of deceptions, practices and tactics to hide its activities, all which made the company appear more profitable than it really was. Once into these deceptions, the company had to work harder and harder to cover its tracks.

All the while, the company was misleading the market, investors and its shareholders through its apparent massive profits, which saw its share price rise to new levels and enabled it to maintain a strong credit rating whilst it was actually losing money. In other words, the company was involved in a massive scam.

At the same time, some of the Enron executives became involved in insider dealing (i.e. trading the company shares with the unfair advantage of inside knowledge, normally for personal gain). This is illegal in most developed countries in the world. In 2001, Jeff Skilling, Enron COO, sold his own shares whilst at the same time encouraging employees to keep their shares.

The company also used offshore accounts to help hide the growing company losses.

Another tactic employed by the company was to set up a number of limited liability entities, which again allowed it to transfer liability away from its accounts. In creating these off-the-books companies, the CFO, Andrew Fastow, was able to syphon off for himself, family and friends hundreds of millions of dollars, paid for by the corporation and its shareholders.

Activity

Find out what happened at Lehman Brothers. Which stakeholders lost out most from the corporate scandal?

How was the wrongdoing uncovered?

The key character in the whistleblowing activity was Sherron Watkins, who at the time was Vice President of Corporate Development at the Enron Corporation. In 2001, Watkins, who had been concerned about some of the company's accounting practices for some time, brought to the attention of the Enron Chairman and CEO, Kenneth Lay, accounting irregularities in the company's financial reporting. Later that year, the company announced a significant loss and, in October 2001, the US Securities and Exchange Commission opened an investigation into Enron's transactions, which led to a long series of investigations and court cases.

Activity

Referring back to Carroll's levels of responsibility theory, what was Enron's most important responsibility?

What happened to the whistleblowers?

Although Sherron Watkins was later criticised for not reporting her concerns earlier to her superior, she managed to avoid much of the damage to Enron and came out of it as something of a celebrity. She was seen by many as a brave and determined woman who was prepared to take the risk of challenging the power of a large organisation, her employer.

Her career expanded publicly into giving high profile speeches at colleges and management conferences and, in 2002, she published a book on the problems surrounding corporate culture: *Power Failure – The Inside Story of the Collapse of Enron.* Also that year, she was announced as one of three "Persons of the Year" by Time magazine. The other two were also female whistleblowers who hit the headlines at the time (Cynthia Cooper of WorldCom and Coleen Rowley of the FBI).

Sherron Watkins was subjected to a number of legal investigative procedures and US government committees from 2001 until 2006, but appears to have survived and prospered from a difficult and highly risky whistleblowing experience. Her involvement certainly seems to have made a difference to the way in which large corporate organisations conduct their financial activities and how they are audited and regulated.

Making a decision to whistleblow in such a situation was not only risky for herself, particularly in that she received only limited support from her superiors, but it also probably involved a major ethical dilemma for Watkins, knowing she could potentially destroy an organisation employing 20,000 people.

Activity

Do you think Sherron Watkins did the right thing in whistleblowing – why?

6.6 Lessons Learnt from Enron

So, did the Enron scandal make organisations more transparent and ethical in their activities?

It certainly increased the visibility of the activities of large companies to a wide range of interested stakeholders and put renewed emphasis on the need for effective corporate governance structures. Overall, it demonstrated the risks and possible costs of unethical and illegal behaviour, even to large, powerful organisations. Organisations cannot become complacent in how they run their business.

For the insurance industry and loss adjusting businesses, key factors are governance structures, good visible ethical practice, and maintaining and where possible exceeding good professional conduct. They should recognise the importance of and benefits of supporting whistleblowing activity and the opportunity for the company to use it as a positive energy for self-improvement.

If the risks of whistleblowing are high, openness and transparency in an organisation cannot be supported.

Activity

What are the positive aspects of whistleblowing to the insurance industry?

6.7 Supporting Whistleblowers

Whilst whistleblowing can severely damage or even destroy a company, it could be argued that it should be part of a process that can support and sustain organisational health, particularly in the case of internal whistleblowing.

Supporting or encouraging whistleblowers within an organisation demands an organisational culture, leadership approach and management style that is open, participative and allows and even encourages a level of constructive criticism (e.g. from employees) rather than a secretive or top-down/authoritarian approach. Such a culture can also be supported by formal processes that are put in place to allow individuals to raise and discuss concerns without fear of reprisals or negative response, and that are used for constructive feedback, e.g. organisations with an open, self-critical perspective such as Facebook.

It could also be argued that good internal communication and management can reduce the need for or risk of whistleblowing. Whistleblowing should not be seen as just a safety valve for dissatisfaction, but as an opportunity for positive input and participation in the development of the company.

In a modern environment of increased scrutiny and speed of communication, it is increasingly important that loss adjusting firms are seen to be trustworthy and to conduct their business ethically. They must be able to demonstrate this clearly in practice, both internally and to key external stakeholders.

Activity

Talk to more senior members of staff and find out what the whistleblowing procedure is in your firm.

6.8 Key Points to Remember

- Whistleblowing can be aimed at internal and external stakeholders.
- It is relevant to all organisations, large and small.
- In extreme cases, it can destroy companies, but it could also be seen as a constructive internal process or pressure for improvement or development.
- The Enron scandal was one of a number of scandals over recent years, but it was a catalyst for change in the way corporate governance, ethics and CSR were viewed throughout the world.
- The Enron corporation appeared to have developed a culture of deception.
- Whistleblowers are often motivated by a strong sense of values or a perceived need for improvement, but they can face high risks.

Summary of ethics

- Ethics concerns standards, ethical norms and acceptable behaviour.
- It can be complex, as ethical standards and norms are not universal. Most organisations face the challenge of ethical diversity.
- Understanding stakeholders and stakeholder relationships is central to ethical business practice.
- Organisations often have to make ethical decisions or judgements about what is the fair or right thing to do. These can be complex as different parties (or stakeholders) involved in or affected by a decision may have differing views about what is fair or not. This is often known as stakeholder conflict. Therefore, it may be difficult for an organisation to make decisions that are seen to be fair and appropriate to all parties concerned.

- Ethics and CSR can have a major impact on the image and reputation of an organisation. Negative perceptions can damage the financial and economic performance of an organisation.
- The ethical health of an organisation can be supported by an open and transparent management approach that can encourage constructive challenge and development.