

Insurance Day

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Captives query value of 'one-stop shops'

Market asks whether it is getting the best deal having all services managed by one player

Greg Dobie

BROKER Aon's decision to start accepting contingent commissions again has raised questions in the captive market about whether owners are really getting the best value for money by having all their services managed as part of a "one-stop shop".

According to Clive James (*pic-*

tured, inset), director at specialist risk and insurance management services provider, Kane, the issue of whether a broker being a captive manager constitutes a conflict of interest has come to the fore in recent years.

James, who joined Kane from Aon at the end of last year, told *Insurance Day*: "Over the past few years you have had one company, for example, a major broker, that may do the placement

of the insurance upfront into the fronting insurer and then do the placement from that into the captive and then also the reinsurance out of the back end of the captive into the reinsurance market.

"They may also be doing things such as claims handling, claims management and risk analysis as well. So they are basically doing everything around the captive.

"The question is: 'is the cap-

tive itself, in terms of the board and the stakeholders, getting the best advice, if one player is doing everything from start to finish?"

"Is it following all the corporate governance and compliance rules? Is it getting the best price, the best deal, the best structure put into place, and is there any objectivity involved in that?" James continued.

Aon's announcement it would once again accept contingent commissions from markets where it was both appropriate and legally permissible, almost six years after the company stopped taking them (*Insuranceday*, Jul 21), drew criticism from the largest coalition of US corporate insurance buyers, the Risk and Insurance Management Society, shortly afterwards.

Now, James has questioned the impact it would have in the captive market: "Does that have a play, in terms for example of the reinsurance placement from the captive into the reinsurance market as well?" he queried.

"There are certain clients who like the one-stop shop and there are areas where that can work well, but as far as the captive is concerned, the way it is operated and the way it is regulated, it is a little bit different from doing transactional management or giving risk advice because it is a separate vehicle and we want to make sure the objectivity is there," James said.

Apart from using different players for different parts of the process, the alternative for those risk managers who preferred a one-stop shop, James suggested would be to have a separate adviser or a consultant to the captive who could review the arrangement on a regular basis to check its efficiency. "That may be a way around it," he concluded.

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Flood survivors cross a temporary bridge over a canal that overflowed in Charsadda, north-west Pakistan

Pakistan's floods are second worst in past 10 years

THE FLOODING in Pakistan is already second in the list of the most devastating global flooding events of the past decade, according to the Belgium-based Centre for Research on Epidemiology of Disasters (Cred).

The Pakistan floods are estimated to have killed more than 1,200 people. The only flooding event to kill more in the last decade was in Haiti in 2004, when two weeks of heavy rains generated floods that killed more than 2,500 people in the south-east of the country.

One-third of Pakistan – an area the size of England – is under water as a result of the floods.

According to Cred, seven of the 11 worst floods in the past decade have taken place the subcontinent.

The high concentration of low-income people living alongside riverbanks in countries such as Pakistan, India and Bangladesh make them susceptible to flooding.

The lack of a community-based early warning system in Pakistan has also been cited as a reason behind the high death toll.

Lloyd's Charities Trust has pledged to match up to £20,000 (\$31.139) in donations from market participants to the Pakistan Flood Appeal.

Those in the Lloyd's market looking to give donations are encouraged to visit www.thebiggive.org.uk/lloyds where they can make a donation to the Disasters Emergency Committee Pakistan Floods Appeal.

Scott Vincent

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St Peter Port, Guernsey: the captive market is asking questions about the value of 'one-stop shops'



Collateral tops list of concerns for CICA survey respondents

COLLATERAL is the number-one challenge facing captive owners and managers today, according to the results of the Captive Insurance Companies Association (CICA) annual survey, writes Greg Dobie.

Respondents ranked collateral at the top of their list of concerns

for the year ahead totalled 27%, up from 21.6% in the previous year's CICA survey. Regulatory issues and policyholder retention/growth came in in second place with 16.4% of respondents each, both up from the previous year.

The issue of collateral has generated lively discussions in cap-

tive circles for years. As the economic and regulatory environment continues to cause financial pressure for carriers, the return to fundamentals and the requirement of adequate collateral to support fronting programmes has come to the fore.

More than 90% (92.6%) of

survey respondents reported collateral was required. In response to the kind of collateral required by their fronting carrier, letters of credit (LOCs) were named by 76% of survey respondents with trust accounts named by 40%, cash by 28% and a parental guarantee by 8%.

Owing to the reduced availability of LOCs there was a reported uptick in the use of cash and parental guarantees to support fronted programmes, CICA noted.

It added: "From these results, two things are certain: change is constant and there will always be challenges to owning a captive."

Less than half of the survey respondents agreed or strongly agreed with the survey's statement that present economic conditions had, or were having, a detrimental effect on their captive.

This number shrunk to less than one-third for single-parent captive survey respondents.

Insurance Day

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Insurance Day is published five times a week (Monday to Friday).
Hard copy subscriptions are available at the following annual rates:
£1,795*; £2,244*; US\$3,231. Cover price: £7.50. Telephone: +44 (0)20 7017 5532.
Prices marked * excluding VAT

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ISSN 1461-5541. Registered as a newspaper at the Post Office. Published in London by Informa UK Ltd, Mortimer House, 37/41 Mortimer Street, London, W1T 3JH

Printed by Newsfax International, Unit 16, Bow Industrial Park, Carpenters Road, London E15 2DZ

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COMMENT

Riot: in spite of a very high number of claims, January's political risk renewals were largely positive

AP PHOTO/PETROS GIANNAKOURIS



Political risk remains an attractive option

AT THE START of this year, political risk was touted as one area in which primary insurers might consider expansion.

Despite an almost unprecedented level of claims last year, reinsurance market renewals in January were broadly supportive of political risk and structured credit insurers, brokers reported.

James Cunningham, UK head of political risks at Marsh, predicted a swathe of new entrants to the market and told *Insurance Day* at the time: "If you are looking to allocate capacity, I would suggest political risk and structured credit is an attractive mar-

ket, with higher premium rates than at any point in its history."

The strength of that sector was seen as good news for London, with around 70% to 75% of global volumes of premium income going through the London market, although there is an active market in Bermuda, six or seven carriers active in the US and some insurers expanding into Asia from the hub of Singapore.

However, not everyone took it as read expansion was the way forward. In May, for example, Chubb stopped writing new political risk and structured trade credit business, despite saying

the business had been profitable.

In a statement to worldwide surety staff, Chubb Surety's chief operating officer, Rick Ciullo, said: "Based on a strategic review of its operations, Chubb has decided to cease writing political risk and structured trade credit business effective immediately."

Beazley also continued cutting back in the line, slashing first quarter premiums for political risk business by nearly one-third.

Elsewhere, though, companies have been upping their presence in the sector, particularly on the international scene.

Ace Global Markets (AGM)

opened a US political risk and credit operation in Los Angeles to work with AGM teams in New York, London and Singapore.

And Liberty International Underwriters (LIU) Europe rolled out a trade credit and political risk business in France, headed by former Atradius underwriter Alexandre Egnell

Inevitably, with the activity taking place in this sector prices have fallen, but demand apparently remains high.

Richard Banks

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3 Allianz CEE suffers

Allianz saw operating profit fall 37% in the central and eastern Europe region during the first six months as a result of weather-related losses in Bulgaria, the Czech Republic, Poland, Hungary, Romania and Slovakia



4 Navigators elects

Former RSA group chief executive Bob Mendelsohn has joined the board of directors at US insurer Navigators. Mendelsohn spent four-and-a-half years at the helm of the then-Royal & SunAlliance

5 Prudential profits

Prudential's failed bid to buy AIA, the Asian life business of AIG, cost it £377m, but it still managed to record a £442m profit in the first half. And the group's chief executive insisted its Asia strategy would continue



6 Discrimination fear

There is a small but real concern standard arbitration clauses may be void because they may discriminate after the UK Court of Appeal decided arbitrators are in 'employment' for the purposes of discrimination law



7 Investors redress

Following the Bernie Madoff Ponzi scheme, the offshore cases illustrate various strategies used by disappointed shareholders/investors in failed funds to redeem subscriptions or recover losses



8 This Week...

The stuttering 2010 Atlantic hurricane season has continued to fail to match its forecasts in its 11th week, with the fifth tropical depression of the year petering out over the Gulf of Mexico yesterday morning

Ironshore is in demand

Christopher Munro

IRONSHORE'S political risks division has received some 300 submissions and conducted transactions in around 80 different countries since it first opened for business at the beginning of April.

Dan Sussman, head of the insurer's political risk division, explained the figures justify the company's entry into the sector.

The Bermuda-based insurer announced it was entering the political risk market in March, with Sussman, former head of XL Capital's financial lines segment, hired to lead its entry into the sector (*Insuranceday.com*, Mar 3).

"We've seen diverse potential sources of business. We are extremely pleased with the diversity of the business and the nature of the business," Sussman said.

It is in the developing markets where Ironshore sees real potential for growth and, according to Sussman, it has already built a geographically diverse portfolio of business. "We've had a lot of interest from Africa, eastern Europe, the CIS [Commonwealth of Independent States] jurisdictions and Latin America," he said. That does not mean the insurer is limiting itself solely to the developing markets, though. "We have also participated in a number of first-world transactions – it's extremely diverse," he said.

According to Sussman, pricing in the political risk market has fallen from the peak seen last year, yet remains considerably higher than in the troughs in early 2006 and 2007: "Pricing is very adequate and volume is very reasonable."

Ironshore's impressive entry into the market has come at a time when there has been an increased focus on political risk insurance. The economic crisis that has dominated the world's markets has affected businesses around the world, while in the insurance sector capacity has left the market, most significantly with Chubb's withdrawal from the political risk and trade credit segments in May (*Insuranceday.com*, May 25). But the impact on the level of capacity serving this area of business has been minimal, with entrants counteracting the withdrawal of capacity.

But despite the apparent benefits of entering the market earlier this year, Sussman said Ironshore is in the market for the long haul: "Ironshore has clearly made a decision to invest in this business and we see it as a long-term opportunity. We believe the risk-management demands of our clients are only going to grow. Over the medium term and as our appetite grows, we can become an even more meaningful player."

The launch of the political risk division, which writes risks from Ironshore's US platform, further enhanced the company's existing capabilities in the market – offered in the UK via Pembroke, its Lloyd's Managing Agency.

Weather-related claims eat into Allianz's 1H CEE operating profit

Scott Vincent

ALLIANZ saw operating profit fall 37% in the central and eastern Europe (CEE) region during the first six months of 2010 as a result of weather-related losses in Bulgaria, the Czech Republic, Poland, Hungary, Romania and Slovakia.

Allianz's CEE business posted a €100m (\$128.3m) operating

profit for the first half of this year. In the second quarter, Allianz recorded more than 91,000 claims across these countries.

"Flooding, thunderstorms and prolonged rain showers plagued the region during the second quarter," Werner Zedelius, member of the board of management at Allianz SE responsible for growth markets, said.

Gross premiums written for property/casualty (p/c) business in CEE rose 1% to €1.39bn in the

first half, but p/c operating profit was down 54% to €56m on the back of the high level of catastrophe activity.

The continued decline of new car sales across the region also led to a shrinking of new-business volumes for motor cover.

Life and health business bought more positive news for Allianz in the CEE region, with double-digit growth in premiums and operating profit.

Life and health premiums in

CEE were up 18% in the first half to €607m, compared with €514m during the corresponding period last year. Life and health operating profit was up 18% to €45m.

Allianz said one of the drivers of this development was the stable demand for traditional life products, accompanied by successful sales campaigns for single-premium products in countries such as the Czech Republic and Hungary.

Allianz said the six-month

period also saw it become the market leader in terms of life and health revenue in Croatia.

Manuel Bauer, regional chief executive of Allianz in CEE, said: "Our life and health segment performed well during the first half of 2010. I am confident we will maintain our growth momentum in this segment. The ageing of the population across the region will create a huge demand for private old-age provision across all age groups."



The Ondava river bursts its banks in Trebisov, east Slovakia: heavy rain and associated flooding saw Allianz's CEE operations hit by a claims surge during the first half

Hiscox inks Dual deal to supply 25% of underwriting capacity

DUAL INTERNATIONAL has entered into a partnership with Hiscox that will see the latter providing up to 25% of the underwriting agency's global capacity, writes Christopher Munro.

The deal, which complements Dual's existing capacity arrangements with Arch Insurance, was described as "a tremendously exciting step forward" by Dual International's chief executive, Bob Van Gieson. He said: "This new partnership represents a tremendously exciting step forward for the Dual group as we seek to expand beyond our traditional lines of business.

"It brings together the strength of Dual's distribution channels and the appetite Hiscox has for exploring profitable lines, while enabling us to maintain our tradition of providing our clients

with access to quality capacity."

According to Van Gieson, several parties came to the table to offer capacity to Dual, but Hiscox was chosen because of its financial strength and security, in addition to "its appetite and willingness to develop a stable, long-term partnership". He added: "I firmly believe this strategic relationship will be pivotal in helping us achieve our ambitions."

The deal will initially see Hiscox providing capacity to Dual's operations in the UK, Ireland, Italy and Australia, with further expansion across Dual's other offices expected in due course.

Gary Head, Hiscox's UK underwriting director, said: "This is an exciting partnership for Hiscox, with a business that has a history of delivering solid underwriting profits. The Dual group has a

strong brand in the professional indemnity and directors' and officers' [D&O] markets and a very experienced team of underwriters, which is a natural fit for us."

Despite the influx of new capacity provided by Hiscox, Arch will continue to be the largest provider of capacity to Dual.

Dual has been busy securing new capacity of late; last week, its Cologne-based managing general agent Dual Deutschland revealed it had secured new capacity from Newline Insurance Company that will allow it to start writing D&O cover for large, German financial institutions (*Insuranceday.com*, Aug 6). And in July, Newline syndicate 1218 and Dual entered into a partnership whereby the former would provide £10m (\$15.6m) in excess capacity for D&O risks (*Insuranceday.com*, Jul 15).

MLP returns to black

Anne-Christin Gröger, Cologne

GERMAN insurance broker MLP swung back into profit in the first half of the year.

The company achieved a profit of almost €5.3m (\$6.8m) in the first six months of 2010 compared with a loss of €6.5m in the same period of last year.

Earnings from commissions for new policies increased during the period to €208.8m from €203.5m the previous year. The growth in profit was mainly owing to higher proceeds from selling health insurance and from wealth management.

MLP's chief executive, Uwe Schröder-Wildberg, said: "The positive signs we noticed at the beginning of this year have been confirmed during the past few months. Despite the fact the

overall situation remains tense, we managed to increase our earnings from commissions in the second quarter."

During this period, MLP earned €99.7m in commissions, compared with €91.9m during the second quarter of 2009.

However, Schröder-Wildberg was not prepared to say the worst is over: "Despite bright spells in the market, we have a long way to go before we reach the level [we were at] before the financial crisis."

However, MLP has made no progress in an important segment: old-age pensions. Revenue from pension policies fell 3.6% to €118.6m. In health, by contrast, sales grew almost 17% to €26.6m.

The number of consultants and customers continues to fall, however. From January to June 2010, MLP lost 24 consultants and has now only 2,359 agents. The number of customers fell 2% to 767,000.

NEWS



Mendelsohn: joining board of directors at Navigators

Navigators adds Mendelsohn to senior management as director

Scott Vincent

FORMER RSA group chief executive Bob Mendelsohn has joined the board of directors at US insurer Navigators.

Mendelsohn spent four-and-

a-half years at the helm of the then-Royal & SunAlliance, having previously served as chief executive of Royal Insurance Group, which merged with Sun Alliance in 1997.

In September 2002, he was ousted from the top position after RSA came under pressure

because of its deteriorating performance. Since then, he has been working as an independent financial services professional based in New York.

Mendelsohn is proud of being the first American to head a major British financial institution.

He led RSA to become the first

British insurer licensed in China, the first foreign insurer licensed in India and one of the largest direct-to-consumer internet insurers outside the US.

Mendelsohn's career began as an attorney at Wilkie Farr & Gallagher and also includes a 20-year stint at WR Berkley Corporation.

At WR Berkley, he rose to the role of president and chief operating officer.

Mendelsohn is also a former chairman of the American Insurance Association and a former trustee of the Chartered Property Casualty Underwriters Society.

Brit Insurance appoints Egan to replace departing Scales as CFO

Peter Birks

BRIT INSURANCE has appointed Scott Egan chief financial officer (CFO).

Egan will succeed Matthew Scales, who earlier this year announced his intention to step down from the role.

However, Scales will remain with Brit until Egan joins. Egan comes to Brit from Zurich Financial Services where he has worked since 2007.

Before that, he was at Aviva, where he held a variety of posts.

Brit Insurance's group headquarters in the ITO-Tower, Amsterdam: the insurer has named Scott Egan successor to Matthew Scales as chief financial officer



Thomas Miller hires Matthews

Christopher Munro

THOMAS MILLER, the UK protection and indemnity (P&I) club manager, has hired Mike Matthews from Shipowners Club.

Matthews, who will reinforce the underwriting teams of both the UK P&I and UK Defence clubs, will work predominantly with the two clubs' Greek memberships when he joins on September 20.

Along with Paul Collier, the company's senior underwriting director, Matthews will work in tandem with the clubs' claims staff in London and Piraeus.

He brings to Thomas Miller more than a quarter of a century's experience in marine insurance broking and underwriting within the P&I field, and takes the number of claims handlers and underwriters at the UK P&I and UK Defence clubs focused on Greek members to 26.

RenRe gets retired Zore on to board

RENAISSANCERE has added Edward Zore, the recently retired chairman and chief executive of Northwestern Mutual Life Insurance Company, to its board, writes Scott Vincent.

Zore replaces William Hecht, who has retired as a director, having served as a member of the board since November 2001.

Zore has served in a number of roles at Northwestern Mutual, where he was chief executive from 2001 until June this year.

He originally joined Northwestern Mutual's investment department in 1969.

Meanwhile, the RenRe board has announced a quarterly dividend of 25¢ per common share on its common stock. The dividend is payable on September 30, 2010 to shareholders of record on September 15, 2010.

The board has also approved an increase in RenRe's stock-repurchase programme, bringing the total authorisation to an aggregate of \$500m.

Last month, RenRe announced a net profit of \$375.3m for the first half of the year, an increase of 1.8% compared with the corresponding period in 2009.

Dixon to fill Ace's MENA MD position

ACE EUROPE has appointed Steve Dixon regional managing director for the insurer's Middle East and North Africa (MENA) region, writes Scott Vincent.

He succeeds Giles Ward, who has been in charge of Ace in the region since 2006.

Ward will now serve as chief executive for Ace Australia and New Zealand.

Dixon's appointment is an internal promotion and he has served Ace since the acquisition of Cigna in 1999.

In 2001, he became casualty manager for continental Europe and emerging markets.

In 2006, he moved to Tokyo to become regional vice-president and director for Ace Far East, where he was responsible for the property/casualty and personal lines businesses.

Andrew Kendrick, chairman and chief executive of Ace Europe, said the Middle East and North Africa region offered significant opportunities.

"This is especially the case within the construction and energy sectors, but also within the accident and health and personal lines arena," he said.

Ace's MENA operations encompass Egypt, Pakistan, Saudi Arabia and the United Arab Emirates through its regional office in Bahrain, which it established in 2007.



Prudential headquarters in London: the insurer managed to record a profit of £442m for the first half

FRANTZESCO KANGARIS/
BLOOMBERG

Prudential reports profits in spite of costly failed AIA bid

Peter Birks

PRUDENTIAL'S failed bid to buy AIA, the Asian life business of AIG, cost it £377m (\$587.8m), but the insurer still managed to record a £442m profit in the first half.

And the group's chief executive insisted its Asia strategy would continue. Tidjane Thiam said: "We find the emerging markets of south-east Asia – such as Indonesia, Vietnam, Singapore and Malaysia, together with Hong Kong – particularly attractive".

Thiam also said the company

saw opportunities for "high returns" in the US, where Prudential planned to continue its focus on increased volumes in variable annuities, "while managing fixed-annuity sales in line with our strategy of capital efficiency".

However, the UK was seen as "a mature market with lower growth and lower returns than are available to us elsewhere in the group's portfolio". The benefit of the UK was Prudential's financial performance there "provides strong support to our credit rating at a Group level and continues to be a significant contributor to our overall performance".

Its first-half performance this year compared with a loss of £254m in the same period of 2009.

Shareholders' equity rose £900m over the period to £7.2bn. Operating profit based on longer-term investment returns was £968m, up from £688m.

Prudential noted, after eliminating variable hedge gains, the International Financial Reporting Standard profit pre-tax would have been £845m, up from £711m in the first half of 2009, and said these numbers were "a better reflection of our underlying performance over the previous year".

Prudential said the cost of the

terminated AIA deal consisted of a £153m break fee payable to AIG, foreign exchange hedge costs of £100m, underwriting fees of £58m and adviser fees of £66m.

The pre-tax profit from continuing operations still came in at £593m, up from a loss of £76m in the first half of 2009, although last year's numbers were affected by a £621m write-off on the sale of Prudential's Taiwan agency business. The Insurance Groups Directive surplus was £3.4bn, the same as at the beginning of the year. Prudential raised its interim dividend to 6.61p a share (2009: 6.29p).

Vietnamese non-life growth is on track to exceed last year's results

Richard Banks

GROWTH in Vietnam's non-life insurance sector in 2010 is predicted to outstrip last year.

The latest estimates from the Vietnamese Ministry of Finance put non-life growth this year at 15%, which would take the figure to Dong 15.7trn (\$822m).

This growth figure is at the mid-point of the projected range first unveiled a year ago, but ahead of 2009's growth of 13%.

Growth this year is expected to come from both commercial and personal lines, with construction, fire and cargo business at the vanguard of the commercial expansion.

Construction insurance has been especially popular as gov-

ernment investment in infrastructure projects increases.

On the personal lines side, motor insurance – including motorcycle cover – has soared on the back of higher vehicle ownership, fuelled by the expanding middle class in the country.

Alongside the growth in premium in the Vietnam market has come a growth in provision.

There are 29 insurers operat-

ing at present and competition is increasing.

Analysis by Japan's Nikkei suggests less than one-third of the non-life insurers in Vietnam made an underwriting profit last year, prompting speculation about consolidation in the coming years.

One commentator suggested the number of players could be cut to 15 over the course of the next decade.

Ping An posts 22.7% premium income rise

CHINESE insurance giant Ping An enjoyed a 22.7% year-on-year rise in premium income in July.

During the month, it wrote Yuan 15.7bn (\$2.3bn) of premium, up substantially on the same period last year, but down 15.6% on the previous month.

So far this year, the group has written premium totalling Yuan 138.8bn.

Ping An Life Insurance is China's second-largest life insurer and life insurance represents the largest proportion of its premium income.

In the first seven months of the year, it wrote life insurance premium of Yuan 101bn.

Property premium, written by Ping An Property Insurance – China's third-largest property carrier – was Yuan 34.9bn in the first seven months.

For the first six months of the

year, premium written by Ping An was up nearly one-third year on year.

Earlier this year, Ping An P&C won an A insurer financial strength rating from Standard & Poor's (S&P).

The rating agency acknowledged the insurer operates in a "highly competitive" marketplace, but noted Ping An P&C's strong competitive position, good underwriting performance, and reasonably prudent investment philosophy, as well as the implicit support from the company's parent.

An improvement in motor business – Ping An P&C's largest line – helped push the 2009 combined ratio below the 100% mark and S&P expects its underwriting performance to strengthen gradually in the next two to three years.

Jin becomes head of life as CNinsure undertakes management reshuffle

NASDAQ-LISTED Chinese broker CNinsure has named Fred Jin the new head of its life insurance operations, writes Richard Banks.

Jin, who has been serving as chief operating officer and chief information officer for the group, replaces Chengbin Li, who will be taking on responsibilities for human resources management and strategic planning.

Li had headed the life insurance unit since 2008 and has held a number of roles within the company including department general manager and general managers of various insurance agencies or financial service firms controlled by CNinsure.

The company is undergoing a management reshuffle as it prepares to focus its resources on four new profit centres: insurance brokerage business, telemarketing and internet sales, consumer credit brokerage business and wealth-management distribution business.

Jin has been chief operating officer of the company since November 2008 and chief information officer since November 2007.

Before joining CNinsure in October 2007, Jin served as assistant president and chief information officer of New China Life Insurance and sales manager and financial planner at US-based Prudential.



Guangzhou, home to CNinsure, which is undergoing a management revamp

LEGAL FOCUS



Marine market: brokers have been handed better protection in the event a policyholder defaults on the payment of premiums

Are marine market participants really seeking change?

A LAW COMMISSION consultation paper in the UK recommends reforms to give marine brokers better protection in the event of a policyholder defaulting on payment of premium. While supporting the proposals, Tim Goodger, a partner at Elborne Mitchell, questions whether market participants want change.

Many people consider a broker's responsibility for the payment of marine premium to insurers, being the default position set out in s53(1) of the Marine Insurance Act 1906 (MIA), to be anomalous and outdated.

The Law Commission, as part of its review of insurance contract law, agrees. It believes the MIA also leaves underwriters unfairly exposed in the event the broker is unable to pay. The commission has recommended reform, either by repeal or replacement of the provision. First, though, it is seeking views.

The commission considers policyholders should be liable for marine premium payments, bringing it into line with general agency law and non-marine insurance business. It also suggests that the combined use of non-risk transfer agreements and the Financial Services Authority's client money regime for brokers, by which client money held by a broker is impressed with a trust, would provide a fairer solution on broker insolvency. A policyholder would be better placed to recoup premium paid to an insolvent broker and then pay the premium again.

Insurers would then be able to

sue policyholders for premium if there were a payment default. An assured has no liability to the insurer even though the insurer remains liable to pay a claim unless the policy has been terminated. The Law Commission rightly has identified the common law fiction – premium treated as having been paid to the insurer and lent back to the broker – as creating confusion.

The commission, however, makes little comment on another matter: the market's use of the words prefacing s53(1): "Unless otherwise agreed ..." Arguably that proviso has always allowed parties to negotiate terms other than the default position. Surely if there is an appetite to do so, parties simply can negotiate that the policyholder be responsible for premium?

The commission suggests brokers may not be able to contract out by simply inserting a term in the terms of business agreement (TOBA) excluding the operation of s53(1), because the policyholder itself is not party to that TOBA. However, it does not mention brokers can also enter into TOBAs with client policyholders and obtain authority to agree which party is responsible for premium. How else would parties agree "otherwise"?

There is now an open invitation to make submissions to the commission on the existing law and practice, as well as s53(2), the right of lien, and on s54 MIA, by 19 October. The market should seize this opportunity.

p7: More on the Law Commission

Arbitrators are 'employed' in discrimination law terms

THERE is a small but real concern standard arbitration clauses may be void because they may discriminate on grounds of race, age or gender, warn Susan Dingwall, a partner, and James Thomas, an associate at Norton Rose LLP.

The UK Court of Appeal case *Jivraj v Hashwani* (June 22) decided arbitrators are in "employment" for the purposes of discrimination law. A rule a sole arbitrator or chairman of the panel must come from a different country from the parties may discriminate on grounds of race, which includes nationality.

This clause is found in the rules of most arbitration institutions such as the London Court of International Arbitration, whose rules are widely used by the insurance and reinsurance market for the resolution of disputes. Other clauses may discriminate on grounds of age or gender. If discrimination is found, the whole arbitration agreement, not just the appointment provisions, could be void.

In *Jivraj*, a joint-venture agreement contained an arbitration clause specifying the arbitrators must be from the Ismaili community. The court found arbitrators are in "employment" for the purposes of the Employment Equality (Religion and Belief) Regulations 2006 because the regulations were based on a European directive access to the labour market must be free to all.

The court held the choice of a solicitor, plumber, arbitrator or anyone who provides services should not be made in a way that discriminates on the basis of religion, race or any other grounds.

The exception in the regulations, for a "genuine occupational requirement", did not apply – the

arbitrators were required to decide the dispute according to English law, not according to any religious principles, and so the requirement to be Ismaili was not necessary to carry out the job of an arbitrator.

The whole arbitration clause was held to be void because the characteristics of the arbitrators are often critical to securing agreement to an arbitration clause and so it was impossible to sever the appointment provisions from the rest of the arbitration clause. The parties were required to agree a new clause or to use the courts.

There is a possibility a requirement an arbitrator comes from a different country from the parties is discriminatory because it is not an occupational requirement. While the justification for the provision is to ensure the impartiality of the arbitration, arbitrators are already required to be impartial by the Arbitration Act 1996.

It is likely the standard Insurance & Reinsurance Arbitration Society clause, that arbitrators must have "not less than 10 years' experience of insurance or reinsurance within the industry or as lawyers or other professional advisers serving the industry", is safe because it is a "proportionate means of achieving a legitimate aim" under existing age discrimination regulations, but this is a question of degree and other clauses may be age discriminatory.

The Equality Act 2010 will soon replace existing discrimination law but will not alter it significantly. Under the act, direct or indirect discrimination on grounds including race (nationality), age, gender, sexuality and disability will be prohibited unless there is an occupational requirement for the provision.

The act seems to affect arbitration agreements governed by English law or where the seat of the arbitration is in England, and the substantive law to be applied to the dispute will be irrelevant. As both the regulations and the act are based on European law, the issues for arbitration may affect other European jurisdictions.

The Court of Appeal decision in *Jivraj* arguably goes against the trend of the English courts to be supportive of arbitration where possible. On the face of it, the

Court of Appeal's decision erodes parties' rights to specify the characteristics of the arbitrators they wish to resolve their dispute.

Party autonomy in this respect now appears to be fettered by employment law. That would not appear to have been the general intention and while the decision in *Jivraj* is of concern, an appeal to the Supreme Court may provide clarity. Alternatively, it is to be hoped the courts will contain the effect of *Jivraj* in future cases.

Arbitration: *Jivraj* case has applied principles of employment law to dispute resolution



FSA's proposals for reforming PPI will be a disappointment to financial services sector

ON AUGUST 10, the UK's Financial Services Authority (FSA) published a policy statement with new rules for reforming payment protection insurance (PPI) and claims to ensure customers are treated more fairly when complaining about PPI and when buying the product.

Dan Preddy, financial services partner at Beachcroft LLP, commented: "While it will not have come as a surprise to many, there will be widespread disappointment at how little the FSA's approach has changed from the proposals it made back in March.

"In particular, there will be deep disappointment about the application of standards retro-

spectively including to sales made before the FSA regulated general insurance mediation and the lack of differentiation between different types of PPI – for example, regular premium mortgage PPI – or different sales channels. Industry concerns about the assessment of evidence, the calculation of redress and the timetable for implementation have also largely been ignored.

"In reaffirming the FSA's existing strategy in relation to PPI complaints, the policy statement represents very bad news for the financial services industry and, in particular, sellers of PPI. The FSA's estimate of the costs of implementing the

redress it is demanding range from £2bn [\$3.13bn] to £4bn and it accepts this may lead to 5% to 10% of general insurance intermediaries failing.

"However, for insurers as opposed to intermediaries, there is some welcome clarification as to their position. It's always been clear the FSA's overriding concern has been with the selling of PPI but where that actually left providers was less clear.

"The FSA now states: 'Distributors are responsible for maintaining a compliant sales process, and therefore should be responsible for redress, where a failing arose from the manner in which the product was sold. If brokers feel undue pres-

sure was placed upon them by lenders or insurers, they may separately have recourse to the courts if they so choose'."

"It is to be hoped the Financial Ombudsman Service takes note of that position because it has been tending to blur the lines between distributor and producer in this context, particularly where it has retrospective jurisdiction over the latter and not the former.

"Of course, although the FSA has clarified who it considers should be taking primary responsibility for making redress, the scope for litigation between intermediaries and introducers for contributions to these payments remains very real."

No money-back guarantee

AMANDA MOCHRIE considers several court cases involving disappointed investors trying to recover their recent losses



FOLLOWING the Bernie Madoff Ponzi scheme, the offshore cases illustrate various strategies used by disappointed shareholders/investors in failed funds to redeem subscriptions or recover losses. The Bermudian cases on the treatment of segregated account companies are particularly interesting because they raise issues of direct relevance to hybrid insurers.

Attempts by investors to recover losses from solvent funds are less widely reported, although some guidance is now emerging from the US.

One route pursued by investors is to issue a statutory demand with a view to winding up a fund. In *Professional Offshore Opportunity Fund v Daiwa Securities Trust and Banking (Europe) plc* [2009], British Virgin Islands (BVI) Eastern Caribbean Supreme Court investors served a statutory demand, which the fund opposed on the basis there was a genuine dispute as to the debt. The fund's directors had tried to suspend redemption liabilities after the due redemption date but before payment of redemption proceeds. The BVI court upheld the statutory demand.

In *Re Matador Investments Ltd* [2009], the Grand Cayman Court, in the context of a redeeming investor where a winding-up petition had been issued on the grounds the company was insolvent and also on "just and equitable grounds", distinguished *Strategic Turnaround v Culross Global* [2008] CILR 447 and held where the fund is trying to suspend redemptions and suspend rights to receive proceeds, you have to look at the precise wording of the byelaws and offering documents to see whether the fund is entitled to do so.

The court noted backdated resolutions will not assist directors with the redemption situation, but in the future adding an express power into the byelaws could assist. A number of recent cases also examine the grounds for winding up including inability to pay debts as they fall due, "just and equitable" and "loss of substrata" in the funds context.

Unfair prejudice claims by shareholders are an alternative strategy being pursued by investors. In *Citco Global Custody v Y2K Finance Inc*, the BVI Court of Appeal [2009], the claimant fund had invested in the Y2K fund. This

was a claim by a non-redeeming investor who was a shareholder.

The fund had permitted the other shareholders to redeem and then put a suspension on redemptions, so this particular investor lost out. This investor lost at first instance, but in the Court of Appeal the claim was amended to an unfair prejudice claim, for which there are a wide range of remedies available (including, for example, that the fund buys out the claimant's shares). The Court of Appeal thought the unfair prejudice claim was a difficult but sustainable claim.

Yet another route pursued by disappointed investors is to assert subscription monies are held in trust. In *Kingate Global Fund Ltd v Knightsbridge (USD) Fund Ltd* [2009], the Bermudian Court of Appeal considered this issue. This was a claim by investors who sent in a subscription at the same time Madoff was arrested. The fund suspended subscriptions and redemptions but had received this money in its account. Investors demanded the fund pay the money back, or at least acknowledge it held this money on trust.

The question for the court was whether in the absence of express wording there was an implied trust as an incidence of the contractual terms. Both the judge at first instance and the Court of Appeal agreed there was a trust and the money belonged to the shareholders until they received their shares.

It was argued there is always a trust in these circumstances but the Court of Appeal disagreed because of authorities relating to unsecured creditors, which the court distinguished in this case. Thus, investors may have the benefit of a trust when they subscribe to shares.

There are various dicta about subscription and redemption monies belonging to shareholders rather than funds that may prove problematic. An issue for the banks is they may hold a trust account for beneficiary shareholders in circumstances where the bank may have thought this money belonged to the fund.

This potentially exposes the banks to liability for breach of fiduciary duty and assisting breach of trust. Unsurprisingly, the case is being appealed to the Privy Council. No redeeming investor has yet claimed a trust.

Tensor Endowment Ltd v Newstream Capital Fund Ltd [2009] is the first judgment on segregated account companies to come out of Bermuda. The fund was set up as a segregated account mutual fund company. The assets held for each segregated account consisted of loan notes.

The applicant, Tensor, applied to appoint a receiver under the local segregated accounts legislation in relation to an account linked to Class K shares. Tensor had sought to redeem its Class K shares in January 2008, but the fund had declined to pay out and

instead had promoted an out-of-court plan designed to create a two-year forbearance period within which markets might recover and to avoid investment losses for all classes of shareholders caused by any fire sale of collateralised assets. Tensor did not consent to the plan.

The court held the plan did not purport to or have the effect of varying Tensor's Class K share rights. However, the court also found the test for insolvency under the segregated accounts legislation, which was limited to cashflow insolvency, was not met and for the purposes of that test the admitted inability to meet redemption requests was irrelevant.

The appointment of a receiver required proof of just and equitable grounds, which in the case of Tensor's application fell away once the insolvency ground failed. Relevant considerations were the majority of Class K shareholders opposed the appointment of a receiver and Tensor had failed to advance a case as to how any receiver might liquidate the account's assets in a more effective manner than was proposed under the plan.

The court observed this did not leave unpaid redemption creditors with no enforcement remedies, as they could bring ordinary civil proceedings against the company in respect of one of its segregated accounts and any such judgment could be enforced against any free assets in the segregated account. The next logical step would therefore be a summary judgment application.

In the most recent round of this litigation, interesting issues arose as to whether the freedom of the managers to manage the assets of a mutual fund; alternatively, the statutory segregation concept (assets linked to particular accounts) and the parties' contractual bargain set out in the byelaws would prevail.

The claims emerging from the US by investors against solvent funds are not directly applicable to the Commonwealth arena because under the relevant misrepresentation and securities legislation the bar is set high in terms of needing to prove fraud.

However, it is of interest to note the misrepresentations relied on are primarily failure to conduct promised due diligence and to ensure diversification of investments. Also, offering materials drafted as they are by lawyers are not proving to be as fruitful a hunting ground as statements made by funds when marketing directly to potential investors.

Amanda Mochrie is a senior commercial litigator at Trott & Duncan, Bermuda. The views expressed in this article are the author's own and not necessarily those of the firm



Madoff: left many investors out of pocket

DANIEL BARRY/BLOOMBERG NEWS

LEGAL BRIEF

BARLOW LYDE & GILBERT



Reforming rules on claims fraud is a timely move

LAST month, the English and Scottish Law Commissions published their seventh Issues Paper of proposals for reform of insurance law. This paper focuses on the respective duties owed between insured and insurer once the contract in question has been formed, specifically once a claim has been made.

Of primary concern to the commissions is how to deal with fraudulent claims. They have made a number of proposals and have invited responses from interested parties by October 11.

Section 17 of the Marine Insurance Act 1906 codifies the basis on which the insured and insurer enter into a policy of insurance: "A contract of marine insurance is a contract based upon the utmost good faith and, if the utmost good faith be not observed by either party, the contract may be avoided by the other party."

The section applies to both marine and non-marine policies. In practice, the duty of utmost good faith after inception of a policy is relatively narrow in its scope.

It translates into a requirement on the insured to act honestly when making a claim and on the insurer to investigate diligently, assess and pay valid claims.

It also applies as and when a policy is being varied or renewed but the commissions have aligned these instances with pre-contract disclosure and misrepresentation and decided to consider them further in that context.

Fraudulent insurance claims in the UK are fairly common and on the increase. Association of British Insurers' data indicates 1.4% of claims made in 2008 were rejected as fraudulent.

Therefore, any real or perceived dilution of the remedies available to insurers to deal with such claims is likely to encounter stiff opposition. The entitlement of an insurer to avoid a policy from its inception if an insured makes a fraudulent claim may, for example, act as a deterrent to some insureds tempted to "bump up" their otherwise honest claims.

The commissions have suggested it is correct a policyholder who lies in connection with a claim (whether by entirely concocting it or by exaggerating the value of a genuine claim) should forfeit that claim, otherwise the moral hazard of policyholders believing they have nothing to lose by submitting a fraudulent claim is too high.

However, the commissions consider the existing law dealing with fraudulent claims to be unnecessarily confused. They conclude avoidance is not necessarily the most appropriate remedy when a fraudulent claim is made.

The commissions deem it unfair insurers could require insureds to repay all claims made under a policy, including valid claims made and settled before the submission of the fraudulent claim.

They point out in a number of cases the courts have ruled the fraudulent claim be forfeited while earlier claims remain undiminished. They therefore propose the Marine Insurance Act s17 should be amended to reflect the direction favoured by the courts. They suggest:

- 1) The insured should forfeit the whole of the claim to which the fraud relates;
- 2) A fraudulent claim should not affect previous, valid claims, whether or not they have been paid; and
- 3) A fraudulent claim should give the insurer the right to terminate the contract, but should not affect a valid claim arising between the fraud and the termination.

The commissions consider it vital the UK's insurance law be perceived internationally as coherent and principled. The Marine Insurance Act should therefore codify the law as it is being applied.

At a time when fraudulent insurance claims are on the increase and criminal prosecutions against those who perpetrate them remain few and far between, it will be interesting to read the market's responses to these suggestions.

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Insurance Day

FRIDAY 13 AUGUST 2010

This Week...



THE STUTTERING 2010 Atlantic hurricane season has continued to fail to match its forecasts in its 11th week, with the fifth tropical depression of the year petering out over the Gulf of Mexico yesterday morning. An area of low pressure did bring rain to the Louisiana coast but the strongest landfall in the US so far in 2010 remains Bonnie's short-lived excursion over Florida last month.

A pattern of storms weakening in their approach to land is possibly emerging, which, if it continues, would be great news for the annual bonuses of underwriters with exposures along the coast.

But the season is not over yet. While some forecasters have dropped their predictions slightly, most still maintain the peak period of the season will see a large number of storms form, with land dwellers in the vicinity warned they are not out of the woods yet.

The second week in August is not traditionally the busiest news week of the year and much of the past few days has been dominated by results announcements. The general trend has seen companies retain fairly sizeable profits despite what is frequently billed as the worst first half on record for catastrophe losses.

The UK's bid to descend from a working system of insurance supervision to regulatory chaos continued to gather pace this week as news emerged of a 128% year-on-year increase in the number of staff leaving the soon-to-be-abolished Financial Services Authority (FSA). The strong reputation the UK insurance sector has built up in the eyes of Europe as Solvency II implementation approaches is threatening to be undermined by the regulatory instability caused by the decision to scrap the FSA.

However, the London Market Group this week told insurers participating in its new electronic endorsements pilot could provide companies with a boost when it comes to meeting the data requirements introduced by Solvency II.

Across Europe, talk about how to prepare for the new regime is continuing. Some might suggest now is the time for action, not words. It seems like many years since we were all first warned: "Now is time to act on Solvency II."

However, many within the industry feel the dialogue still needs to continue as there is more talking to be done. Allianz chief executive, Michael Diekmann, believes there is still the need for more discussion and has called into question the timetable for the implementation of Solvency II.

Any delay in plans to implement at the end of 2012 will be great news for the various consultancy companies that have been given a licence to print money by the ongoing process.

Also in the news this week:

- Northern Ireland's Department of Justice said an increase in terrorist attacks is on course to push claims to the province's Criminal Damage Compensation Scheme up 25% year on year;
- Tropical storm Dianmu made landfall in South Korea before following a path towards northern Japan;
- Caspar Gilroy said he was confident the US version of his captive-focused Grafton Insurance Company will be up and running by the end of the year; and
- The former chief executive of Swiss Re UK, Tim Carroll, returned to the London market, taking on a position as a non-executive director of Chaucer Syndicates.

Scott Vincent

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A JULY hailstorm in Calgary is reported to be the costliest in Canadian history. The Insurance Bureau of Canada said the tens of thousands of claims resulting from the July 12 storm have caused an estimated loss of C\$400m (\$382.5m). Local reports described golf ball-sized hail, with at least 55,000 claims subsequently reported. The previous costliest storm was also in Calgary in 1991, which caused an estimated C\$342m of property and motor damage. A storm lasting 30 minutes caused 116,000 claims. In 1996, orange-sized hail caused around \$300m in losses in both Calgary and Winnipeg, with both cities also affected by major flooding.



NEWS IN BRIEF

Pembroke PI product

LLOYD'S syndicate Pembroke has added a specialist professional indemnity (PI) coverage for the oil and gas industry to its portfolio of products. The new product offers protection for people operating throughout the entire oil and gas industry, and can include coverage for high-risk exposures such as pollution, bodily injury, property damage and, subject to review, consequential loss. Pembroke forms part of Ironshore International and the latter company's chief executive, Mark Wheeler, said: "Recent oil spill disasters in the Gulf of Mexico and China's Yellow Sea have heightened awareness of the significant risk exposures surrounding such unexpected incidents and the potential for significant loss within the oil and gas sector on a global basis." Pembroke has extensive knowledge of the PI market, and Wheeler explained this allowed the company to craft "a comprehensive coverage solution in response to the increased insurance risk within the highly specialist oil and gas industry".

Fortress buys 80% of AIG's American General

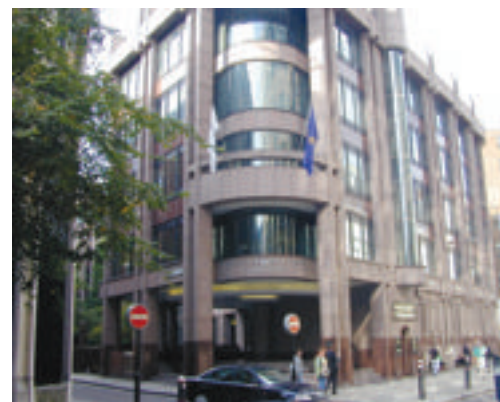
NEW YORK-BASED AIG is to sell an 80% stake in American General to Fortress Investment Group for \$130m, retaining a 20% stake to gain some benefit should the operation recover. The sale will shift \$17bn in debt off AIG's books, reducing the pressure on the parent's capital requirements and removing the danger of having to put more money into the operation to maintain the parent company's credit rating. AIG and Fortress were said to be looking to complete the deal by the end of March 2011, with a major technical challenge being how to maintain American General's credit rating after it loses the implicit backing of its government-owned parent company. Fitch said a sale could imply a downgrade because "new ownership and existing management may potentially seek to engage in some kind of business reorganisation, up to an including a restructuring of the firm's capital structure".

Willis brings in Burns

WILLIS' global placement unit has been strengthened with the arrival of Marsh's Alastair Burns. He takes the role of managing director of Willis' insurance facilities practice, which forms part of the global placement division. Burns joins the company early next month, and will be based in London, where he will report to Dominic Samengo-Turner, the chief executive of the global placement unit.

Madison joins Heath Lambert

ALAN MADISON has joined Heath Lambert's London corporate team in the first step of a significant drive to strengthen its position in the sector. Madison was previously at Aon, where he spent four years developing new business across a wide range of vertical markets in the UK and globally. In his new role, he will report to Judy Baker, head of Heath Lambert's London corporate division, who said: "I want to make sure the London corporate team can evolve by offering great service and products to both existing relationships and prospective clients." Madison's position at Heath Lambert is non-sector specific, thereby giving him the freedom to exploit new opportunities at the corporate level, the company said.



Heath Lambert: strengthening London corporate team