



Case Study 4 Management Turbulence at ACR Retakaful Berhad

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Abstract: This case discusses the issues that arose during the change process in a Kuala Lumpur based Retakaful company, ACR Retakaful Berhad. The chain of catastrophic events in Asia during the years 2010 and 2011 had raised a huge number of claims against the company which went into financial difficulties. The company had no option but to change. A new CEO arrived and quickly took serious measures to rectify the situation and put the company on the right track in order to secure sustainability, growth and profitability. However, the change process was not running smoothly. Employees were not involved in the change and many chose to withdraw voluntarily. Subsequently, staff turnover reached the highest level ever known in its history. Instead of moving to a better state, the company's performance was getting worse with each passing day.

BACKGROUND

ACR Retakaful Berhad (ACRR) is the most capitalised Retakaful Company in the world with a capital of USD 300 million. Based in Kuala Lumpur, the company began operations in July 2008. The Company is a member of Asia Capital Reinsurance Group (ACRG), a Singapore reinsurance group established in 2006. Apart from ACRR, ACRG has three other operating entities in the Group i.e., Asia Capital Reinsurance Singapore (ACRS), Asia Capital Reinsurance Malaysia (ACRM) and ACR Retakaful MEA in Bahrain (ACRR MEA).

ACRR's sources of income are from two channels, that is, from its own business and from the Intra Group Transaction (IGT). Its own business means income directly secured by ACRR from their clients, takaful and insurance companies in South-east Asia and in the Indian subcontinent. The IGT includes the business written by other

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Figure 1. Reciprocal exchange of risk portfolio within ACR Group

entities within ACRG that is proportionally passed on to ACRR through reinsurance contracts. In other words, ACRR acts as reinsurer for ACRS. With this arrangement, ACRG cleverly accesses and utilises capital allocated across the group, so that it can maximise its premium income. From ACRR’s point of view, this arrangement diversifies its portfolio by being exposed to other territories in which it does not directly operate, such as in East Asia, Middle East and North Africa. From the risk management perspective, this situation is not an ideal one; in fact it puts the company in a bold, dangerous and vulnerable position when large losses occur. It creates accumulation of risks within the group. The diagram above shows how entities within the ACRG reciprocally exchange their risk portfolios through the IGT, where each entity receives risk portfolios from all other entities.

CHAIN OF DISASTERS

It was very unfortunate that the 2010-2011 period was jolted by a series of natural catastrophic events giving the insurance industry a hard time, unprecedented in its history. It first began with the Christchurch (New Zealand) earthquake in September 2010, followed by the Australian floods in December 2010; then a second Christchurch earthquake in February 2011, immediately followed by the Japan earthquake in March 2011, and lastly the Thai floods that started in September 2011. Water continued inundating the areas along Chao Phraya river stream, including Bangkok, for more than three months. The ACRS entity within the group, authorised to cover the Thailand insurance market, suffered severe financial loss from the domino effect of these disasters, especially due to the floods in Thailand. ACRR and other entities do not

directly write business from these affected countries as there is no takaful operator in these countries. However, they were hard hit through IGT transactions by the ACRS.

The total insured loss of the Thailand floods was estimated to reach a staggering USD 12 billion. Lloyd's of London, Munich Re and Swiss Re were the three reinsurers with the largest nominal loss amount from the Thai floods. At the same time, they were also the first three of the largest reinsurers in the world. The ACRG share in Thai loss was way below those three giants; however, the impact of the loss to its financial standing was much worse. This was simply because ACRG was a young group of companies; hence its financial reserves were relatively still very small. Furthermore, the ACRG portfolio was still concentrated in Asia. For those three reinsurers, the impact of the Thai floods could be absorbed easily by their huge reserves and diversified portfolio that was spread all over the world. Their huge payouts in Asia could be compensated by their lucrative businesses in Europe or America.

The flood losses threatened the financial standing of ACRG and this led to both S&P and AM Best downgrading ACRG's "A" rating into negative watch. This status had a negative impact on the company image since it indicated that the company's ability to meet its financial liability was weak.

Within the ACR Group, ACRS the largest entity was the worst affected by the floods. Therefore, rescuing ACRS from that collapse became the top priority for the group. Within a short period of time, in fact within a few months, the ACRS management succeeded in saving ACRS through two strategic actions: first, by having a Japanese investor (Marubeni Group) on board, with a significant shareholding of 22.5%; second, by arranging a strategic alliance with Berkshire Hathaway, a reinsurance company owned by the world's richest man, Warren Buffet. This allowed ACRS to proportionally pass liability on to that company.

ACRS had been saved from sinking. But, new investors meant new demands. The deals put further pressure on ACRS to reach even higher revenue targets than ever before. ACRS needed to find new revenue sources to reach the top line. Among the initiatives taken by the Group management was the transfer of all conventional businesses from territories currently handled by its younger sister ACRR and ACRR MEA, which left both of them to focus solely on the takaful business.

On one side, this Group decision made ACRR more Shariah compliant, since its portfolio was purified from conventional businesses. However, on the other hand, ACRR's playing-field suddenly shrank and made the company too big for too small a business potential. Their capital was simply too high for the market which was too small.

YOUR WORST NIGHTMARE BOSS

Under this new group direction, the Board of Directors of ACRR refused to reduce revenue budget and expected the management to continue recording decent growth and high return in equity (ROE). The ACRR management at that time found this to be mission impossible, since things were in conflict with each other. After such a big

loss, the company was supposed to review its risk appetite and tighten the underwriting strategy in order to improve the quality of risk portfolios, which would lead to a drop in income, at least temporarily. However, in reality, shareholders wanted higher revenues after reducing the market. It was impossible to reach top line without significant compromise in underwriting (risk selection and pricing standard), considered '*haram*' in the insurance industry.

Zaini Noor, a Malaysian, ACRR CEO at that time did not agree with this new direction and tried his best to negotiate with the Board to review their stance. Unfortunately, the Board stuck to its decision. Zaini refused to commit to the new direction and tendered his resignation shortly.

Four months later, Patrice Evra arrived as the new CEO with the major mission being to turn around the company, and to operate in the new direction with the still ambitious top line target and profitability to serve capital, despite the shrinking market. From his profile in www.linkedin.com, the Frenchman claimed to be a specialist in turning around a company and in re-engineering failing businesses. He has been moving from one company to another with relatively short tenures in each one.

Most of the employees pinned high hopes on the new CEO to turn around the company towards profitability. The company had been in a state of 'limbo' for a few months after the departure of the former CEO. This expectation seemed to be true when in the week prior to the CEO's arrival, all staff received an email from his personal assistant announcing that Patrice would like to have face-to-face sessions with each and every staff, one-by-one. A complete schedule was attached to the email. Every staff would have 30 minutes to an hour of an individual session with him. Most of the staff viewed this as a good opportunity for them to share their feelings and opinions in order to fix the company's current poor situation. Everyone was looking forward to the session.

Danial Ahmad, a 37-year old Indonesian, was Head of Underwriting at ACRR office in Kuala Lumpur, leading a team of nine staff consisting of senior underwriters, underwriters and assistant underwriters. He had joined the company a year ago with the mission of building a profitable portfolio and a strong underwriting team. When he had arrived in the company, the underwriting team had only four staff members. Danial had previously worked in Indonesia and in the Middle East.

Danial had his session on the afternoon of the first day for an hour. The first five minutes of introduction went smoothly since they already knew each other and had met once, about three years ago, at a business meeting in Bahrain. Patrice, at that time, was the CEO of a Dubai-based takaful operator, and Danial was a manager at a Bahrain-based Retakaful operator. The interaction after that meeting was not that intense, apart from the fact that they were connected in *linkedin.com*.

Unfortunately, the next fifty-five minutes of the session did not go as expected. It was basically a one-way session in which Patrice expressed negative views about the company, in general, and especially his disappointment on what he called as "very poor and bad attitude of employees" towards work. He said that his first task was to

fix that attitude defect by all means. Danial tried to interrupt with a query, asking for clarification, and attempted to explain or tried to give his opinion. Unfortunately, Patrice was reluctant to listen. Danial wondered how for someone who had just arrived two days ago, Patrice could have such strong negative perceptions, which was not all true and accurate. It was very obvious that Patrice relied on one-sided information and was not interested in verifying it or listening to both sides of the argument. He certainly had been framed and convinced by someone who must be aware of the company's problems, that everything in the company was a mess and that the staff was no more than a bunch of dumb people. The session turned into the worst meeting he had ever had. He walked out of Patrice's office hardly able to express his feelings, but it was certainly one of disappointment, uncertainty and confusion.

Next day, in their weekly department meeting, Danial queried each of his team members about their sessions with the new CEO. Sadly, each and every one shared a story similar to that of Danial's experience. Some had a very tough 30 minutes, since Patrice had even used harsh words and body language when expressing his disappointment or elaborating what he called as the 'bad' attitude of employees. Some felt they had been personally targeted by Patrice.

Andre Castello seemed to have the worst session among all his colleagues. He walked into Danial's office right after the weekly meeting and explained what had happened during his session with CEO. He believed that he was personally targeted by the CEO to get him to resign by accusing him of being a lazy, irresponsible underwriter and, only because he had tried to explain to Patrice that the current market situation was not that encouraging with the competition getting fierce. Patrice quickly came to the conclusion and told Andre that he was too pessimistic and laid-back and this would have a damaging effect in the business environment. Whatever explanation or clarification he attempted to give did not help at all. Andre felt that Patrice really wanted to get rid of him. He simply couldn't take that type of humiliation and was seriously considering quitting his job, with or without a job in some other place.

Andre, a 47-year-old Malaysian Indian, was an Engineering Senior Underwriter who was a first class specialist and very well respected for his expertise by his peers and industry. He was a civil engineer by training and profession, and had been working as a Construction Site Engineer for 8 years before joining the insurance industry. He had been on site during the construction of the Petronas Twin Towers, something that he was very proud of. He joined ACRR in 2011 and had 13 years of experience with the world's largest reinsurance company as an engineering underwriter in its Kuala Lumpur branch. Patrice's remarks to him during their session had upset him badly. A week after, he decided to tender his resignation despite the fact that he would be jobless. Luckily his wife had a stable job and could support the family.

SEEKING CLARIFICATION

After a gloomy department meeting and a sad discussion with Andre in his room, Danial found himself in a very uncomfortable situation since everything seemed to be

uncertain. As the head of department, he realised that he needed to take the initiative to deal with the situation. He then requested another session with Patrice to understand and clarify many things. He had hoped that with a greater understanding, he would be in a better position to decide what to do and how to manage his team during that turbulence.

As expected, again the session was a one-way traffic – Patrice did the talking, Danial the listening. Patrice once again expressed strong disappointment on the staff's poor attitude towards work, which he considered as "unprofessional and unacceptable", and which also entailed a lot of "mess" in operations, such as data entry backlog and unallocated receipts, where money had been received in the bank account but couldn't be linked to an individual business. He told Danial that he would take very tough measures to rectify the situation and restore discipline. Danial felt that this statement was exaggerated

To be fair, these are common problems in the takaful industry as most takaful operators are young or start-up companies in the developing countries with an unstable administration and database systems. The administration of their Retakaful partners also shared similar problems. Most of the takaful operators are not capable of recording their Retakaful transactions properly and dispatching the required documentation to their Retakaful operators in an orderly manner.

Retakaful operators do recognise this limitation and have taken initiatives to train their takaful operator partners in Retakaful accounting and administration. Internal aspects also contributed to the backlog in the company, especially as the pressure to reach ambitious targets had shifted the focus and energy to marketing activities and allocated fewer resources to administration. ACRR is, by the way, also a start-up company, with very limited experience and a rather weak and unstable database system.

Danial tried to raise these facts carefully, but Patrice's response was, as expected, a reluctance to hear. He accused Danial of being defensive. Danial realised that there was no point in arguing at that stage and decided to focus on his initial objective of requesting for the meeting, that is, acquiring as much information as possible and trying to figure out of what he wanted. Nonetheless, a good thing about that meeting was that Danial gained crucial understanding about the direction and strategy of the company in going forward, which is de-risking and downsizing commercial line portfolios and developing personal lines.

Commercial lines refer to commercial and industrial type of Retakaful business such as industrial risks, construction risks, engineering, marine, aviation etc. The majority of the participants or insured entities are corporations. They are typically very volatile and subject to natural catastrophic exposure. To manage these types of risks, high capital and advance risk management expertise are required. The current size of the global takaful industry is still too small-spread to allow any Retakaful operator, including ACRR, to build a large enough and well-spread risk portfolio in order to absorb the inherent volatility. The small universe makes it impossible for Retakaful operators to pick and choose good quality risks to be brought into their pool

without compromising in terms of underwriting standard and discipline. Compromising on standards is considered “*haram*” for Retakaful operators, since almost certainly it leads to financial disaster by increasing the number of claims.

Personal lines refer to takaful or insurance products for individuals, such as home insurance, personal accident, travel insurance, health and family (life). This type of portfolio is less volatile than commercial lines. The sum insured is typically low, and entails a small premium (contribution). Therefore takaful or Retakaful operators must be able to build a very big portfolio size in terms of number of participants. To develop these lines of business, the company needs to build a completely different set of skills. The problem was that all ACRR staff were commercial lines people.

From a strategic point of view, bearing in mind the current landscape of the global takaful market, Patrice’s plan seemed reasonable. Industry statistics showed the global takaful portfolio to be heavily dominated by personal line products. However, the company had a ‘small’ problem. Due to the relatively small sum insured, the takaful fund managed by takaful operators would be able to comfortably absorb all of the risks, so Retakaful capacity was at a minimum level. They only needed to worry about catastrophic events such as pandemics, natural disasters, or a commercial airplane disaster. They certainly needed to get protection from Retakaful operators or reinsurance companies for such events. However, it would not cost too much, which meant that the flow of income to Retakaful would be very small.

Patrice recognised this threat and dealt with it by building a comprehensive expertise of personal lines offered as a package of services to takaful operators. Luckily, there were many takaful operators out there, who were not trained to properly design, launch and manage personal lines business in an effective and efficient way. Knowing this situation, Patrice was determined to build a strong team of personal lines experts in-house. Under this business model, ACRR would actively work hand-in-hand with its clients in each or most of the processes of product development and charge nothing. ACRR prepared itself to assume deficit at the outset. The compensation for ACRR was the commitment from takaful operators to share the business proportionally during a certain period of time (between 5 to 10 years). This was considered as a revolutionary way of doing Retakaful or reinsurance business. Traditionally, Retakaful would only supply underwriting capacity, without providing other extra services. This was a very big shift and turn-around for ACRR, but did they have any other option to survive?

Although Danial knew Patrice did not reveal everything, he walked out of Patrice office feeling much better than he had felt in the first session. He gathered new insight into the situation, but at the same time, was also convinced that the way forward would be tough and turbulent. He suddenly thought about his team. He had a good team of experts of commercial lines; a few of them had earned much recognition from the industry. Was the personal lines initiative really a sustainable solution for ACRR? Could his team be transformed into personal lines team with completely new mindsets and skills? Would all of them welcome the turn-around process, which was certainly not easy? Would they be staying under the dominant style of the Patrice?

Danial's mind was overwhelmed by so many questions. In fact, he himself could neither provide the answers to these questions nor foresee the answers as yet. He was even unsure whether he could manage himself through this turbulent time. He might survive or surrender.

Patrice's unfriendly, arrogant and aggressive personality really cramped Danial's mind. He was worried that it would be extremely difficult to manage the change process. Patrice might have a fantastic plan, but his personality could prevent him from winning the staff's trust and confidence.

THE FINAL CALL

One week later, Danial still could not find the answers to the questions; how could he provide the answers to his colleagues? In the meantime, Patrice fulfilled his promise of taking tough action on the administration backlog. He ordered all the underwriters, assistant underwriters and accounting department personnel to resolve the issues within a time period of three weeks. All had to work during the weekends. Nobody was allowed to take leave and prior approved leave was cancelled. The failure to meet deadlines or breaching the rules would have brought serious consequences. He said that the tough measures were necessary since the backlog occurred due to poor discipline and unprofessional conduct of the staff. It appeared as a punishment. This instruction was announced in a meeting attended by all staff members of the company. As usual, no one had the opportunity to explain the situation and why it had occurred from a different perspective. Most of the employees viewed it as a personal humiliation.

After this development, Danial realised that he needed to make up his mind as soon as possible. He took a day-off, doing nothing except sitting on a bench in the park, in his apartment compound. He thought very hard about the whole situation and what needed to be done.

The hours spent in the park were worth it. Eureka! He had found the answer and was confident of the action that he had to take. He reached the conclusion that Patrice's plan to promote personal lines and reduce commercial lines was reasonable in the short term, but was not sustainable in the long run. Even if his conclusion was wrong, he was sure that Patrice would fail in transforming the Company, since he could never win employee's trust given his arrogant style. He did not believe the Company had a bright future; therefore, he had to activate his back-up plan. He felt that it was only right that he share his views with his team. Ultimately, it was their call to decide what to do. As he had a good relationship with his subordinates, they were happy to share their feelings and plans with Danial. This made his work a little easier in navigating his team through such a difficult time.

About two weeks after the backlog clearance project was announced, Fazila, one of the assistant underwriters, decided to quit. She had been approached by another company. She quickly decided to accept the offer. It was a good offer anyway. This was another big loss. She was the best among the three Assistant Underwriters. She had a degree in actuarial science. A smart newbie, her good academic qualifications

and ability were balanced by good interpersonal skills. In reality, those with actuarial qualifications receive one of the highest pay packages in financial services. But she chose to be trained as an underwriter first before switching back to the actuarial path. By doing so, she would be an actuary plus (with underwriting knowledge and experience), a rare expertise in the industry. That was the reason why she agreed to join as an assistant underwriter and work side by side with the underwriter.

THE EXODUS

Patrice continued with his iron fist approach in executing the transformation plan. One by one, the staff members voluntarily withdrew. After Fazila, Danial lost his underwriter Yusas Nugraha. He was another first class underwriter in the team; smart, hard-working, a good team player, efficient, dedicated and committed. He moved to a Singapore-based reinsurer to be posted in Indonesia, his home country. What a great deal it was for him, working in his own country but being given an expatriate package.

A month later, Aishah and Harry took the same course of action. Aishah, an assistant underwriter, was seen as a very reserved person who did not talk too much. In reality she was a very good employee. She was smart, a quick learner, technically strong, dependable and was able to focus on solving relatively complex tasks. Harry was another assistant underwriter with 10 years working experience without significant progress. Though the least dependable member of the team, he was still able to find another job relatively easily.

The most recent casualty was Zunaida, who tendered her resignation and decided to retire early. Zunaida, 50 year-old, was a happy mother with 4 children. Her husband was a successful senior executive in the insurance industry. Her eldest child had just graduated in medicine from a Russian university under a scholarship from the Ministry of Defense and had joined the Malaysian Army as a medical doctor with the rank of Lieutenant. Her second child, a daughter, was studying accounting in London. Zunaida was the most senior member in the team, in terms of age and length of service in the industry. She had extensive networks in the market. When it came to work, she was the least efficient since she was not quick enough to adapt to new technology or to new approaches. Generally speaking, she had not been flexible towards change and new things.

An exodus of staff also took place in other departments at various levels. Staff resignations included the Human Resources Manager, Claims Manager, Compliance Managers, Actuary, Business Development Manager, Chief Marketing Officer, Chief Operating Officer, Chief Risk Officer, Product Development Manager, Shariah Officer and Patrice's personal assistant.

Patrice was working hard in recruiting new staff to build a new team of personal lines as well as to find replacements for the vacant positions resulting from resignations. Surprisingly, some newcomers interviewed and recruited by Patrice also quit. They had all left the job within the three months of the probation period.

Although Patrice would never admit to himself, company image and business were badly affected. High turnover certainly disrupted service delivery to clients. The market was clouded with various rumours regarding the company being in disarray. Most clients took a 'wait and see' attitude towards the company and ceased offering new business to the company. The target certainly could not be achieved that year.

Unfortunately, Patrice did not play his role as the company ambassador in the market to tackle the rumours. He was too focused on internal restructuring and paid minimum attention to proper communication with the market. He hardly visited clients, even to introduce himself. He stuck to his opinion that social meetings or functions among industry players were a waste of time.

The Underwriting Department was left with only three personnel, i.e., Danial, Vijay Kumar and Mohammad Hashim. Vijay, a British national, had previously worked in Manchester for 8 years as a credit insurer and as a member of the Allianz group. He was smart, a quick learner, had good interpersonal and communication skills, and was humble and adorable to the market.

They were all actively in a "searching" mode for new opportunities. Finding a new, good job wasn't that easy for Danial and Vijay, since both were expatriates. New jobs normally involve relocation of the whole family; therefore they had many factors to consider. Hashim was not too active, since he had joined the company only a year ago. He thought it would not look good on his CV if he had a very short period of service with an employer.

The company's management disarray certainly attracted the attention of shareholders. They began to closely supervise management activities. They requested reports more frequently and many decisions made by Patrice now needed Board approval before implementation.

CONCLUSION

At a certain stage of development, organisations may face situations that force them to undergo significant change. Changes may involve a new strategy, a new process, or a new organisational set up. Changes must be carefully planned and executed, failing which the organisation may fall into a worse state.

DISCUSSION QUESTION

1. What is the main problem in this case?
2. Explain the leadership style of Patrice. How could he have acted differently?
3. Did Patrice manage the change process effectively? Why or why not?