

Agenda Item No.7 (d)

DERBYSHIRE COUNTY COUNCIL

CABINET

22 September 2015

Report of the Director of Finance

**INDEPENDENT INSURANCE SCHEME OF ARRANGEMENT
(COUNCIL SERVICES)**

1 Purpose of the Report

To advise Cabinet on the Independent Insurance Scheme of Arrangement and recommendation of the options for recovery under it.

2 Information and Analysis

2.1 Background

Independent Insurance was a substantial insurance company based in the UK with operations and assets in various jurisdictions around the World. On 13 June 2001, the Company ceased to write new business and went into run-off and on 17 June 2001 was placed in provisional liquidation.

The Company was insolvent and unable to pay its creditors in full. The Provisional Liquidators are proposing a Scheme of Arrangement as a means of making dividend payments to creditors in respect of their claims against the Company ("**Scheme Claims**"). The alternative to the Scheme would be a liquidation of the Company.

Mark C Batten and Dan Schwarzmenn have been appointed as Joint Provisional Liquidators and believe that liquidation would be the less attractive alternative.

The Scheme was approved by a meeting of Creditors held on 1 June 2015 and became effective on 13 June 2015.

2.2 Analysis of Scheme

A Scheme of Arrangement is a way of binding creditors to a proposed compromise in accordance with provisions in the Companies Act 2006. This has become an acknowledged method of administering claims and distributing assets in the insolvency of insurance companies in the UK.

The Council is also a member of the MMI Scheme of Arrangement which was recently triggered. The MMI scheme relates to a reserving scheme of arrangement whereby the company's business remains in run-off in the normal way with interim distributions being paid to creditors with agreed claims. The Independent scheme is an estimation ("cut-off") scheme where creditors are required to submit their claims to the company by a particular date (the "bar date"), after which no more claims can be submitted.

The Bar date will be 180 days after the Scheme is effective.

A dividend will then be paid to creditors in respect of their validated claims.

Since the Company went into run-off it has been agreeing but not paying claims. These claims form the "Unpaid Agreed Claims" category of which the Council has none.

An estimation of contingent claims (incurred but not reported - IBNR) will also be included in the calculation of dividends payable to creditors.

Various elements can be offset by the Company against the claims being made including premiums due and defence costs already paid by the Company. As the Council have registered no claims neither of these are applicable.

2.3 Qualifying Policies Held

Derbyshire County Council had a number of Excess Public and Products Liability insurance policies between 1993 and 1997. These policies applied to individual losses in excess of £2million and were arranged on a joint basis with other insurers (Co-insurance). The exposure was as follows:

Year	Excess Policy	Exposure to Independent	Policy Evidence
1993	£19 million in excess of £2 million	23.81%	Located
1994	£14 million in excess of £2 million	31.83%	Located
1995	£14 million in excess of £2 million	61-66%	There is premium invoice record of this but no policy evidence located.
1996	£14 million in excess of £2 million	61%	There is an insurance broker cover note evidencing this but no policy document evidence located.
1997	£14 million in excess of £2 million	61%	There is premium invoice record of this but no policy evidence located.

Where there is only premium invoice evidence located it is not confirmed that Independent were a party or that the quoted percentage is that applying to them. To obtain formal confirmation contact would be needed with the Council's previous insurance broker Henderson as the Council no longer has some of the original Policy records. Formal confirmation is only needed as evidence for an IBNR claim under the Scheme of Arrangement or if cover was in dispute.

3 Financial Considerations

3.1 Claims Exposure

The Council has, to date, had no individual insurance claims of a level which have been exposed to this excess layer insurance.

Therefore, claims of a latent nature which might form the IBNR exposure fall into a number of categories:

- Alleged abuse or neglect of children or vulnerable adults
- Failure to train or educate
- Work-related stress/bullying/harassment
- Asbestos related: Mesothelioma, pleural plaques, asbestosis
- Noise-induced hearing loss/Industrial deafness
- Hand-vibration syndrome (includes vibration white finger)
- Upper Limb disorders (includes repetitive strain injury)

The individual claim values for each of these are unlikely to breach the primary £2million policy and would have no exposure to Independent policies.

The only realistic potential for exposure above the £2million primary policies might be:

- A series of claims originating from the same source which insurers may argue constitute one occurrence. The Council has not seen anything which insurers have treated on this basis to date but there is the small possibility that systemic abuse claims could be argued as such. Other councils have reported each claimant being treated as a single claim though (even where the perpetrator was the same individual) and advice from the Council's insurance broker is that this interpretation is unlikely.
- A single pollution event (such as Corby). Cover for most of the Independent insured years was limited to "an immediate discharge consequent upon an accident". It is unlikely there would be an insured incident that far back which the Council didn't already know about.

In summary, the overall likelihood of claims occurring now under the Independent Excess Layer Policies is remote. Once any dividends are paid under the Scheme of Arrangement the Council will be its' own insurer for these policies. There is no specific insurance fund provision if any claims occur under these policies with any claim being met from General Reserves. When risk assessing the appropriate level of General Reserve the Council should maintain a view is taken on exposure to uninsured risks.

3.2 Preparation of an IBNR Claim

To produce an actuarially derived IBNR satisfying the scheme requirements and undertake subsequent negotiation with the administrator, the cost of using the Council's existing actuary is anticipated to be approximately £20,000 to £25,000.

Any claim must be submitted to the Scheme administrators by 11 January 2016. It would take a minimum of one month for the Actuary to prepare supporting calculations for any claim.

3.3 Payment under the Scheme

The scheme is likely to pay a dividend of 10p to 15p in the pound for agreed claims.

Comment was sought from the Council's Insurance Fund actuary during the recent Fund Review on the potential of submitting a claim under this scheme.

Advice received suggested that, in order for it to be cost effective there would need to be a single claim in excess of £25m in any one single policy year. This takes into account the actuarial fees that would be incurred in producing such a claim and the actuarial principles that must be applied according to the Scheme rules.

As the maximum excess layer policy limit on any one single year is £19million a claim of such magnitude would not seem possible and the estimated likely recovery is therefore £nil.

The Actuarial Summary advice is included in Appendix A to this report for reference.

4 Other Considerations

In preparing this report the relevance of the following factors has been considered – legal and human rights, human resources, equality and diversity, health, environmental, transport, property and prevention of crime and disorder considerations.

5 Key decision?

No

6 Is it necessary to waive the call-in period?

No

7 Background Papers

Supporting papers are held in the Risk and Insurance Section.

8 Officer's Recommendations

It is recommended that:

- No IBNR claim is made under the Independent Scheme of Arrangement.
- Members accept the position that the Council will become “uninsured” for those insurance policies underwritten by Independent Insurance between 1993 and 1997.

PETER HANDFORD

Director of Finance

1 September 2015

APPENDIX A

Extract from “Independent Actuarial Review of Insurance Fund as at 31 March 2015” carried out by HJC Actuarial Limited.

Interaction with the Independent Scheme of Arrangement

“The Independent Scheme of Arrangement (if approved by the creditors) is an estimation/”cut-off” scheme; if the council does not submit a claim for outstanding and IBNR claims by the Bar Date (December 2015), the council’s policies will be cancelled with no future payments possible. Any claim for such outstanding and IBNR claims must be in a prescribed actuarial format (the estimation Guidelines).

The alternative for the Council is to do nothing, for which its policies would then be cancelled automatically in December 2015.

The estimated scheme pay-out is 15p/£; professional actuarial fees to construct a suitably detailed actuarial report in the relevant prescribed format (including subsequent negotiations with the Scheme Actuarial Adviser and Scheme Adjudicator) are likely to be in the region of £20k-£25k.

Erring on the side of caution, and noting that any scheme pay-out will be at Net present Value (NPV), for the purposes of this report I will assume (e.g. if the Scheme Administrator has underestimated the extent of Independent’s liability) a round pay-out of 10p/£.

Therefore, for it to be cost beneficial for the council to submit a claim for outstanding and IBNR claims (at a total estimated maximum professional fee of £25k) the estimated IBNR must be at least £250k. Given Independent’s c50% share, this would have to be a gross claim of more than £500k, above the primary XS of £2m.

In accordance with the Estimation Guidelines, the probability of such claims must be allowed for. As a working assumption, if I were to assume a probability of 10%, this would require a gross claim of more than £25m (@ 10% probability, this gives £2.5m, i.e. £0.5m above the £2m XS).

Although there is the potential for a Corby-type claim (estimated cost c£10m, perhaps £20m in future monetary values), the policy limit is c£19m (xs £2m), thus £21m is the largest gross claim payable under the excess policies. Even with a higher probability (say 25%, thus a £5m gross claim) this would be apportioned across policy years, thus it is very unlikely that any single policy year would be allocated any amounts above the primary XS, unless the pollution happened gradually over less than 3 years.

Based on the current information, the estimated materiality of likely recoveries is £nil.”

Note: Subsequent correspondence from the Scheme Administrators dated 22 July 2015 has amended the Bar Date to 21 January 2016.