

## SPECIAL REPORT: RUN-OFF

# Support grows for solvency schemes

By Richard Banks

IN a world where insurance run-off has become a respected industry in its own right, several solutions promising to bring finality to shareholders and fair recompense to policyholders have emerged.

While there are proponents for solutions such as reinsurance or sales of closed books of business, the most widely discussed — some might say controversial — process is the solvent scheme of arrangement. Essentially, solvent schemes of arrangement, which developed from the concept of insolvent schemes of arrangement used to run off failed companies, allow administrators to close run-offs more quickly and therefore more cheaply than traditional run-off.

Inevitably, they are slower to bring finality sales or reinsurance but do bring complete finality in a way that reinsurance in particular does not.

## Scheme deadline

Schemes, which for statutory reasons cannot be used for employers' liability business in the UK, work effectively by setting a bar date by which all claims must be filed — in most cases this deadline is 90 days from the date the scheme becomes effective. So the run-off is completed much more quickly than under traditional methods. In fact the run-off duration, which for some companies might be more than 10 years, can be cut to a matter of a couple of years.

But practitioners promoting schemes of arrangement are keen they should not be seen as a panacea for all ills.

Mike Walker, a partner at KPMG, which has a number of schemes of arrangement in development, urges against complacency. In a presentation in London earlier this month he echoed the caution expressed in an article in *Insurance Day* by his KPMG colleague Tony McMahon (*ID*, Sep 24). Mr Walker identifies a feeling among some policyholders — notably in the US — that some schemes are rather "scams of arrangement", doing little to offer protection to the policyholder and instead focusing on the concerns of shareholders. In his article Mr McMahon highlights some specific concerns about schemes, including:

- An unreasonably short notice period for submitting claims

- Insufficient effort being made to contact policyholders
  - Inability to understand clearly from the scheme document what books of business are actually being schemed
  - The ability for the company promoting the scheme to abandon it should the claims not be to its liking
  - Lack of transparency in the role of the advisers and how they are remunerated
- "The danger is that all schemes are seen as 'scams'," Mr Walker warns, claiming there is already evidence some policyholders are so disillusioned with the concept of schemes that they automatically reject them. According to Mr Walker, it is not sufficient for scheme arrangers to ignore such concerns. "It's important the market takes these things seriously. Dealing with these issues will enhance the reputation of schemes."

Dan Schwarzmann, a partner in the solutions for discontinued insurance business team of PricewaterhouseCoopers (PwC) indicates the sea change there has been in awareness of schemes in recent years. Mr Schwarzmann is regarded as something of a pioneer in the realm of solvent schemes of arrangement. He says: "We've just finished a couple of detailed feasibility studies on companies in the market that are thinking about doing

schemes — they're not the largest that have been issued but they're certainly in the top quartile — and we've been going around talking to policyholders to see if they would be receptive to the idea.

"We've not had one person asking what a scheme of arrangement is. That's a huge change over a couple of years ago. Furthermore, there has been resounding support for these proposed schemes of arrangement and the benefits they produce."

## Not suitable for all

Mr Schwarzmann emphasises schemes of arrangement do not work in all instances and are not suitable for all run-offs. He says they should be seen not as an overarching solution, rather each scheme should be considered an individual deal. Still, he acknowledges there is often some commonality between schemes as the process of drawing them up has evolved.

Schemes have even been put forward where liabilities such as asbestos are involved. Again Mr Schwarzmann urges caution: "I'm not saying that if you've got asbestos liabilities, [a scheme] is definitely going to work." But equally he says that just because a client has asbestos liabilities on his or her books, this is no reason not to consider a scheme.

PwC's analysis of the response to its schemes suggests it has been successful in



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winning over clients. For a scheme to get court approval the administrators need to demonstrate it has the support of a majority of policyholders on two counts: 50% by number and 75% by value of claim. According to Mr Schwarzmann, PwC's analysis indicated its schemes have received support from policyholders on both counts averaging 98%. "You can't keep

issuing schemes and getting that sort of result if the market is not receptive," Mr Schwarzmann tells *Insurance Day*.

And he says on every scheme there are likely to be policyholders who have been creditors on other schemes, so the strong approval rate indicates some degree of satisfaction with existing schemes as well as reflecting the relationships built up between scheme administrator and policyholder, which he describes as "one of the most important things about schemes". Still, he stresses that with each scheme there are individual concerns that need to be addressed.

## Addressing concerns

Nigel Montgomery, head of the insurance and risk solutions group at law firm DLA, agrees that policyholder concerns that could prevent potentially successful schemes in the future must be addressed. He says: "[Schemes are] a technique for closing discontinued business — and, like any technique, as it evolves some aspects work better than others, and those that do schemes self-correct and learn as they go on."

Mr Schwarzmann, who alongside colleagues from PwC has been behind 34 of the 40 schemes issued so far, defends the process from some criticism. In particular, some commentators have queried whether setting a bar

date for claims 90 days after a scheme comes into force allows enough time for policyholders to submit their data.

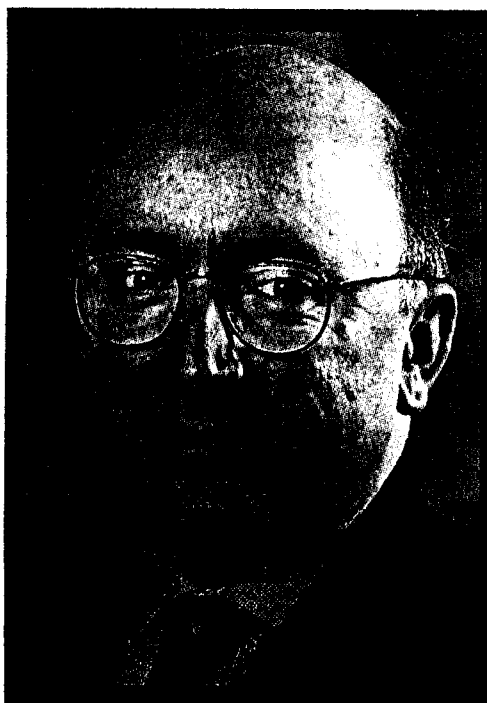
## Policyholder involvement

He responds by saying policyholders will have generally been involved in the negotiations well before the scheme is scheduled to come into force officially. But he is adamant that on those occasions a 90-day deadline might not be sufficient, alternative arrangements should be made.

"If 90 days is too short, that will be extended if that's what policyholders want."

According to DLA's Mr Montgomery, there also has to be some thought given to how much notice is given to creditors when the scheme is originally mooted. He suggests six to eight weeks' notice for meetings but acknowledges that in cases where there is a small number of creditors that are easily identifiable and in a close geographical area less notice time could be possible.

Mr Schwarzmann defends provisions in schemes that allow the possibility of a reversion to run-off as protection for the policyholder as well as for the shareholder. "You could issue a scheme where suddenly there's some litigation which makes the scheme inappropriate for the policyholder," he says. In such cases the reversion to run-off provision offers protection to the policyholder.



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