JUNE 2024

RISK MONITOR

Insights to help reduce risk for mid- to large-size businesses

INTRODUCTION

Things that never happened before happen all the time.[1]

In the world we're operating in, the only constant is change. From GenAI to significant geopolitical and supply chain shifts, climate change, biomedical breakthroughs, cyberattacks – and so much more – the world is fundamentally different than it was a decade ago. And we know the next decade will be fundamentally different than today.

Change necessitates innovation. That's why it's such an exciting time at The Hartford and across our Commercial Lines businesses. Our robust technology investments, product depth and breadth, and collaborative culture all have a common focus: elevating the agent, broker, and customer experience.

In that spirit, we're excited to share the second edition of The Hartford's Risk Monitor Report. Born in response to feedback received from distribution partners and customers on top risk concerns, Risk Monitor provides deep insight into some of the most pressing topics in insurance, including cyber incident response, business interruption, legal system abuse, property valuations, AI and the labor market, and autonomous robots. The articles come directly from talented leaders at The Hartford, showcasing our specialization across products and industries.

The Hartford celebrated its 214th anniversary on May 10, which is remarkable considering less than one percent of companies in the United States make it to 100 years old, let alone 200. Innovation, adaptability, and customer centricity got us here – and they're the same things that will carry us into the future.

Thanks for your continued trust in The Hartford,

Mo

Mo Tooker
Head of Commercial Lines and Enterprise Sales & Distribution

[1] Scott D. Sagan, The Limits of Safety, 1993, Princeton University Press

WHAT OUR POLICYHOLDERS SAY*

Our Middle & Large Commercial policyholders identified the following areas as top concerns they're focused on while consulting with their agent/broker and insurer.

ECONOMIC TRENDS

- Labor market
- Nuclear verdicts
- Social inflation
- Property value

SUPPLY CHAIN ISSUES

- Business interruption
- Jobs being delayed
- Contingency plans set in place

INCREASED SOPHISTICATION IN TECHNOLOGY

- Cyber attacks and progression of tactics
- Artificial intelligence integrating into workplace
- Automation decreasing the skills of workers
- Social engineering
- Steps to take after a loss

* The Hartford surveyed their Middle & Large Commercial policyholders who are business insurance decision makers. Study was conducted from November 7 through November 20, 2023 in order to identify top risk concerns, emerging trends and topics of interest.

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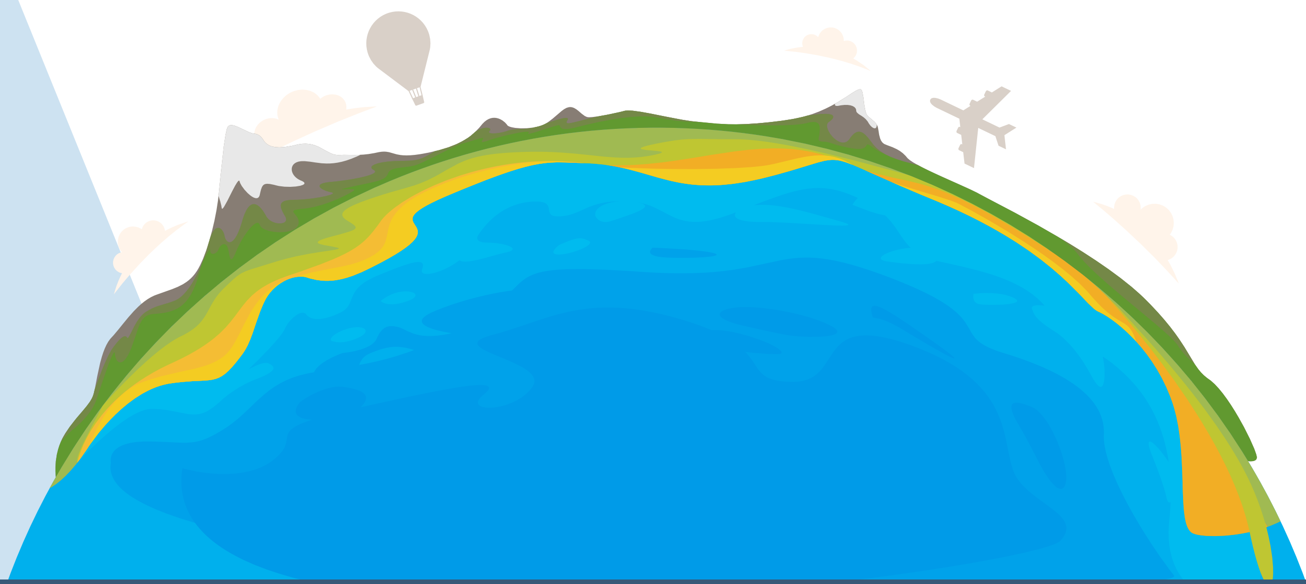


AI AND LABOR: WHAT 250 YEARS OF HISTORY TELLS US

Shailesh Kumar
Head of The Hartford's Global Insights Center

The rise of artificial intelligence (AI) is met with both optimism and pessimism. On the latter, some worry that AI could upend labor demand and the need for human capital going forward. There are many unanswered questions when it comes to the future with AI: What happens with the next generation of workers? The impact on society? The social contract between citizens and their government? What about the future of the economy itself? Those are some concerns, but there are positives to look toward. At The Hartford's Global Insights Center, we believe that AI will ultimately augment labor and further enhance productivity over the next 30 plus years.

> We tracked over 250 years of productivity rates of change, analyzing the effects on the labor market.

How did we come to this belief? To understand this view, past technological cycles need to be considered and their impact on productivity, layered with the expected outlook for U.S. labor and demographics. To help paint this story, we tracked over 250 years of productivity rates of change, analyzing the effects on the labor market per each.

PRODUCTIVITY AS A GAUGE FOR ECONOMIC GAINS

Productivity refers to the amount of output divided by the collective number of hours for that output, which we observed year over year. For example, if it takes one hour to make a sheet of metal, then the next year it takes just 30 minutes. Productivity (output per hour) goes from one sheet to two sheets, or an increase of 100%. During this time, we've enhanced productivity.

1700s to 1900s

As many are hesitant to address AI in fear of what it means for the labor market, we can look back in history to where new adjustments in productivity have been good for the labor force and overall global economy.

In our study, The Hartford's Global Insights Center began tracking productivity in the United Kingdom (the dominant global economy in the 1700s-early 1900s) then transitioned productivity in the United States from the mid-1950s onwards. We noted five specific intervals over almost 250 years where productivity increased for a sustained period of 20 to 40 years, or approximately a generation.

1. **Early 1800s:** Colonialism gathered during this time and the U.K. likely accrued increases in output from the nations it took over.

2. **Mid 1800s:** The Industrial Revolution takes place and new technologies (mainly the steam engine) improved efficiencies and output. It ended around 1880 when the gains from the industrial revolution were fully integrated into the economy.

3. **Early 1900s:** Before World War I, improvements in shipping, a drop in tariffs and the advent of trade-relations led to an increase in global interconnectedness. This ended around the time of the Great Depression.

4. **1950s:** After the end of World War II, military/industrial output grew due to investments in technologies and the Marshal Plan helping Europe's economy, while spending on the U.S.'s highway program helped overall output effectively reducing transit times.

This era ended in the 1970s likely due to the decline in U.S. manufacturing.

5. **1990s:** The advancement and adoption of the internet increased productivity but began to wane after the financial crisis in 2008. It went on to create more jobs in industries that we could not even fathom in the 1990s.

The 21st Century: Innovation of AI

In 2024, we are on the cusp of a potential sixth generation-long increase in productivity, the integration of AI into modern society. Like the previous five noted, all occurred largely due to the introduction of a new technology which appeared worrisome to many at first.

> The U.S. has been running an economy with more open positions than available workers, making labor a scarce resource.

Similarly, AI, at a minimum, has the potential to increase productivity. Of course, productivity can replace labor, making certain jobs obsolete, but new technologies like AI can spur industries we cannot even imagine today. To emphasize this point, let's remember that the past technological cycles took 20 to 40 years to play out entirely. Hence market conditions have ample time to conform allowing labor to find a way and not be upended immediately.

CURRENT LABOR MARKET STATUS

It's also important to consider that we have a labor shortage in America. According to the numbers, we are entering a cycle where it will be difficult to backfill jobs as workers retire, and even more difficult to expand the national labor headcount. The U.S. has been running an economy with more open positions than available workers, making labor a scarce resource. Upcoming demographic shifts may further exacerbate hiring challenges.

Because scarce resources are rarely discarded, we expect AI will be used to boost labor rather than replace it, given our structural labor shortages. Some individual skills and job duties may shift, but this should be the exception rather than the rule.

THE FIGHT FOR AI OWNERSHIP

On a more macro basis, the question also comes down to which nations can harness and dominate the AI landscape. Like the industrial revolution, the nations that dominated shipping and trade in the early 1900s, the countries that pivoted post World War II to launch an investment cycle, or the operators that captured the gains from the internet era early, the rise of AI will be dominated by the nations that can truly leverage its potential.

Based off this, we can conclude that AI "ownership" will be a dominating facet of geopolitics in the decades ahead. This includes:

- Semiconductors development
- Growth in technological capabilities
- Capital investments
- Access to and the development of necessary power generation
- Imposition of tariffs
- Trade restrictions on nations seen as adversaries in this space
- A fight for labor (i.e., potential changes to immigration laws)

No nation can afford to fall behind, because if they do, they will likely not be able to bend the benefits of AI to support their economies and generate prosperity in the face of labor shortages. Today, we are already seeing the early stages of this ownership struggle through restrictions on the trade of technological hardware, which is integral to the development of AI.

Artificial intelligence deserves more hope than fear. AI, like past technological cycles, can lead to a generation-long increase in productivity. Granted, productivity can rise absent human capital. However, we need to remember the labor shortage our country is currently dealing with and how AI can support the future labor dynamics. Similar to past cycles, we believe labor conditions will comport and evolve over that generation to work alongside AI and vice versa. The critical question comes down to which nation or nations will control AI to benefit their labor and productivity needs. That, in turn, reveals to us the geopolitical fault lines that have already emerged and will only widen over the years to come.

Steve Deane
Chief Claims Officer

LEGAL SYSTEM ABUSE AFFECTS LIABILITY EXPOSURES FOR BUSINESSES

Ads for lawyers seem to show up everywhere these days, from billboards to websites, social feeds to TVs. Their omnipresence is part of a changing business model.

That's because plaintiffs' lawyers now have far more resources to devote to trying to convince potential clients they can win big payouts. Hedge funds and other investors help drive this shift. The investors fund litigation for the right to keep a sizable portion of any court winnings that plaintiffs eventually may be awarded.

Third party investors spent $22 billion last year, mostly in the U.S., funding lawsuits with which they were not legally involved.[1] To them, the lawsuits were just an investment opportunity. Much of the money they invested went to court fees, expert witnesses, and other litigation costs, and helped fuel $1.4 billion in ads to lure litigants.[2] Remarkably, despite the size and the impact of this investment industry, it is essentially unregulated.

When businesses have to pay large legal judgments, it can force them to raise prices as a way to recoup their losses.

PLAYING ON JURIES' SYMPATHIES

The barrage of ads does more than help lawyers find clients. The ads also subtly influence jury pools. When potential jurors regularly see and hear about huge verdicts, the idea that massive payouts happen frequently becomes normalized.

The pervasive impacts of advertising are mixing with another changing social sentiment: a prolonged, nationwide rise in anti-corporate feelings.[3] The American public in particular holds businesses in lower esteem than in the past. This shift in attitude has made it easier for lawyers to sway already-biased jurors against businesses. Instead of looking to ensure that an injured claimant is properly compensated for an injury, plaintiffs' lawyers position verdicts as a way to *send a message* to corporations so that something bad won't happen to others in the future.

By reinforcing the perception that huge verdicts are common and that businesses must be punished, plaintiffs' attorneys have been successful at convincing jurors to be more receptive to awarding unjustifiably large awards.

THE COST OF BIG VERDICTS

In the legal world, $10 million is a milestone. Verdicts of $10 million or more are commonly called "nuclear verdicts."[4] The name reflects the fact that the dollar amount is exceedingly high, often much higher than the amount that would seemingly be justified based on the injuries sustained and the facts of a case. They're happening more often. An analysis by The U.S. Chamber of Commerce found that the number of nuclear verdicts increased 27.5 percent from 2010 to 2019.[5]

The fallout from nuclear verdicts goes beyond the courtroom. When businesses have to pay large legal judgments, it can force them to raise prices as a way to recoup their losses. This phenomenon is called "social inflation" because price increases are not based on underlying economics, but on the way that social sentiment influences verdicts and judgments, which in turn drives up costs for everyone.

Keep in mind that verdicts and judgments are a big piece of the economy. All told, the U.S. tort system cost an estimated $443 billion in 2020,[6] with a sizable portion coming from nuclear verdicts. That equates to around $3,600 a year per American household.[7]

COSTLY FOR PLAINTIFFS

The costs may be high, considering who really benefits. While lawyers, their ads, and outside investors *claim* plaintiffs win big, the reality is different. Plaintiffs typically receive just a portion of the awards. Meanwhile, investors and others keep almost half of any judgments in cases they win.[8] In some cases, investors have earned up to a 30 percent return on their investment.[9] That profit margin is three times the average stock market return.[10]

LEGAL SYSTEM ABUSE (continued)

At the end of the day, injured parties can be left with less money – sometimes substantially less – than if they had settled their claim and had their injuries paid for directly without attorneys or funders involved.

REFORMING THE SYSTEM

When someone is responsible for an accident, the legal system aims to make those injured in the accident whole for their damages and injuries. The system does not aim to be a profit-making opportunity for investors, which is exactly what third-party litigation funding does. When we allow verdicts to be treated like a commodity market, it has a bad ripple effect on society and the economy.

Legal system abuse reform can eliminate some of the excessive costs these lawsuits generate. The Hartford supports and works closely with several organizations that are calling for greater transparency and accuracy in legal advertising. We're also advocating for increased transparency in third-party litigation funding, as we recently did in Indiana, where legislation passed that will limit foreign investments in lawsuits.

Legal system abuse reform isn't merely an insurance issue. It's a broader societal issue that desperately needs reform. Especially since we all end up paying for the increase in costs.

LEGAL SYSTEM ABUSE COSTS ARE HIGH

Legal System Abuse increases the cost of the tort system, where people sue for injuries and damages. Tort costs were **$443 billion** a year in 2020, which equates to **$3,600 per American household**.[11]

That's the same amount as:

5 months
of car payments[12]

or

7+ months
of groceries[13]

or

2½ months
of mortgage payments[14]

[1] "Revisiting the Impact of Litigation Finance on US P&C Insurers," Evercore ISI, March 26, 2024.

[2] "Study: Trial Lawyers Spent $1.4 Billion on Advertising in 2021," American Tort Reform Association, Feb. 22, 2022.

[3] "Historically Low Faith in American Institution Continues," Gallup, Jul. 6, 2023.

[4] "Social Inflation," National Association of Insurance Commissioners, Aug. 23, 2023.

[5] "Nuclear Verdicts: Trends, Causes, and Solutions," U.S. Chamber of Commerce Institute of Legal Reform, Nov. 22, 2022.

[6] "Tort Costs in America: An Empirical Analysis of Costs and Compensation of the U.S. Tort System," U.S. Chamber of Commerce Institute for Legal Reform, Nov. 22, 2022.

[7] Ibid.

[8] "Tort Costs in America: An Empirical Analysis of Costs and Compensation of the U.S. Tort System," U.S. Chamber of Commerce Institute for Legal Reform, Nov. 22, 2022.

[9] "Considering Paths to Disclosure of Third Party Litigation Financing," Reuters, Feb. 22, 2023.

[10] "What is the Average Stock Market Return," Nerd Wallet, Mar 5, 2024.

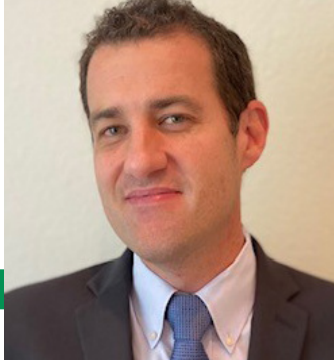
[11] Tort Costs in America: An Empirical Analysis of Costs and Compensation of the U.S. Tort System," U.S. Chamber of Commerce Institute of Legal Reform, Nov. 22, 2022.

[12] Based on a monthly payment of $726. "The Average Car Payments for New and Used Cars in 2024," Adam Palasciano, NASDAQ, January 21, 2024.

[13] Based on an annual food budget of $5,703. "Consumer Expenditures – 2022," Bureau of Labor Statistics, September 2023.

[14] Based on an average monthly mortgage payment of $1,427. "Average monthly mortgage payment," Andrew Dehan, Bankrate, January 2024.

NAVIGATING THE HIGH STAKES OF PROPERTY VALUATIONS: WHY ACCURACY CAN'T BE OVERLOOKED



Ryne Carney
Head of Property and Marine Product

Caleb Woodby
Chief Property & Marine Underwriting Officer

The number of risks facing business owners continues to increase. From a catastrophic natural disaster to a ransomware attack to an essential piece of equipment breaking down, business owners need to be sure they are purchasing adequate insurance to stay ahead of any risk exposures they might face.

Accurate property valuations are an essential component of any property insurance program. Yet, companies often unknowingly underreport the value of their property assets, potentially leaving them underinsured.

To support accurate valuation, it's critical for a business owner to provide as complete and in-depth of information about their property as possible. This includes the size, age and use of the property, as well as any specific or unique construction details.

THE ROLE OF PROPERTY VALUATIONS IN COMMERCIAL PROPERTY INSURANCE COVERAGE

Savvy business owners understand the importance of regularly updating valuations to ensure they reflect market changes. Given that labor and material costs will fluctuate, it's a best practice for property valuations to be revisited minimally on an annual basis. In the past, annual valuations changed about 2%-3% each year, but recently those changes have been as high as 5%-8%.

For instance, companies often underestimate the actual replacement cost of equipment. That could lead to a business not being insured for the full price of replacing an essential piece of equipment and having to pay the difference out of its own pocket.

Reconstruction costs have been impacted by recent inflationary pressures, which makes it even more critical for companies to provide their insurer with the actual cost to replace property or equipment, not the book value. There is a big discrepancy between book value, which is what the company said it cost to acquire the equipment or property, rather than the full replacement value.

CONSEQUENCES OF INACCURATE PROPERTY VALUATIONS

Underinsured business owners are likely putting their companies at financial risk. When a business doesn't have an adequate amount of property insurance, the business owner may be responsible to pay the remaining replacement costs when their insurance doesn't cover the entire claim. These costs can be devastating for a business.

Property owners need to consider the insurance to value (ITV) ratio when purchasing property insurance, which is the ratio of a property's insured value relative to what it would cost to replace that building. If you hear the phrase 100% insurance to value, it indicates that the insured limit on the policy should track in line with the actual cost to replace.

NAVIGATING THE HIGH STAKES OF PROPERTY VALUATIONS: WHY ACCURACY CAN'T BE OVERLOOKED (continued)

BEST PRACTICES FOR ACCURATE PROPERTY VALUATIONS

The more information and more detail an insurer has about the makeup of a property allows the building valuation assessment to become more granular and more accurate.

For instance, property owners should disclose any:

- Protective features, such as sprinkler systems.
- Permanently installed or attached equipment in the building.
- Specialty construction features or building components.
- Warehouses and the value of inventory sitting within them.

> Companies that fail to provide an accurate valuation of their property and assets put their business at risk for long-term financial consequences.

Companies should also consider one-time costs versus reoccurring costs during a potential loss. For instance, if an operation is down for several months, the company will need to relocate their operations. This means paying rent and electricity bills at an alternative site, while still paying the bills for its existing location and the cost of the repairs there. The company will have extra expenses to cover the temporary repairs while they are making permanent repairs to the facility.

Property owners should also let their insurers know of any seasonal inventory fluctuations. If there is a time of year when the company might have twice as many goods as they normally would have, then understanding peak values is crucial if there is a loss.

HOW A COMPANY'S PROPERTY VALUATION CAN IMPACT THEIR SUCCESS

Imagine two companies of similar make up – same industry, size and complexity of operations. Company 1 works closely with their insurance carrier on an annual basis to make sure their property valuation is accurate, and their coverage is comprehensive, avoiding potential gaps. Company 2 does not, and thus is not valued accurately. They each experience a similar catastrophic loss event, resulting in a total loss.

Here are the impacts:

Company 1: *Accurate property valuation, comprehensive business continuity planning and organized regarding schedules of equipment and inventory.*

- Appropriate limits of insurance purchased to ensure they will get the needed funds to help restore operations to prior capacity levels.
- Likely to experience a timely claim assessment of damaged structures, equipment and inventory.
- Likely better positioned to maintain business continuity following the loss, utilizing key suppliers to help mitigate business interruption.
- Likely to see improved restoration time due to being organized with well-maintained facilities, proper risk valuation, up-to-date equipment details and business continuity plan to help minimize long term interruption of business for customers.

Company 2: *Inaccurate property valuation and lack of attention to risk mitigation and business continuity planning.*

- With no plan in place, it takes longer to get back on track after a loss, meaning more downtime. Plus, if there's trouble getting products to customers, they might lose market share, which can be hard to get back.
- If full replacement valuation is disputed with the insurance company pre-loss, a co-participation or margin clause may be part of the insurance policy resulting in the insured being financially responsible for a portion of the loss.
- If the insurance policy is providing coverage on an Actual Cash Value (ACV) basis, the claim settlement will reflect the value of property on a depreciated basis rather than the actual replacement cost.
- May find it harder to bounce back from a large loss, causing long-term issues for the business.

ACCURATE VALUATIONS ARE KEY TO EFFECTIVELY MANAGING RISK

Companies that fail to provide an accurate valuation of their property and assets put their business at risk for long-term financial consequences. With inflationary pressures persisting and increased global risks, it's essential that owners partner with insurers to reassess their property valuation each year as part of their overall risk management plan.

UNCOVERING THE LIFECYCLE OF A ROBUST CYBER INCIDENT RESPONSE PLAN

Tony Dolce
Head of Professional Liability, Cyber and Tech E&O

At the current rate of growth, damage from cyberattacks will amount to about $10.5 trillion annually by 2025 – a 300% increase from 2015 levels.[1] These numbers are enough to give any business pause. With more regulations being implemented from the government and sophisticated attacks becoming more frequent, it's critical that companies are aware of cybersecurity best practices.

> At the current rate of growth, damage from cyberattacks will amount to about $10.5 trillion annually by 2025 – a 300% increase from 2015 levels.[1]

Once the realization comes to light that a company has fallen victim to a cyberattack, it is time for them to execute on an incident response plan (IRP) which is an outlined approach to dealing with a cyber threat head-on. During an incident, a company is required to make several decisions quickly and in a coordinated manner. It is not the time to come up with an IRP on the spot. If a plan is not in place and familiarized by leadership, the company can end up overlooking many elements during the attack, resulting in more resources spent to remediate the incident.

A robust IRP will include many vendors and services that are professionals in their respective areas and assist with remediation and recovery efforts. These groups all fit in within the lifecycle of the plan, from preparing for a cyberattack, identifying the incident, containing and mitigating the damage, and recovering the operations.

CRAFTING AN IRP

A company can easily access multiple resources to build out an IRP specific to their organization. A company's cyber insurance carrier should play a critical part in the planning process and tapping into their resources should be a main priority. Whether it's pulling an off-the-shelf incident response plan template and customizing it to their organization's needs or going direct to a third-party cyber firm to draft a plan, an IRP is a necessary instrument for businesses of all sizes.

Standard considerations should be included within the IRP, like a list of key people needed during a crisis, their contact information and clarity in role and responsibilities during a cyberattack. The plan should be updated periodically because an outdated IRP will not be helpful during a crisis. An IRP should also be kept as a hard copy, in addition to a digital one, in case computer systems are inaccessible.

THE QUARTERBACK OF REMEDIATION

Too often, companies rush to their IT teams as the sole first responders to a cyberattack. While such a reaction is understandable, businesses might be losing out on critical services that a cyber insurance provider can leverage in those situations.

Immediately upon receipt of notice from an insured that there is a cyber incident or attack ongoing, the carrier will engage an incident response coach or cyber attorney to work with the company. An attorney can be seen as the quarterback of the response team. Establishing privilege in communications up front will allow for the attorney to give their client detailed instructions on how to best respond to the cyber incident. Speed of response is critical, and companies could be wasting valuable time that could negatively impact their ability to recover as quickly as they could have.

UNCOVERING THE LIFECYCLE OF A ROBUST CYBER INCIDENT RESPONSE PLAN (continued)

THE SUPPORTING TEAM

The attorney will assist in engaging additional resources and services to help build out a remediation strategy for the company, making sure each step along the way is covered by a service provider who has deep breach response expertise.

The carrier works very closely with the following vendors throughout the course of the claim, to make sure the insured is doing everything they need to respond and investigate the incident and restore them to their pre-incident state.

Computer Forensics and Data Restoration

Computer forensics are professionals who identify the source of the cyberattack and the scope, as well as impact of the breach. These experts can help companies determine the perpetrators and pinpoint specific directions for remediation. Understanding the threat vector can also help companies fortify their cyber defenses in the future.

Data restoration vendors are also key players who help determine how the lost or corrupted data can be revived. Their efforts may allow a company to operate and help get back to the functionality they had prior to the attack.

Notification Services and Call Centers

Incident notification laws dictate that companies need to notify specific parties about an incident usually within a short amount of time. These laws vary state by state and are ever evolving. Whether the parties are customers or business partners whose data might be compromised, they may be required to be notified in a required time frame. Lack of a proper response to an incident can lead to the company having penalties imposed on it or exposing it to civil liability. Notification vendors can identify these notification needs and take care of the efforts quickly and at scale.

Threat Actor Negotiators

During a ransomware attack, a negotiation service may be needed to work directly with the cyber threat actor. Working with the attorney will help the victim of the attack navigate the various laws and regulations in this area. They will negotiate and facilitate a payment if necessary for that extortion so the company's systems can get back up and running so that operations can continue.

Crisis Communications

Crisis management is often an overlooked step when remediating a cyberattack. Companies should consider involving a crisis management public relations firm that is part of their cyber carrier's vendor panel. These firms can help protect the reputation and brand that takes years of goodwill to burnish. A company will want to get in front of the crisis and deliver an accurate and coherent message to both internal and external stakeholders.

NO PLAN IS COMPLETE WITHOUT A TEST

IRPs should be tested and not just talked about. It isn't until a company is running a simulation that they might realize a piece of their plan isn't clear or is missing entirely. To test an IRP, its best for a company to do the following:

- Identify certain scenarios that are unique to the company to verify whether they are addressed and protected by the plan that is put in place. Go a step further and conduct tests on situations that may be relevant to the industry or type of business operation.
- Assess policies and procedures with the staff to make sure they are still the right approach given changes could occur within the organization since the last test.
- Scan and identify any weaknesses within the security system and address any gaps.
- To keep leadership up to date, conduct a hands-on tabletop exercise or a simulation test, with the key stakeholders so they know how to take action during a cyberattack incident.

Companies are not expected to know all these steps upfront, so getting to know their cyber carrier's service providers will help them to understand who they need to engage in the event of a cyberattack. Company leaders should educate themselves to the appropriate level and scope of cyber insurance, allowing them to benefit from the services that an experienced cyber claims team can afford. An ounce of prevention is worth a pound of cure.

[1] McKinsey & Company – New survey reveals $2 trillion market opportunity for cybersecurity technology and service providers

THE RISE AND RISKS OF AUTONOMOUS ROBOTS IN THE WORKPLACE

Andrew Zarkowsky
Head of Artificial Intelligence Underwriting

The introduction of autonomous robots and artificial intelligence (AI) has the power to change the way businesses operate. For example, warehouses might reduce the risk of workplace injuries by having robots complete higher hazard tasks. These robots can take on tasks like carrying heavy materials or entering workspaces that would require humans to wear protective gear to guard against noise or toxic chemicals. However, as technology continues to rapidly evolve, it is important to understand both the risks and the benefits of introducing autonomous robots into your operations.

THE RISE OF AUTONOMOUS ROBOTS

Autonomous robots are intelligent machines that can perform tasks such as finding and picking items in a distribution center or sanding fiberglass at a construction site. But to do the job right, robots need sensors and visual data to make decisions and operate autonomously and sometimes they need human intervention to keep them on track.

Despite these limitations, robots give workers the ability to delegate mundane and hazardous tasks to machines, allowing humans to focus on the more engaging and valuable parts of their job. In 2024, nearly 21% of warehouses use some form of robotics, up from 15% in 2018.[1]

Autonomous robots are being used across a variety of industries, including:

- Logistics: Robots can transport orders across warehouses and shipping facilities.
- E-commerce: Robots can support order fulfillment, returns handling, raw materials transport and inventory management.
- Manufacturing: Robots outfitted with appropriate gear can assist in the production process.
- Data Centers: Autonomous robots can be used to transport material that is sensitive or an essential part of operations.
- Healthcare: Autonomous robots can move supplies and medicine, as well as support cleaning and sanitizing routines.
- Biotech: Robots can perform repetitive monitoring tasks or aid with waste removal from the production line.

A robot's biggest asset is its lack of human limitations. Robots are not constrained by heat or chemicals, allowing them to perform tasks that are potentially dangerous to humans. For example, robots with sensors can venture into high-hazard areas to check for radioactivity or diminished air quality.

Companies are also using robots for overnight security. Robots can drive around the parking lot of a vacant building, for instance, to show a presence of security, record events and hopefully be able to prevent a bad actor from causing an issue.

ASSESS WORK ZONES BEFORE USING AUTONOMOUS ROBOTS

Robots, however, are not infallible. In addition to potentially breaking down, autonomous robots can perform the wrong action if not programmed correctly. For example, robots have been known to go off course and end up in the wrong section of a warehouse or get stuck on a loading dock. And if the robots are interacting with humans, the risks increase.

THE RISE AND RISKS OF AUTONOMOUS ROBOTS IN THE WORKPLACE (continued)

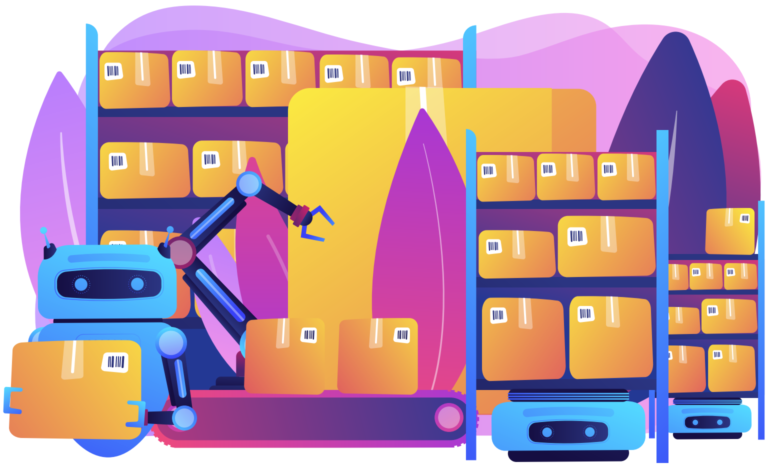
Companies considering the use of robots should assess the work environment and every individual task a robot would complete. A controlled environment, such as a warehouse, entails less risk than a robot functioning outside on a public road.

> Companies considering the use of robots should assess the work environment and every individual task a robot would complete.

When using autonomous robots, a company should evaluate its risk based on the environment and concurrently evaluate insurance coverage – particularly general liability, workers' compensation, property, professional liability (also called Technology Errors & Omissions or Tech E&O) and cyber liability.

There is a risk correlation to the environment and the end use. It's important that whoever uses the robot understands their liability and the availability of appropriate insurance coverage.

Users should spend time thinking about risk transfer and understanding the contract wording in the SOW (Statement of Work). Expectations and warranties should be clearly defined, as well as how the insurance policy will provide or exclude coverage. If something goes wrong, the insurer will evaluate whether it was caused by the manufacturer's design or if the company using the robots designed the constraints incorrectly.



REDUCE YOUR RISK WITH ROBOTS IN THE WORKPLACE

First, do not let risk deter you. Waiting to use robots can be its own risk, hindering a company's productivity and innovation. Companies should start somewhere, even if it is exploratory. The ramp up time from not having robotics in the workplace to having them is significant. It might take years to use the robot efficiently.

With that insight, here are some steps to consider:

- Start small: Deploy robots in low hazard and controlled environments to minimize risk and maximize learnings. Ensure sensors detect what is needed and partner the robot with a human to refine your process before it is deployed on its own.
- Contain the environment: Work in well controlled and mapped locations. Ultimately, if you want your robot to support humans in a warehouse, train it first in a contained space with simple directions. As it achieves goals, level up its duties.
- Educate on misuse of robots: Risks emerge when a robot isn't used the way it is designed. To reduce potential problems, educate human counterparts on correct usage. For example, if a robot is designed to move at 2 to 3 mph, but a user forces it to 4 or 5 mph, that could incur a major risk.

When initiating a robot program, consider hiring someone internally to oversee the initiative or bring on a consultant who deeply understands what's involved. It will take a true combination of understanding your business and process while also understanding AI and robotics. Just having one or the other won't be sufficient.

[1] Industrial Robots – 2023, Interact Analysis, accessed January 2024.

INSURING SUPPLY CHAIN RISK: THE ART OF BUSINESS INTERRUPTION INSURANCE

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Whether it's a natural disaster, a transportation issue or a supplier failure, it's crucial for businesses to have a robust plan to protect against unexpected circumstances that could lead to business disruptions and create financial risk.

> Companies go through extraordinary efforts to expand globally, yet all too often they fall short on insurance.

There are a variety of steps a business can take to help safeguard revenue and plan for continuous operations in the face of disruption. For savvy players, it's important to understand and map out the unique supply chain – from components to raw materials – for each stage of operation and to understand suppliers and dependencies.

Although global expansion can create substantial economic opportunity, it's not without its risks. Companies that operate globally must have backup plans and inventory in case there is an interruption.

Knowing your operation, processes and having a contingency plan are critical. All too often companies have a piecemeal perspective of their risk as opposed to understanding the complex interplay between the operations and the balance sheet.

PROTECT AGAINST SUPPLY CHAIN INSTABILITY

The global supply chain continues to face instability, which places additional risk on businesses operating on an international scale.

During COVID, vulnerabilities within 'just-in-time' manufacturing came to light, highlighting society's dependence on reliable – yet expensive – air, land, sea and freight shipping. Long supply chains that require the movement of materials and components across the globe leave companies vulnerable, especially because trade restrictions can fluctuate.

Russia's invasion of Ukraine is an example of this. At first, European auto manufacturers virtually shut down because many of the wire harnessing systems for European-manufactured cars were made in Ukraine. As a single good, it's not a high value-added product, but without access to wire harnessing systems, many European manufacturing plants came to a halt.

INSURING SUPPLY CHAIN RISK: THE ART OF BUSINESS INTERRUPTION INSURANCE (continued)

As a result, companies today are tasked with shortening extended supply chains to reduce vulnerabilities. A way to do that is to find clusters of countries where low-cost manufacturing can happen within a tighter radius.

The process can be challenging because as this shift is happening, countries are scrambling to bring ecosystems together. The growing demand in Vietnam, Indonesia, the Philippines, Cambodia, Mexico and Canada is one to note.

CREATE MULTINATIONAL RESILIENCE

Dwight D Eisenhower said it best: "Plans are worthless, but planning is everything." For a company with a multi-country supply chain, it's the thorough understanding of your processes and dependencies and having backup plans along the way – that could help reduce risk.

Here are key considerations to defend against business interruption:

- **Political risks:** No one could have predicted many of the world events that have happened in the last 24 months. Performing desktop exercises for worst-case scenarios is a prudent part of an operator's playbook. If a business is considering expanding into a politically turbulent region, it is encouraged to research the business approach dealings, opportunities and challenges of companies already operating in that particular region.
- **Cyber risks:** Companies can and should work with internal IT teams and third-party resources to have an incident response plan in place for the possibility of a cyberattack. Given the continued risk of cyber threats, the protocol around cyber protection should be explicit and in the hands of people who are collecting information and manipulating data for the company.
- **Regulatory risks:** A global operator needs to follow the laws of every country it operates in – a formidable task for any organization. Three parties are required to put together an effective multinational insurance program: an experienced broker, a trusted advisor and a global insurer.
- **Financial and tax risks:** For operators to understand their financial risk, they must know the values of their properties, including buildings as well as replacement costs. Global businesses operating in different countries must also map out country-specific tax requirements and environmental regulations. Understanding the rules, the norms and the practice in an individual country is critical.

ENSURE THERE IS ADEQUATE COVERAGE

Companies go through extraordinary efforts to expand globally, yet all too often they fall short on insurance. The same rigor with which leadership runs a business should be applied to understanding your insurance program and how it interplays across various countries and geographies.

To that end, companies should be wary of buying insurance in individual countries. Global operations can benefit from an insurer who can take a comprehensive view of your business. A carrier must be able to offer a program structure that adequately addresses and responds to the active dynamic of your operations and the people and products in motion around the world. It is important to be certain that the insurance program can respond to a loss in the country where it occurs and in any other country that then experiences a negative financial impact because of that loss occurrence.

To do this, underwriters need to see a detailed plan that breaks down all the activities of each operation, from sourcing to packaging and distribution. This level of detail allows the insurer to perform an accurate forensic review of the operations and determine the potential extent of the loss as well as the payments that are necessary at each step of the process to make the company operational as quickly as possible following a loss event.

ADDITIONAL RESOURCES

Economic and Geopolitical Research
Large Property
Cyber Risk
Technology
Multinational
Product Information

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