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AP Photo/ Alexandre Meneghini

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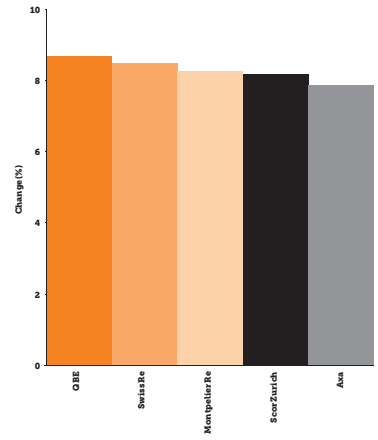

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Market news, data and insight all day, everyday
Insurance Day is the world's only daily newspaper for the international insurance and reinsurance and risk industries. Its primary focus is on the London market and what affects it, concentrating on the key areas of catastrophe, property and marine, aviation and transportation. It is available in print, PDF, mobile and online versions and is read by more than 10,000 people in more than 70 countries worldwide.

First published in 1995, *Insurance Day* has become the favourite publication for the London market, which relies on its mix of news, analysis and data to keep in touch with this fast-moving and vitally important sector. Its experienced and highly skilled insurance writers are well known and respected in the market and their insight is both compelling and valuable.

Insurance Day also produces a number of must-attend annual events to complement its daily output. The London and Bermuda summits are exclusive networking conferences for senior executives; meanwhile, the London Market Awards recognise and celebrate the very best in the industry. The new Insurance Technology Congress provides a unique focus on how IT is helping to transform the London market.

For more detail on Insurance Day and how to subscribe or attend its events, go to info.insuranceday.com

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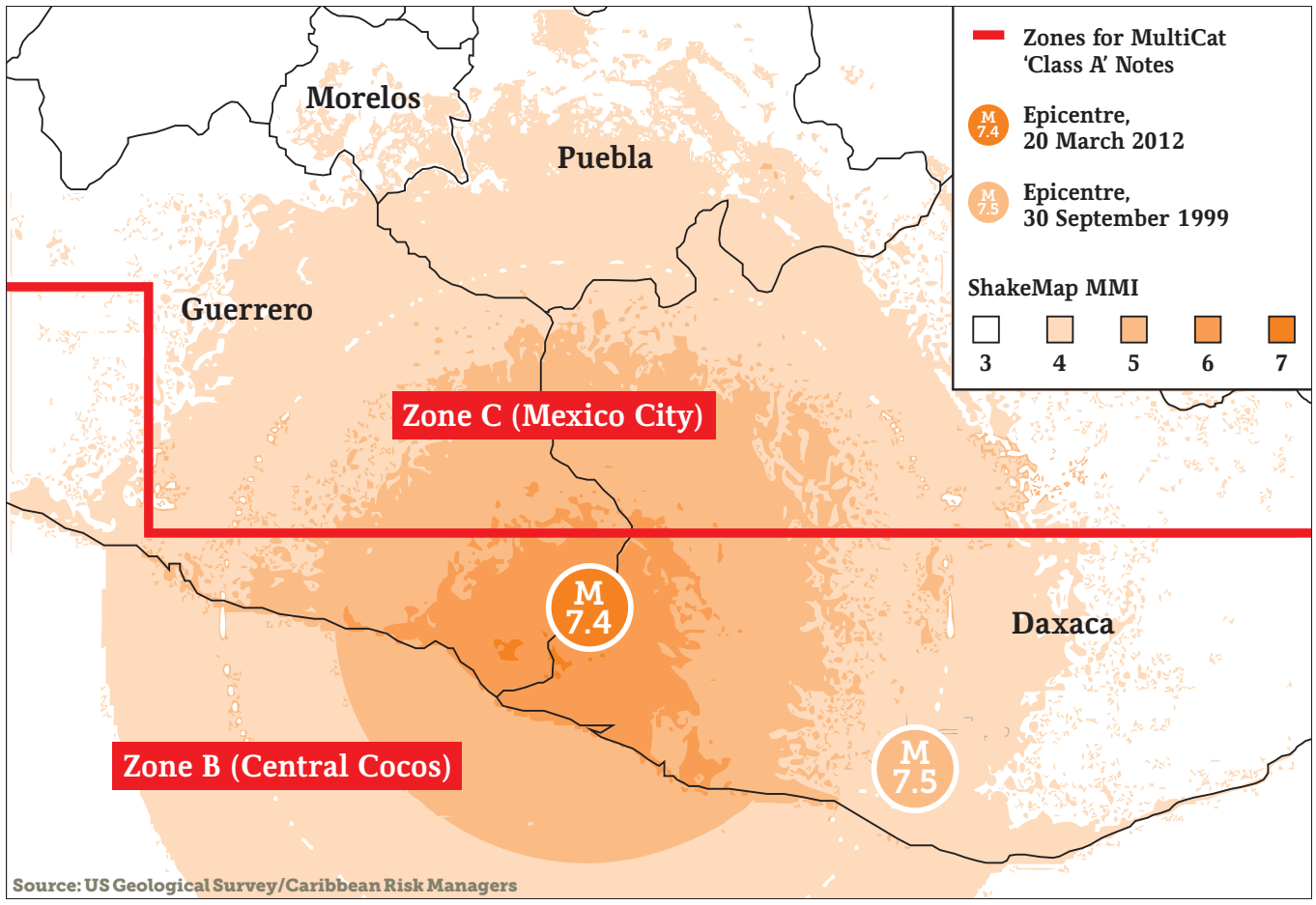


Mexican quake damage must top $300m to trigger Fonden excess-of-loss cover

Scott Vincent
Deputy editor

Infrastructure damage from the magnitude 7.4 earthquake that hit Mexico late on Monday evening would probably need to exceed $300m for the event to trigger Fonden's internationally placed excess-of-loss cover.

Fonden, the division of Mexico's federal government with responsibility for financing recovery from natural disasters, is liable for infrastructure damage to public assets and has a $1bn retention in place before its $400m excess-of-loss cover is triggered. In the policy year to date, close to $600m of this $1bn retention has been used.

Fonden's responsibilities include financial recovery for damage to schools, hospitals, roads, bridges and hydraulic infrastructure. In addition, the Fonden budget also provides cover for low-income households.

Rubem Hofliger, managing director at Fonden, has said he expects further payments to be incurred in relation to damage to hydraulic infrastructure as a result of drought between now and the policy's June 10 renewal, but does not expect these to take Fonden's disaster bill beyond $700m.

This left a major earthquake as the only likely cause of the cover being triggered for this policy year, with both the Atlantic and Pacific hurricane seasons now over.

Monday's quake was of sufficient strength to cause significant damage but the cost of repairs will be limited by the event striking a sparsely populated region in the state of Guerrero, close to the border with the southern state of Oaxaca.

Damage reports from the quake and its subsequent aftershocks were still emerging as *Insurance Day* went to press.

In the region close to the quake's epicentre, 500 houses were reported as damaged to the south-west of Ometepec, a town in Guerrero state. Fewer than 75 were reported in the state of Oaxaca, to the south of the epicentre.

The region immediately surrounding the quake's epicentre is largely unpopulated, with residents primarily rural and relatively poor.

Tao Lai, principal engineer at AIR Worldwide, said most property near the epicentre was constructed of unreinforced masonry, which is not expected to stand up well to the quake.

Residential property damage paid for by the private insurance market will be limited – less than 5% of the 30 million insurable houses in Mexico have cover for natural risks such as earthquakes.

In the first 24 hours following the quake, Axa is understood to have received 25 claims for damage to insured buildings, mostly houses and small to medium-sized enterprises. This includes claims for property and contents damage.

Adjusters have also been appointed to adjust claims for Grupo Mexicano de Seguros (GMX), a Mexican property/casualty insurer, which has received claims for damages to government-owned buildings and a limited number from businesses.

Neither firm has yet given an estimate of their insured loss.

Buildings swayed in Mexico City, 200 miles north of the epicentre, for around 60 seconds as an aftershock followed the quake, but initial indications suggested no major damage had been reported in the Mexican capital.

In addition to its excess-of-loss cover, Fonden also transfers earthquake risks through its MultiCat special-purpose vehicle, which was launched in 2009.

The location of Monday evening's quake was just 35 km away from triggering the MultiCat bond. Although the quake occurred in one of the three defined zones covered by the bond, it was in Zone B, where the magnitude trigger is 8.0. Analysis by Simon Young, chief executive of Caribbean Risk Managers, has shown the quake would likely have triggered the bond had it occurred 35 km to the north in Zone C, where the trigger is magnitude 7.4.

£1bn Lloyd's cash cost from taxation changes

Scott Vincent
Deputy editor

The London market's long-term gain from revised corporation tax measures will be partially offset by the short-term pain of a £1bn ($1.58bn) tax bill spread over the next four years.

While changes to tax rules for claims equalisation reserves and stop-loss and quota-share reinsurance have been well trailed, the latest UK budget report has for the first time put a figure on the likely cost of these changes for the sector.

The changes in stop-loss and quota-share reinsurance address an anomaly in the way corporate members at Lloyd's are taxed and while the change has been expected, the cash cost it will bring is significant.

The exchequer's budgets showed it will be boosted by an increase in tax revenue of £790m during the next four years as a result of this change.

The end to tax relief for claims-equalisation reserves was announced in the chancellor's autumn statement last November.

This has now been costed in the latest budget report and although the government has not costed recoveries of this relief for the next two years, the subsequent three years will see a tax bill of £255m.

Colin Graham, insurance tax partner at PricewaterhouseCoopers, said the London market is well aware of the changes but added the cash cost of the changes is significant.

"This represents a clawing back of relief already obtained by the sector but, at a macro level, the government is taking the best part of £1bn in tax receipts from Lloyd's over the next four years it wouldn't have without these changes.

"The budget has generally provided the insurance industry with good news, but these changes do represent a cash cost to the sector over the next five years."

Insurers urged to take on 'compensation culture'

The latest UK budget has cemented the insurance industry's central role in revamping the country's health and safety climate and chipping away at the so-called compensation culture by demanding insurers take a more robust approach to "vexatious civil claims", *writes Richard Banks*.

The chancellor of the exchequer's full budget document outlined plans to "scrap or improve 84% of health and safety regulation" in the UK, including introducing legislation to reduce the civil law liabilities of employers that take a sensible approach to safeguarding staff welfare.

84%

Of health and safety regulations to be scrapped or improved

George Osborne asked for a commitment from insurers to "challenge vexatious civil claims in order to tackle the compensation culture", and he committed the government to working more closely with the Association of British Insurers to build confidence in challenging such claims and to ensure businesses have access to the right guidance and support.

The government also called on insurers to produce guidance for small and medium-sized firms setting out what is and is not required to demonstrate compliance with health and safety law when obtaining insurance cover as agreed. This was agreed at last month's prime minister's insurance summit.

Tax moves will 'encourage insurers to the UK'

The reduction in corporation tax and evidence of progress on controlled foreign companies (CFC) reform outlined in yesterday's budget are likely to see insurers relocating to the UK – a reverse of the trend seen in recent years – according to a tax expert at PricewaterhouseCoopers (PwC), *writes Scott Vincent.*

Many Lloyd's insurers have moved away from the UK to lower-tax domiciles such as Bermuda, Ireland and the Netherlands after complaining of the onerous tax burden in the UK, but last year Bermuda's Lancashire moved its tax jurisdiction to the UK in response to the CFC proposals.

According to PwC's UK insurance tax leader, Colin Graham, yesterday's budget included a lot of good news for insurers that would contribute to further such moves.

"The chancellor referenced the progress that has been made on the CFC reform debate and the fact more firms are moving to the UK.

"We wouldn't be surprised to see more announcements of insurers' intention to move to the UK in the coming 12 months. The need for certainty for business over tax cost cannot be understated and the only nervousness is around the introduction of a General Anti-Avoidance Rule [GAAR].

"We wouldn't be surprised to see more announcements of insurers' intention to move to the UK in the coming 12 months. The need for certainty for business over tax cost cannot be understated"

Colin Graham
PricewaterhouseCoopers

"There is a difficult balance to strike here – the need to protect tax revenues but also enable businesses to execute commercially driven transactions with certainty."

Chancellor of the exchequer, George Osborne, said there would be further cuts in corporation tax during the next two years, giving Britain a corporation tax rate of 22% by 2014.

He also revealed plans to cut the 50% tax rate for people earning more than £150,000 ($237,654), although as expected these changes will not be implemented immediately.

Osborne said the 50% tax rate was "the highest in the G20" and had a "damaging effect on the British economy".

The rate will be reduced to 45% as of April next year.

NEWS

Vote moves Solvency II a step closer

Scott Vincent
Deputy editor

Solvency II has moved a step closer to reality with the passing of yesterday's Committee on Economic and Monetary Affairs (Econ) vote on Omnibus II paving the way for the first trialogue meeting to take place on April 11.

The trialogue phase of Solvency II preparations now begins, during which the European parliament, the Council of Ministers and the European Commission must consider their respective drafts of Omnibus II and reach an agreed position to put to the parliament plenary vote on July 2.

The Econ vote was passed by majority, with 38 voting for, five against and no abstentions.

According to Nick Lowe, director of government affairs at the International Underwriting Association, today's outcome suggests that a more flexible approach will be made to third country equivalence and an easier transition to the new regime.

"Both aspects are welcome, however we would like to study the wording closely to make sure it really delivers on these promises," Lower said. "Our concern is that London companies with parents outside the EEA should receive fair treatment under Solvency II."

Otto Thoresen, director-general of the Association of British Insurers, said the measures agreed were far from perfect but pave the way for a constructive discussion in the next phase of negotiations on Solvency II.

"We urge the finance ministers, the European parliament and the European Commission to work together in the weeks to address the outstanding issues," he said. "It must remain possible for insurers to continue to deliver products with long-term guarantees that are attractive to consumers. These are products people rely on for their income in retirement.

"The final text must not constrain European insurers from competing successfully in the global market. The issue of equivalence must be resolved for the EU insurance industry to remain competitive and this will be an issue for which we, and our European counterparts, must seek a successful regulatory outcome."

Paul Clarke, global Solvency II leader at PricewaterhouseCoopers, said the vote was important progress which had left the industry "one step closer to having rule certainty.

Chris Ratcliffe/ Bloomberg News

"We urge the finance ministers, the European parliament and the European Commission to work together in the weeks to address the outstanding issues... It must remain possible for insurers to continue to deliver products with long-term guarantees that are attractive to consumers. These are products people rely on for their income in retirement"

Otto Thoresen
Association of British Insurers

"As always the devil is in the detail and the industry will be keeping a close eye on the finer details as they emerge over the coming weeks. In particular, progress on the discount rate, equivalence, transitional measures and reporting thresholds.

Janine Hawes, Solvency II director at KPMG, said: "The industry has won some important battles, including recognition of the need for a mechanism to avoid insurers being forced to sell investments owing to market volatility at a time when their liabilities have not crystallised.

"The existing text includes conditions the US would not be able to meet. Today's version of Omnibus II also maintains the one-year differential between regulators gaining their powers and firms complying with Solvency II, which remains scheduled for January 1, 2014."

The next step is the first trialogue meeting, provisionally scheduled for April 11.

According to KPMG, if a positive vote is reached at the first reading on July 2, there is a strong chance Omnibus II will be able to appear in the Official Journal shortly after parliament's summer recess, allowing the release of the next stages of Omnibus II.

Hardy's board agrees £143m takeover with CNA

Canada's CNA Financial has agreed a £143m ($226.7m) deal to buy Bermuda-based Lloyd's insurer Hardy, *writes Christopher Munro*.

CNA's possible acquisition "significantly expands CNA's global capabilities and aligns well with our specialised underwriting focus", the company's chairman and chief executive, Thomas Motamed, said.

280p
Takeover proposal values each of Hardy's common shares at this amount

Barbara Merry, Hardy's chief executive, will continue to lead the operation following completion of the deal, while Patrick Gage, director of underwriting, will also remain in his position.

The proposal values each of Hardy's common shares at 280p, a premium of close to 37% compared with Tuesday's closing price. And the £143m total represents 1.55 times Hardy's book value at the end of last year.

The agreement with CNA does not come as much of a surprise, with analysts suspecting other would-be bidders were waiting for confirmation of Hardy's 2011 performance before coming forward with official expressions of interest.

Hardy recently posted a pre-tax loss of £42.1m for 2011, compared with £10m profit in the previous year. Blame for the result was laid firmly at the feet of catastrophe claims, with net Thai flood exposures alone accounting for £19.8m of losses.

In December, Hardy undertook a strategic review in light of the expressions of interest it had received from companies like Beazley, as well as the significant catastrophe claims it has incurred in recent years.

Hardy said at the time: "In any transaction which emerges from this strategic review, the board would seek to safeguard the interests of all stakeholders, however, there can be no certainty an offer will ultimately be made for Hardy."

Motamed added: "We are delighted to have reached this agreement. Hardy is a specialist insurer and reinsurer with a respected brand and a long and distinguished history of disciplined underwriting in the Lloyd's market.

"While Hardy's recent results reflect the extraordinary level of natural catastrophe losses across the global insurance industry, the Hardy franchise is built on a strong foundation and has a bright future."

Hardy's chairman, David Mann, said the level of interest shown in his company demonstrates the underlying quality of the business, people and franchise.

And he praised the company's new owners: "CNA is a highly regarded insurer with an international presence and a strong reputation for delivering outstanding client service.

"The board believes that CNA's offer represents the most attractive outcome for our shareholders and will enhance Hardy's business in the interests of our customers, partners and employees."

Asia-Pacific cats see annual loss for Ecclesiastical

Michael Tripp, chief executive of specialist insurer Ecclesiastical, hailed the success of its UK unit after the carrier's exposure to a number of Asia-Pacific catastrophes, including last year's Christchurch's earthquakes, contributed to an annual overall pre-tax loss of £7.7m ($12.2m), *writes Greg Dobie, Sydney*.

The leading insurer of churches and faith organisations saw its UK arm secure an underwriting profit of £7.6m last year in what Tripp described as a "relatively static general insurance rating environment".

Although he said its UK liability account had deteriorated in line with much of the market he attributed the unit's underwriting profit to the success of its new property owners' product in the London market and its growing education account.

Tripp said the insurer is taking underwriting and pricing action to correct increased liability claims in the UK. "These are solid results in a turbulent financial environment and highly competitive insurance market," he said. "We've delivered good growth and profit in the UK while dealing with some of the worst natural disasters our overseas businesses have ever faced."

Ecclesiastical had reported the New Zealand and Japan quakes, combined with the Australian floods and other global disasters, contributed to £419m general business gross claims for the first half of last year, which was higher than its total gross claims cost for the whole of 2010 (*Insuranceday.com*, Aug 25, 2011).

As well as being a significant factor in the its pre-tax loss of £7.7m, compared with £50.4m profit the previous year, this claims burden ensured the carrier's combined operating ratio worsened to 105.4% compared with 102% the previous year.

In addition, Ecclesiastical saw its underwriting loss soar to £16.1m, compared with a £5.9m loss in 2010. This was based on general insurance gross written premiums totalling £465m, which was down on the previous year's £474.4m.

Ecclesiastical's exposure to the Christchurch quakes has also led to it pulling the plug on its church insurer in New Zealand, Ansvar.

After previously saying it would not be renewing policies as they expired at the end of September, it ceased all insurance underwriting operations in the country as of the end of last year, citing "the prohibitive cost of reinsurance" as the main factor behind this decision.

NEWS

Starr Companies receives direct Singapore licence

Unit to write energy, engineering, marine and accident and health

Greg Dobie, Sydney
Managing editor

Starr Companies has received a licence to operate as a direct insurer in Singapore, as it continues to expand its footprint in the Asia-Pacific region.

The Singaporean regulator, the Monetary Authority of Singapore (MAS), granted the licence to Starr International Insurance, a wholly owned subsidiary of Starr Insurance & Reinsurance in Bermuda.

Starr is expected to offer a broad spectrum of risk products including energy, engineering, marine and accident and health, with property/energy representing the key line of business.

It plans to diversify its portfolio by steadily shifting to accident and health, casualty and engineering.

"We are pleased the MAS has granted a full licence and we are confident about the opportunities in Singapore," Ed Navarro, head of international insurance operations for Starr Companies, said.

In addition, Starr has announced the hiring of Chan Tat Yoong as the principal officer of the Singapore operations. The 20-year insurance veteran worked in Singapore's Ministry of Defence before his insurance career.

AM Best has assigned a financial strength rating of A to the carrier, which it said reflected its solid risk-adjusted capital and the support it would receive in terms of underwriting, asset management and reinsurance arrangements from Starr Insurance & Reinsurance.

The rating agency also said Starr International Insurance Singapore would benefit from the management and underwriting expertise provided by its sister company, Starr International Insurance Asia, which was licensed as a general insurance company in Hong Kong three years ago.

AM Best added Starr International Insurance Singapore will primarily generate its business through the existing business network of Starr International Insurance Asia.

Sportscover unveils specialty lines division plan

Sportscover's Lloyd's syndicate 3334 is to launch a specialty lines division early next month, *writes Greg Dobie, Sydney*.

The division will initially comprise the specialist sports and leisure insurer's existing bloodstock and contingency lines of business.

Sportscover said the advent of the division represents part of the carrier's continuing diversification into specialist areas of business and constitutes an important step in the evolution of the syndicate's operations, providing the foundation for future expansion into other complementary areas.

Senior underwriter Robin Blunt will head the team, supported by Ben Wiggins, who will assume the position of contingency underwriter and take on day-to-day responsibility for the contingency portfolio. Ally Halstead will continue in her present role, supporting the team across both classes.

"We have enjoyed tremendous support from brokers over the past few years, enabling us to build a significant and growing book of contingency business. Sportscover is always looking at opportunities to develop other areas of business, so it is therefore logical to bring these specialist lines under one roof"

Murray Anderson
Syndicate 3334

The insurer told *Insurance Day* it intends to develop the syndicate's presence and profile in the existing contingency and bloodstock market and focus on "delivering innovative insurance solutions" in other specialist areas.

Murray Anderson, active underwriter for syndicate 3334, said: "We have enjoyed tremendous support from brokers over the past few years, enabling us to build a significant and growing book of contingency business. Sportscover is always looking at opportunities to develop other areas of business, so it is therefore logical to bring these specialist lines under one roof."

It will launch its specialty lines divisional structure on April 5.

Sportscover's Lloyd's syndicate 3334 was established six years ago to provide a range of tailored products to the sports and leisure industry. Its specifically designed products include personal accident, liability, property, contingency and leisure activities, which it offers across the UK, Europe, Australia and Asia.

Sportscover has recently been expanding the number of countries in which it conducts business in the Asia-Pacific region. The group's main underwriting operations comprise Sportscover Underwriting, syndicate 3334, Sportscover Australia, Sportscover Europe, Sportscover Insurance and SCI Capital.

It has offices in Melbourne, Sydney and the Pacific Islands, as well as a Shanghai operation.

Aviva France sets €10bn turnover target by 2017

Aviva France aims to grow its yearly turnover from €6.1bn ($8.07bn) last year to €10bn within the next five years, which could involve acquisitions, *writes Fabien Buliard, Paris*.

In an interview with French daily *Les Echos*, Philippe Maso y Guell Rivet, head of Aviva France, said France is the group's "second priority market", generating 20% of Aviva's operational profit.

He indicated the company already has several strong distribution partnerships in life insurance and intends to develop its property/casualty (p/c) operations significantly, but added Aviva will not be able to reach its €10bn goal without external growth.

He said the group aims to grow its distribution organically by 20% over the next five years and is "also open to all opportunities that may arise" to go beyond that goal.

However, he also indicated Aviva has not bid for Groupama's brokerage unit, Gan Eurocourtage, which has been up for sale since the end of last year.

Aviva France ambitions

€10bn
Annual turnover within five years

20%
Organic growth in distribution

40%
Of revenue to come from p/c

He explained some of Gan Eurocourtage's segments do not appeal to Aviva, namely its consumer and transport insurance activities.

Aviva France is also seeking to rebalance its business toward non-life activities, as life and savings operations account for 75% of its turnover at present. The company wants p/c activities to generate 40% of its revenue and also intends to boost its presence in the professional p/c segments.

Maso y Guell Rivet is the former head of Axa UK and became chief executive of Aviva France in July of last year. He also serves as underwriting, pricing and product director for Aviva Europe.

WORLD LOSS INTELLIGENCE/LIABILITY

Judgment: Court refuses to refund chemical tanker security payment

CALIFORNIA: Berlian Laju Tanker (BLT) has suffered a major setback in the US, after a federal judge in California rebuffed the company's attempts to secure an immediate refund of the $2.5m security it posted three weeks ago to release the chemical tanker *Partawati.*

US district judge William Alsup ruled on Tuesday the matter is being "held in abeyance" until July 19, to allow plaintiff KPI Bridge Oil to establish its case in Indonesia. "The defendants [BLT] must co-operate in the discovery or else the deadlines may be extended," he said.

Sources familiar with KPI's legal affairs told *Lloyd's List* in Connecticut on Tuesday the ruling was "a major victory. This is exactly what KPI needed to disprove [BLT's] case". As *Lloyd's List* has reported previously, bunker supplier KPI Bridge Oil secured a Rule B attachment against the 2011-built, 21,280 dwt tanker *Partawati* in San Francisco Bay in February, seeking recourse against an unpaid $2.5m fuel bill. BLT posted a $2.5m bond to satisfy the claim and *Partawati* was released the next day. However, BLT's lawyers contested the legality of the arrest and sought a refund of the $2.5m on the grounds the formal shipowner was a leasing vehicle of Standard Chartered Bank and not BLT.

Alsup J's ruling adds to BLT's legal problems in the US, after plaintiff Lantern Maritime last week revived its $55.3m Connecticut lawsuit against the Indonesian group in a charter dispute involving the 2010-built, 25,000 dwt chemical tanker *Wilutama*.

Wilutama, now renamed *Chem Ranger*, is effectively owned by private equity player Delos Shipping. Delos principal, Brian Ladin, told *Lloyd's List* in an interview last week his company's total claim against BLT was $110m, comprising two $55m claims involving *Chem Ranger* and *Chem Bulldog*, formerly named *Pitaloka*.

Ladin said he has chosen to delay the second lawsuit to give BLT a chance to settle out of court, but confirmed Delos would bring the second $55m lawsuit against BLT if the embattled Indonesian group failed to satisfy his claims.

Ladin spoke out after BLT secured a Singapore court order to forestall creditor arrests of its ships, followed by a complementary Chapter 15 order in New York a day later.

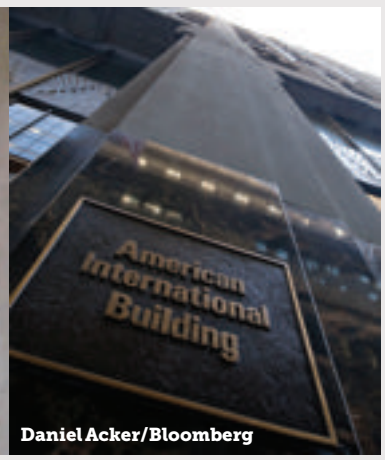
Report by Rajesh Joshi, Lloyd's List

Appeal: Liberty plans challenge to $450m settlement

US: Boston-based Liberty Mutual plans to file an appeal against US district court judge Robert Gettleman's recent final approval of a $450m settlement that AIG is to pay rival carriers for intentionally under-reporting workers' compensation premiums to state regulators for decades, a move that was designed to reduce AIG's premium taxes and residual-market charges.

Liberty Mutual asserts AIG under-reported premiums by $6.1bn, not the $2.1bn assumed in the settlement. Among the companies that approved the settlement were Hartford, Travelers and Ace.

JB Reed/Bloomberg News



Daniel Acker/Bloomberg

Jirau dam damage: Resolution sought through Arias

BRAZIL: Reinsurers are pursuing a resolution through the Insurance & Reinsurance Arbitration Society (Arias) arbitration group for the dispute over claims related to damage to Brazil's Jirau hydroelectric dam.

The dam suffered an estimated $550m in damage following a workers protest last year, which has led to reports of insurers contesting liability to pay claims on the basis the protest was political in nature.

The dispute relates to damage caused by workers at the dam, which is being built in the Amazon basin. The workers set fire to their temporary lodgings and to the buses that transported employees to and from the worksite.

According to local reports, lawyers for Energia Sustentavel, the group building and operating the dam, say the fires were a criminal act and should be fully covered by the insurance companies.

The reinsurers of the primary insurer in Brazil include Allianz, Mapfre, SulAmerica, Itau Seguros and Alianca do Brasil.

IN TOMORROW'S WORL
LIVES & LIV

Y & SETTLEMENTS

2.5m

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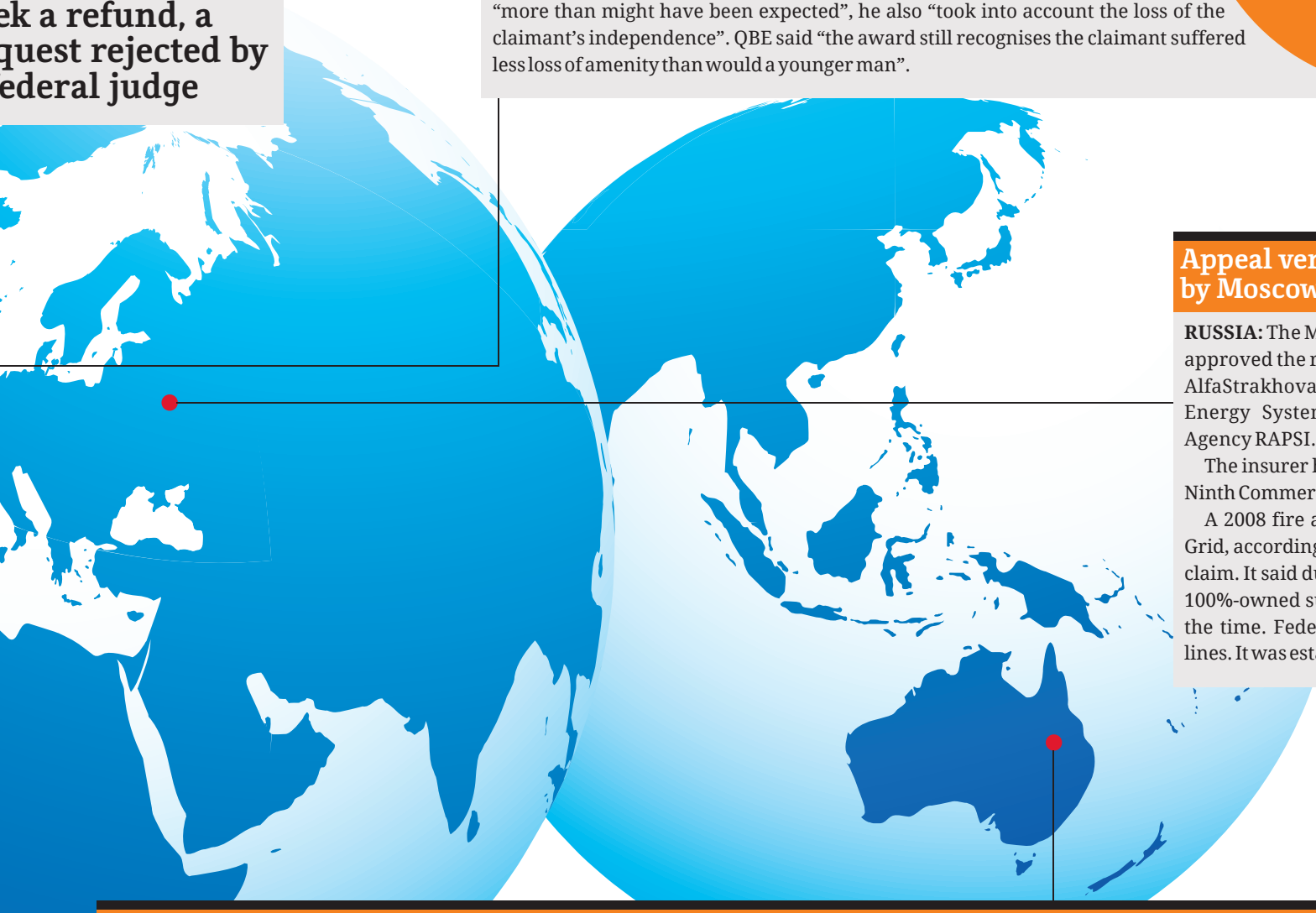
Mesothelioma: Advanced age proves no barrier to significant award

UK: A 92-year-old mesothelioma victim has been awarded £50,000 ($78,000) in a High Court case that hinged on the extent to which the amount of compensation awarded for "loss of amenity" should be less if the claimant is very old.

The former National Coal Board worker was diagnosed as suffering from mesothelioma at the age of 92 and he sought damages for his asbestos exposure. The only area of disagreement was on loss of amenity. The state defendants claimed the claimant's activities were similar to what they were likely to have been had he not been diagnosed with the illness.

The claimant's lawyers argued, although the claimant had a short life expectancy when diagnosed, the illness had deprived him of his independence. The defendants had argued for compensation in the range of £35,000 to £40,000, while the claimants suggested something at the lower end of the range £60,000 to £65,000. In its Technical Briefing this month QBE said, although the judge awarded "more than might have been expected", he also "took into account the loss of the claimant's independence". QBE said "the award still recognises the claimant suffered less loss of amenity than would a younger man".

£50,000
Compensation awarded to 92-year-old mesothelioma victim for 'loss of amenity'



Appeal verdict: $3.68m recovery approved by Moscow district court

RUSSIA: The Moscow District Federal Commercial Court has approved the recovery of $3.68m from locally based insurer AlfaStrakhovaniye by the Federal Grid Company of Unified Energy System, reports the Russian Legal Information Agency RAPSI.

The insurer had appealed against a judgment passed by the Ninth Commercial Court of Appeals in November 2011.

A 2008 fire at a substation damaged the assets of Federal Grid, according to the claimant, but the insurer dismissed the claim. It said during the hearing the accident was caused by a 100%-owned subsidiary that was repairing the substation at the time. Federal Grid controls Russia's main transmission lines. It was established in 2002.

Class action: Wivenhoe dam operator faces legal challenge

AUSTRALIA: Sign-up is gathering pace for a planned class action on behalf of any businesses, community groups and householders downstream of the Wivenhoe dam (*pictured*) in Queensland that were flooded last year.

The action relates to the failure of the dam operators to escalate their flood mitigation strategy on January 8 and 9 last year.

Engineers are alleged to have misled a subsequent inquiry over their management of the dam ahead of the floods that inundated Brisbane and Ipswich, with their oral testimony now being questioned.

Rod Hodgson, partner at law firm Maurice Blackburn, which represents victims of the disaster, said: "The dam operators did not release enough water early enough and that meant far too much was released later on. The operators failed to take account of rainfall forecasts at key times.

"The inquiry also found opportunities may have existed for earlier releases of water. The findings of the inquiry give hope to those wanting to be part of a potential class action."

The law firm said it needs to undertake more investigation work ahead of any potential class action and it has teamed up with national litigation funder the International Monetary Fund "to commit to those investigations".

"This potential class action is on behalf of any businesses, community groups and householders downstream of the Wivenhoe dam and which were flooded," Hodgson said.

"The inquiry found the possibility existed of at least some improvements in the flooding outcomes for Brisbane and Ipswich.

"As sign-up for the potential class action gathers pace, our efforts to gather further evidence focus on independent hydrodynamic modelling to show how much of a difference the proper operation of the dam would have made."

LD LOSS INTELLIGENCE: VELIHOODS

FINANCIAL WORLD TODAY

Insurers benefit from market confidence in wake of bank stress tests

Japanese groups also gained from the significant reduction in recent months in their exposure to the sovereign debt of vulnerable eurozone countries

Rasaad Jamie
Global markets editor

Federal Reserve: outcome of bank stress tests and FOMC announcement boosted stocks

Insurance and reinsurance stock prices, under heavy pressure over the previous three or four weeks, recorded strong gains, mainly as a result of developments in the broader market, which boosted stocks across the board but which particularly favoured financial sector stocks such as banks, with insurance sector stocks very much benefiting from the association with banks in the minds of investors.

Federal Reserve announcements

These market developments were driven by two announcements from the US Federal Reserve Bank: the release by the Fed early in the week of the results of the stress tests on US banks' capital adequacy, which the vast majority of the largest US banks passed; and the announcement by the Fed's open market committee (FOMC), confirming the accelerating pace of the US economic recovery and its decision to leave interest rates unchanged.

The FOMC, while acknowledging the recent marked improvement in US employment figures, however, expressed concern about the continued high number of Americans who remained unemployed. The FOMC also maintained interest rates but unlike on previous occasions, it did not reconfirm its willingness to implement further quantitative easing measures should they be necessary.

In the context of the market volatility of recent months, a statement along these lines by the Fed was more or less guaranteed to boost the markets by at least a few points. But the Fed's reservations about the unemployed and the omission of any reference to quantitative easing was soon forgotten by the release on the same day of US retail sales figures for February, which recorded their largest gain in five months despite rising petrol prices; a sign, if any, of the increasing resilience of US consumer confidence.

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Banks stress tested by the Federal Reserve passed, out of a total of 19

Stock values boosted

This developments significantly boosted stock values over the course of the week, not only in the US but also in Europe and particularly in the export-orientated economies of Asia, including the stock values of regional insurance groups.

In Japan, the financial market profile of the biggest insurance groups also benefited from the significant reduction in their exposure to the sovereign debt of vulnerable eurozone countries during the fourth quarter of last year. These insurers reduced their holdings Greek, Portuguese, Irish, Italian and Spanish bonds by 47% over the quarter.

Nippon Life, which had by far the biggest exposure, reduced its so-called PIIGS exposure from ¥450bn($5.35bn) to ¥200bn. Mitsui Life said it sold all its Italian sovereign debt in October. Apparently, the strategy behind the sell-off was to dispose of such holdings at a time when it was still possible to compensate for the losses from these deals with profits from other areas of the insurers' operations.

Capital positions

According to the Fed, 15 of the 19 US banks tested would have enough capital even if they suffered a financial shock that saw unemployment reach 13% and housing prices drop 21%. The message, according to one Fed official, was the capital positions of US banks had improved substantially in the past three years. Indeed, the stress tests were introduced by the Fed in 2009 to allay widespread fears about the perilous state of banks' balance sheets.

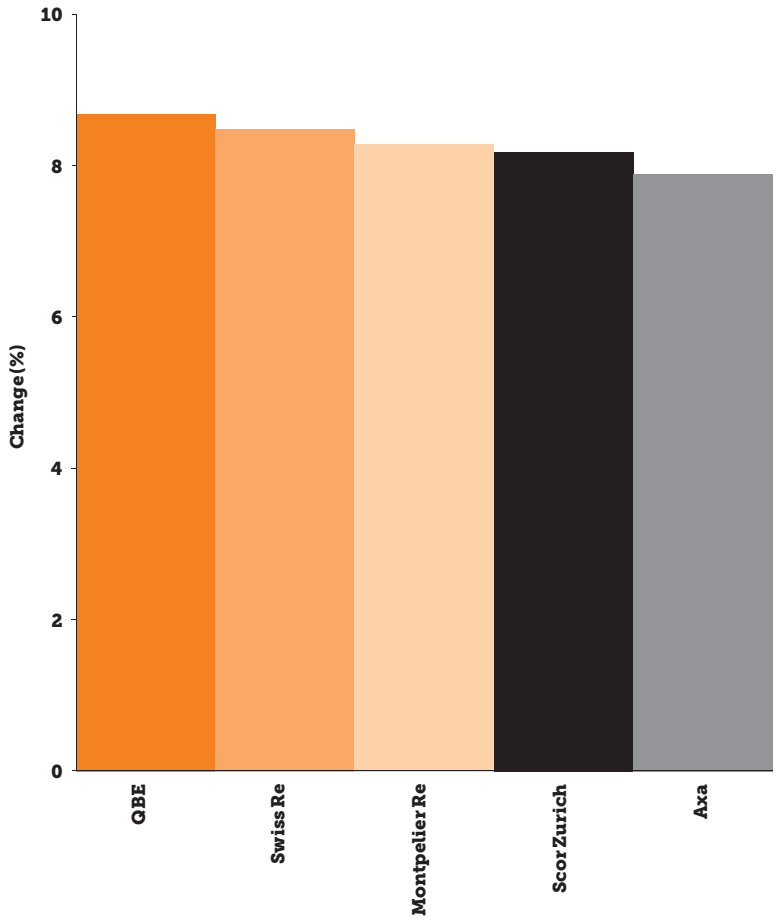
Table: Share prices as at close March 15, 2012

Company/group	Currency
Ace	US dollar
AIG	US dollar
Alleghany Corporation	US dollar
Allianz	Euro
Allstate	US dollar
Alterra	US dollar
Amlin	Pence
Arch Capital	US dollar
Aspen	US dollar
Aviva	Pence
Axa	Euro
Axis Capital	US dollar
Berkshire Hathaway (A)	US dollar
Catlin	Pence
Chubb	US dollar
CNA Financial	US dollar
Endurance Specialty	US dollar
Everest Re	US dollar
Generali	Euro
Hannover Re	Euro
Hiscox	Pence
Insurance Australia Group	Australian dollar
Korean Re	South Korean won
Montpelier Re	US dollar
MS&AD Insurance Group	Yen
Munich Re	Euro
NKSJ Holdings	Yen
PartnerRe	US dollar
Platinum	US dollar
QBE Insurance Group	Australian dollar
RenaissanceRe	US dollar
RSA	Pence
Scor Paris	Euro
Scor Zurich	Swiss franc
Swiss Re	Swiss franc
Travelers Companies	US dollar
Tokio Marine Holdings	Yen
XL Group	US dollar
Zurich Financial Services	Swiss franc

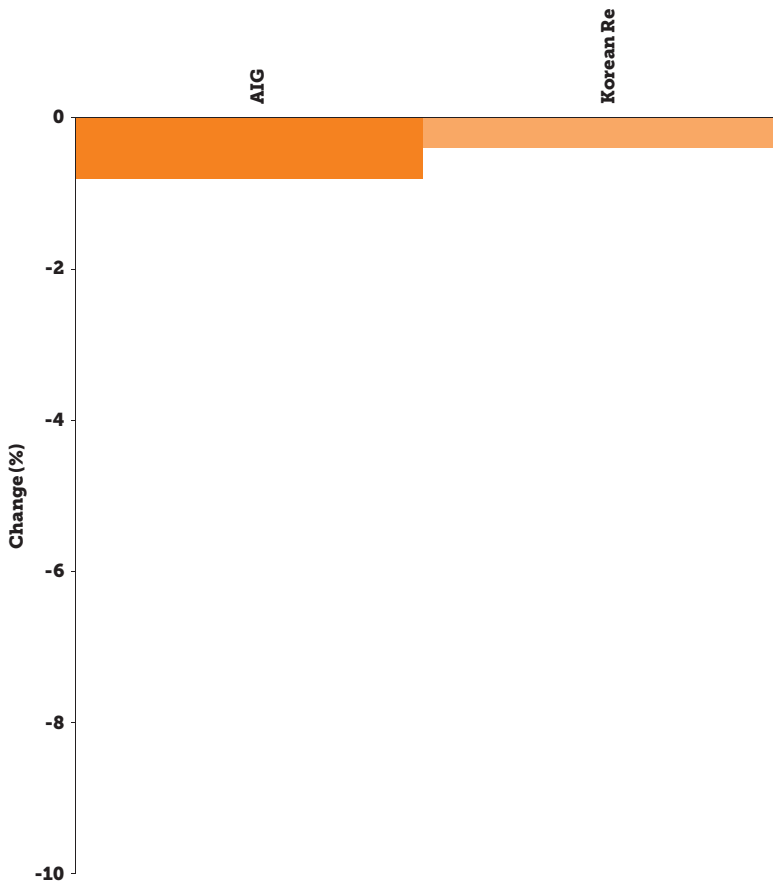
Source: Insurance Day

Dec 31, 2011	Mar 8, 2012	Mar 15, 2012	Change from Mar 8 (%)	Capitalisation ($m)
70.12	71.49	73.37	2.6	24,737
23.20	28.31	28.08	(0.8)	53,264
285.29	323.31	338.80	4.8	2,897
73.43	88.60	92.30	4.2	54,935
27.41	31.24	32.59	4.3	16,239
23.63	23.00	23.49	2.1	2,451
313.90	338.60	350.60	3.5	2,734
37.23	36.83	37.22	1.1	4,994
26.50	26.76	28.22	5.5	1,997
300.80	356.80	374.90	5.1	16,534
10.05	11.98	12.93	7.9	38,774
31.96	31.68	32.88	3.8	4,302
114,755.00	118,430.00	122,000.00	3.0	114,192
398.70	420.30	421.90	0.4	2,382
69.22	67.35	68.65	1.9	18,613
26.75	28.38	29.68	4.6	7,994
38.25	37.66	39.12	3.9	1,585
84.09	90.35	93.31	3.3	5,014
11.63	12.78	13.03	2.0	26,405
38.30	41.29	42.35	2.6	6,688
373.50	410.00	413.50	0.9	2,473
2.98	3.20	3.37	5.3	7,356
15,000.00	13,950.00	13,900.00	(0.4)	1,408
17.75	17.97	19.46	8.3	1,184
1,426.00	1,706.00	1,786.00	4.7	9,024
94.59	108.25	115.00	6.2	29,727
1,510.00	1,912.00	2,011.00	5.2	38,104
64.21	63.29	66.22	4.6	4,330
34.11	36.44	37.05	1.7	1,316
12.95	11.96	13.00	8.7	14,119
74.37	72.40	74.62	3.1	3,843
105.20	109.00	114.10	4.7	6,187
18.06	20.20	20.69	2.4	4,989
21.50	23.10	25.00	8.2	5,092
47.87	54.40	59.05	8.5	23,749
59.17	57.10	59.08	3.5	23,223
1,705.00	2,189.00	2,313.00	5.7	21,849
19.77	21.00	21.88	4.2	6,907
212.50	231.00	242.00	4.8	38,696

Graph: This week's winners...



...and losers



The Fed had not forgotten the stress tests were as much a public relations exercise as they were part of a necessary process of financial due diligence in the wake of the financial crisis. More than one commentator said the Fed failed enough banks to give the tests credibility (Citigroup, the third-largest bank in the US, notably failed) and at the same time reassure the markets that the banking sector was well capitalised.

Importantly for banks, along with the pass mark from the Fed came permission to increase dividends to shareholders and to buy back stock. So, for example, JP Morgan Chase, one of the top performers in the stress tests, was given permission to raise its dividend 20% and to spend up to $12bn buying back stock in 2012.

MetLife

The other notable failure was MetLife, the largest life insurer in the US and the only insurer to be subjected to the stress tests because it is deemed a bank holding company by the Securities and Exchange Commission because of its ownership of MetLife Bank, an online retail operation MetLife has been trying to dispose of (without much success) since July last year.

According to the Fed report, MetLife failed the stress tests as a result of its risk-based capital ratio, which, at 6%, was the lowest of all the banks tested.

On the day it was announced it had failed the stress test, MetLife's stock price promptly dropped 6%, the biggest fall on the S&P 500. This was largely because the Fed promptly refused MetLife's request to increase its dividend 50% and to implement a $2bn share-buyback programme.

A number of the bigger US insurers, to be defined as non-bank systemically important financial institutions, are expected to be subjected to the Fed's stress tests in future. As part of the Dodd-Frank regulatory changes, a list of such companies will be announced later this year. ■

LAW & ORDER

No easy ride for non-executive directors

Recent guidance from the Cayman Islands sheds light on non-executive directors' responsibilities

Lauren Sadler-Best, barrister
Trott & Duncan Bermuda

Being a non-executive director of an offshore company sounds like an attractive proposition, but few would like to be in the shoes of the directors of Weavering Macro Fixed Income Fund (WMFIF), who were lambasted in court as follows: "In spite of the fact the directors obviously appreciated the Western world was in the middle of a serious financial crisis, they continued to go through the motions of holding meetings and [Hans] Ekstrom continued to sign minutes designed to give the impression they were functioning as a board of directors, whereas in reality they had not read the materials sent to them and had made no attempt to understand the Macro Fund's financial condition."

Damning statements

These are just a few of the very damning statements made by the court against Stefan Peterson and Hans Ekstrom, directors of WMFIF in the recent Cayman Islands case of *Weavering Macro Fixed Income Fund (in liquidation) v Peterson and Ekstrom (Weavering)*.

Having found the directors were aware of their "high-level supervisory role" but did nothing to fulfil it for almost six years, the court determined the directors' neglect was intentional and using this test of intent as established in *Re City Equitable Fire Insurance* (1925), the directors were found guilty of wilful default in fulfilling their duties.

What does this case mean for independent directors and how have their duties changed?

Non-executive directors such as Peterson and Ekstrom do not hold executive or management positions with the company. They are independents appointed to sit on the company's board to, in the words of The Cadbury Report 1992, "bring an independent judgment to bear on issues of strategy, performance and resources".

The traditional view has been a non-exec is not expected to devote all his time and attention to the company's management or to be an expert in the company's business. Indeed, non-execs usually have other full-time responsibilities. They are therefore entitled to rely on the expertise of those in management and those to whom certain functions have been delegated.

This was recognised in the *Equitable Fire* case, where it was determined a director need not exhibit greater skill than may be expected from someone with his knowledge and experience. He is not bound to give continuous attention to the company's affairs. His duties are intermittent and are performed at periodical board meetings. In respect of all duties that pursuant to the company's articles can be left to someone else, the director is entitled, in the absence of suspicion, to trust that official to perform his duties honestly.

This is, however, subject to the superseding principle all directors, including non-execs, must attend to the company's affairs diligently. This principle has more rigidly been applied in modern cases such as *Dorchester Finance Co v Stebbing* (1989), where the court held the rule in *Equitable Fire* related only to skill, not to diligence. With respect to diligence, what was required was "such care as an ordinary man might be expected to take on his own behalf".

Taking it a step further, the court in *Equitable Life Assurance Society v Bowley and others* (2004) found to the extent *Equitable Fire* is relied on to support "unquestioning reliance" on others, this does not represent modern law. *Citing Re Barings plc (No 5)* (2000), also cited in *Weavering*, Justice Langley found while directors are entitled to delegate particular functions to management and to trust their competence and integrity "to a reasonable extent", the directors are not absolved from their duty to supervise the discharge of the delegated functions.

Boardroom: non-executive directors' responsibilities have been clarified by the court's decision in Weavering

While directors are entitled to delegate particular functions to management and to trust their competence and integrity 'to a reasonable extent', the directors are not absolved from their duty to supervise the discharge of the delegated functions

Altering non-execs' position

Has *Weavering* altered the position regarding non-execs?

The principles applied in *Weavering* are not novel. *Weavering* does not so much mark the evolution of directors' duties as highlight those duties. What is clear is the tradition that has developed, whereby boards of directors delegate nearly all of their power to the top executive employees and adopt the recommendations of those employees almost without fail, will no doubt come under greater scrutiny.

In fact, the role and duties of directors have attracted even more attention with the recent explosion of litigation worldwide, arising from the numerous hedge fund collapses, and is now the subject of widespread corporate governance reform.

The relevant lessons to be learned from *Weavering* with regard to delegation and reliance (and the recent cases preceding it), therefore, may be summarised thus:

1) While directors are entitled to delegate management and administration functions, they must maintain a high-level supervisory role;
2) Therefore, notwithstanding the directors' lack of expertise, they must satisfy themselves those charged with various duties fulfil them in accordance with their respective contracts. They are not entitled to assume this;
3) Directors must acquire sufficient information to understand the company's financial position and to satisfy themselves the company is complying with the relevant investment restrictions;
4) Directors must act independently; and
5) Directors who make a concerted attempt to perform their duties are likely to be protected by any indemnity offered in the company's bylaws in the event of negligence.

Watch this space

There can be little doubt the facts of *Weavering*, though not unheard of, are unusual. The court found the directors of *Weavering* did nothing throughout the life of the fund and the board's sole purpose was to appease Magnus Peterson, the fund's investment adviser (brother to director Stefan Peterson and father-in-law to director Hans Ekstrom) and to rubber-stamp his decisions.

In less extreme cases, how *Weavering* will be applied remains to be seen. It is clearly an important development for directors' and officers' liability underwriters to watch carefully. In any event, in light of the expected volume of hedge fund litigation, *Weavering* will undoubtedly soon receive greater judicial attention. ■

US appeals court rebuffs judge rejecting SEC settlement with Citigroup

Mark Leimkuhler, partner
Lewis Baach, Washington DC

A US appeals court in New York has criticised a trial judge's rejection of a US Securities and Exchange Commission (SEC) settlement of allegations against a unit of Citigroup.

The trial judge had rejected the settlement primarily because the unit, Citigroup Global Markets (Citigroup), had neither admitted nor denied liability.

Last week's ruling stayed trial proceedings while the appeal is pending because "the SEC and Citigroup have made a strong showing of likelihood of success in setting aside the district court's rejection of their settlement". Corporate executives and their insurers are closely watching the appeal.

Last October, the SEC sued Citigroup for alleged securities law violations in marketing collateralised debt obligations and simultaneously filed a proposed consent order to settle the allegations. This is a common practice in US securities enforcement.

However, district judge Jed Rakoff rejected the proposed settlement, saying he could not determine whether it was in the public interest without "proven or admitted facts" concerning Citigroup's liability. Both the SEC and Citigroup appealed.

The trial court's ruling sparked a debate about judicial approval of SEC settlements. Some said requiring an admission of liability would preclude settlements and increase litigation, squeezing regulatory budgets and exposing corporations to greater potential liability and legal expenses.

This would make it harder for companies to acquire directors' and officers' (D&O) liability insurance and would upend pricing assumptions of D&O insurers. Others said Rakoff was right to press the SEC to obtain admissions of liability that could help investors recover losses in private litigation and avoid settlements that were "costs of doing business" rather than genuine disincentives to improper conduct.

The Second Circuit panel determined Rakoff had improperly prejudged whether Citigroup had misled investors and whether the SEC could prove that at trial. The panel also found troubling Rakoff's failure to give deference to the SEC on "wholly discretionary matters of policy" because courts should not "dictate policy" to government agencies.

It also found no precedent to require regulators to present "proven or admitted facts" in settlements which are often, by their nature, compromises of opposing views about the facts.

The panel's ruling is not the final word in the appeal; that will be up to a separate panel. But the finding the appeal has a "strong likelihood of success" signals a probable reversal of Rakoff's decision, which would eliminate the uncertainty his ruling has created for D&O insurers and their insureds. ■

Professional indemnity insurers lose out

Leon Taylor, insurance and reinsurance partner
DLA Piper London

Just as the UK's Financial Services Authority (FSA) is increasingly requiring financial institutions to take active steps to compensate customers in cases of mis-selling, insureds risk falling between a rock and a hard place vis-à-vis their professional indemnity (PI) insurers: the cost to an insured of "doing the right thing" by customers may not always be recoverable under its PI cover.

In *Standard Life Assurance v Ace European Group and others*, the High Court has provided policyholders with some relief – to the frustration of insurers. The claim concerned allegations of mis-selling against Standard Life in relation to one of its pension funds.

Following the collapse of Lehman Brothers in 2008, Standard Life switched to a different valuation model for the fund, which caused it to lose 4.8% – close to £100m ($158.6m) – of its value overnight. In response to a mass of complaints from investors, Standard Life decided to restore the value of the fund rather than deal with claims individually, which it considered would prove more expensive in the long run.

Standard Life's PI policy included cover for "any payment of loss, costs or expenses reasonably and necessarily incurred… in taking action to avoid a third-party claim or to reduce a third-party claim".

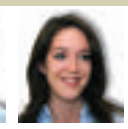
Standard Life claimed its £100m cash injection to restore the fund was covered as a mitigation cost. Insurers disagreed because one of the reasons for restoring was to protect Standard Life's brand. The court rejected insurers' arguments: the proper approach was to consider the intended effect of the payment. Standard Life's subjective motive for it was irrelevant.

Even if the payment benefited Standard Life's reputation, if its intended effect was at least partly to avoid or reduce claims, the policy responded. After all, the policy did not require mitigation costs to be incurred "solely" or "exclusively" to avoid claims.

The court also rejected insurers' suggestion the loss should be apportioned to reflect the different purposes of the payment. While valid in marine insurance, the court was very doubtful apportionment could play a role under a liability policy. Insurers also lost an aggregation argument with the result a single deductible applied to all the customer claims.

While the insured was successful in this case, disputes like this usually turn on the particular wording of the insurance policy. The decision may encourage insurers to consider whether to tighten mitigation costs wordings so only expenses made "solely" or "exclusively" to reduce losses are recoverable. ■

Sanctions – the exercise of due diligence

CLYDE&CO

Insurers have long dealt with a variety of economic sanctions – for example, against designated individuals.

Since 2010, there has been a step change in line with EU sanctions targeting insurance of a much broader range of individuals and entities in a country and of products – first Iran, then Syria and most recently the European Council decision in January 2012 targeting insurance related to the import, purchase or transport of Iranian crude oil, petroleum and petrochemical products.

The council decision will be implemented by an EU regulation in the next few weeks and this might clarify important aspects, for example, whether protection and indemnity (P&I) insurance can be provided by an EU insurer in respect of a lawful voyage from Iran to Asia not involving an EU-owned vessel.

The existing sanctions against Iran include a prohibition on the insurance of entities that are directly or indirectly owned or controlled by Iranian individuals, entities or bodies. So an EU insurer cannot insure a company anywhere in the world if, for example, its parent company is Iranian or if Iranian individuals exercise control over the company's board.

The prohibition is absolute, but an insurer has a defence against liability if it does not know and has no reasonable cause to suspect it would be in breach. We anticipate a similar defence being available in the forthcoming EU regulation.

So what is due diligence? Much depends on context but a recent insurance case, *Sealion Shipping v Valiant*, might offer some guidance. In the context of a standard hull policy wording the court equated the phrase "due diligence" with reasonable care.

How much due diligence is reasonable? It is a flexible yardstick, which depends on the circumstances of each risk. There is no "one-size-fits-all" guidance that can cater for every eventuality.

A Middle Eastern company seeking export cover requires much closer underwriting scrutiny than a householder in Devon wanting motor cover or a US trucking company involved in purely US transits. Different procedures are also needed for risks that are not individually underwritten, such as those bound under delegated authorities or treaty reinsurances.

Due diligence is required not merely at the underwriting stage, but every time an insured is added or endorsement made to a cover. It extends beyond the underwriting process to claims. Clearly, no payment should, in principle, be made to an Iranian entity.

Practical ways to ease the burden more generally include making sure the broker provides full information (at every stage) and incorporating a suitable sanctions clause in the insurance contract. Neither of these is, however, a substitute for an insurer's own obligation to exercise due diligence.

Less obvious examples include where claims authority is delegated to a third party, for example, a third-party administrator or a broker in respect of lower-value claims. An insurer needs to consider what steps it should reasonably take to ensure the third party has correctly applied the sanctions legislation and to document those steps.

Practical ways to ease the burden more generally include making sure the broker provides full information (at every stage) and incorporating a suitable sanctions clause in the insurance contract. Neither of these is, however, a substitute for an insurer's own obligation to exercise due diligence.

Excellent guidance is available in Lloyd's recent Market Bulletin Y4560, addressed to managing agents, although ultimately every insurer has to determine its own due diligence procedures. ■

Mike Roderick is a partner and Henrietta Wells an associate at Clyde & Co