Willis Towers Watson

Insight
Insolvency & Restructuring

Q2 2016

Welcome to our first Insight of 2016. The year started off with a bang for us as we announced our new company following a merger with Willis Group Holdings and Towers Watson and despite the relatively low level of formal insolvencies in the economy we continue to see a strong flow of referrals across a broad range of sectors. 2016 has plenty more in store however, on the 12th August the new Insurance Act comes into force and the well-publicised end to the insolvency carve out in the Legal Aid, Sentencing and Punishment of Offenders Act 2012 ("LASPO") took effect on the 6th April. This quarter we will provide guidance around these issues and other risk matters which are currently affecting the Insolvency & Restructuring industries.

Welcome to Willis Towers Watson

A Truly Compelling Combination

A strong client focus, an emphasis on teamwork, unwavering integrity, mutual respect and a constant striving for excellence are the values at the core of the new Willis Towers Watson organization.

39,000 colleagues in **120+ countries**

Scale, diversity and financial strength **$8.2 billion revenue**

A deep history dating back to **1828**

We Aim to Be the Leading global advisory, broking and solutions company.

We have relationships with:

The 5th January 2016 marked the start of a brand new organization – combining the talents, expertise and ideas of more than 39,000 people in over 120 countries. Created through the merger of Willis Group Holdings Plc and Towers Watson, this new company will transform the way our clients manage their risks and engage their people.

Our distinct, connected perspective across talent, assets and ideas unlocks potential for our clients. While many just look at mitigating the downside, we see how a unified approach to people and risk is a path to growth.

Powered by market analytics and behavioural insight, our integrated teams reveal hidden value within the critical intersections of our clients' organizations. We design and deliver solutions that manage risk, optimize benefits, cultivate talent and expand the power of capital to protect and strengthen institutions and individuals.

We have already met with new colleagues who are assisting our client base with new solutions including Pensions Advisory, Wind Up Services and Trustee Services. We have also provided over £300m of equity via our pension fund clients to capitalise a new open end fund that has been set up to acquire distressed property assets.

We are excited by our expanded scope of services and increased global footprint and the strong foundation for growth this merger has provided us. We will keep you updated as and when we leverage these new opportunities, but in the meantime if you have any questions please contact myself or one of the team.

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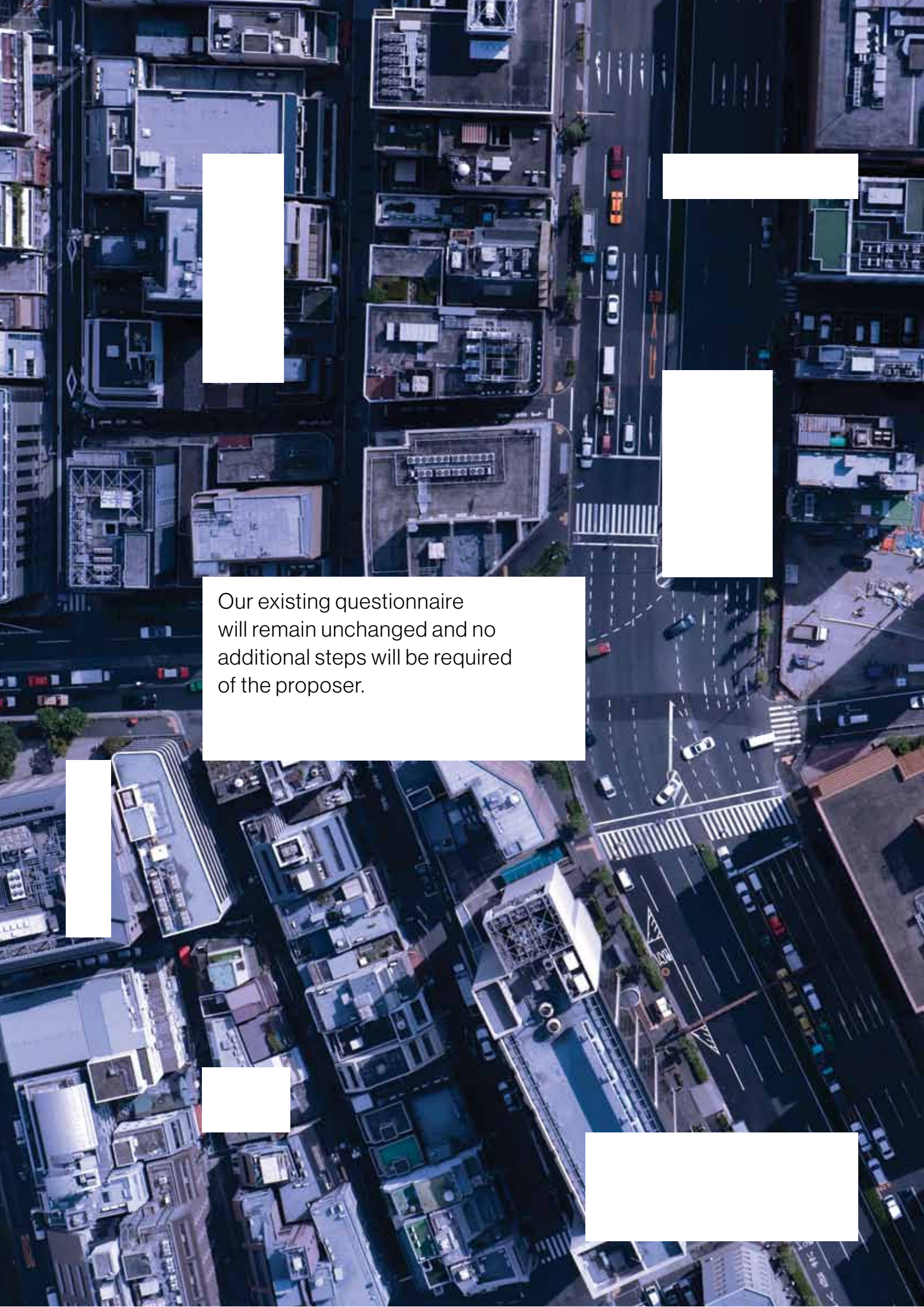

Our existing questionnaire will remain unchanged and no additional steps will be required of the proposer.

The Insurance Act 2015

On 12th February 2015 a significant new piece of legislation was passed that will significantly change how insurance is transacted in the UK. This legislation comes into force on the 12th August 2016 and seeks to provide much more clarity to the buyer of insurance contracts as to what they can expect in terms of claims settlement.

Under the existing framework much of the governance around insurance contracts comes from the Marine Insurance Act 1906. This Act places a lot more onus on the proposer in terms of ensuring that the proposal contains what a prudent underwriter requires. This in effect puts the proposer and underwriter in equal positions in assessing what is relevant or not. Many see this as an unfair position to take and that is indeed one of the principal issues that the Insurance Act looks to address. The Insurance Act has therefore been designed to replace the Marine Insurance Act and to create a less onerous and more certain environment for the proposer. The legislation is seeking to create a new and fairer balance between policyholder and insurer.

The changes will have a significant impact on how insureds and insurers approach policies, creating new duties for insurers and policyholders to comply with.

The Act deals with:

- Duty of disclosure, both before a contract incepts and when amended
- Warranties (including basis of contract clauses)
- Terms not relevant to the actual loss
- Fraudulent claims by insureds
- Good faith
- Amendments to the Third Parties (Rights Against Insurers) Act 2010

Many will say it is about time and they are probably right, but here we are less than 6 months away and much of the industry is silent, so why?

Insurers have been looking at them closely for some time to see how they can comply with the act with as little detrimental impact on their bottom line. The natural concern for insurers is that they will either have to be more selective in terms of risk acceptance, charge higher premiums, make lower profits or potentially suffer losses. The motive for insurers against this backdrop would be to adopt the most stringent interpretation of the rules but in a competitive market place they risk losing business to other insurers offering a more open and relaxed interpretation.

Out of the many hundreds of insurers who operate in the London and wider UK insurance market, only a handful have declared their position on this Act, so it impossible at this point to advise on a unified approach to how proposals must be made and to suggest how behaviours should change, if indeed they have to at all, come the 12th August.

Willis Towers Watson is at the forefront of negotiations with the general insurance market and seeks to gain definitive responses from all insurers on how they will interpret and implement this act.

By using one main insurer, Willis Insolvency Services has a very strong position on the Insurance Act and aims to include non-disclosure of facts prior to the Insolvency Practitioner's appointment, amongst other key safeguards, within the Open Cover wording. This means that whilst other brokers using more than one insurer on a regular basis might struggle with this non-disclosure issue being agreed and understood on a case by case basis (and indeed this might only become clear in a claims situation) Willis Insolvency Services will not have this issue and can offer the Insolvency Practitioner and Receiver peace of mind. These safeguards and the rationale behind them are laid out in more detail below.

As stated above, the act, does not seek to make current levels or processes of disclosure more onerous; **indeed, our existing questionnaire will remain unchanged and no additional steps will be required of the proposer**. Instead it looks to ensure that once that disclosure has been made more certainty is present as to whether the insurer will pay claims. It does however put an onus on insurers that if they have queries over the risk based on the initial disclosure, that they ask further questions they feel relevant to satisfy their ability to underwrite the risk. If they do not ask any further questions they are unable to suggest at a later date that a fair representation was made, assuming that any information omitted was done so innocently.

There is also a very important part of the act which provides an escape from representation of the risk where the insurer explicitly provides that waiver:

“In the absence of enquiry, subsection (4) does not require the insured to disclose a circumstance if it is something as to which the insurer waives information.”

This is perhaps the most important part of the act to the Insolvency Profession as it allows Office Holders to state the limitations of their disclosure, due to a lower than normal knowledge of the risk and if accepted by insurers removes any right they may have previously had to avoid a claim for non-disclosure.

This is the main strategy Willis Towers Watson believes should be adopted, particularly when considering insolvency business. Writing specific descriptions into the policy wording of what constitutes fair representation for insolvency professionals, removing any requirement to disclose historic information i.e. claims experience and also removing any requirement to engage third parties to also provide surveys and valuations etc. In essence the proposer should only be completing their usual questionnaire and it should be accepted that they will only do this with the information readily to hand.

The role of the broker here is key, many will not understand the unique position Insolvency professionals are in, or may lack the commercial ability to get all of the required safeguards put into place. It should also be noted that in the absence of strong relationships with insurers who have significant experience writing insolvency business, it is likely brokers will be forced to adopt a common and onerous approach to satisfy a broad range of insurers in the open market. It should not be forgotten that the more information disclosed, the more risk is then present that some of this information might subsequently be found not to be accurate and non-disclosure issues will arise.

The advice Willis Towers Watson are imparting to our clients based on the discussions we have had with insurers is:

- Do not commit to providing more information than you would have done previously, the intention of the act is not to raise the bar, but to ensure that there is more certainty with the existing levels of disclosure.
- Ensure that the most senior person actively involved with the proposal, reviews the information prior to submission. Again, specific safeguards should be included within policy wordings to protect senior managers who are not actively involved in the insurance proposal from liability in the event of non-disclosure.

- Ensure that anyone acting on your behalf in terms of insurance placement or management, understands the act, its intention and how insolvency office holders are uniquely placed in terms of risk awareness and personal liability
- Obtain key safeguards:
  - Restrict duty of disclosure to information to hand, post appointment and without the need to engage third parties i.e. surveys and valuations
  - Look to include Innocent Non-Disclosure Clauses
  - Include severability to ensure Joint Insureds (joint office holders for example) are not without cover if one of the other insureds breaches the policy conditions.

We feel that this piece of legislation is incredibly positive for insolvency professionals. It provides the opportunity to continue with existing working practices and to reduce the ability of insurers to avoid claims.

More information will be released in the coming months but if you have any queries in the meantime please contact us to discuss this further.

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Insurance Premium Tax ('IPT')

In the 2016 budget George Osborne announced that the standard rate IPT would increase from 9.5% to 10%.

The new standard rate of IPT will be due on insurance premiums treated by the legislation as received on or after 1 October 2016, except where insurers operate a special accounting scheme. From 1 February 2017, the new rate applies to all premiums, regardless of when the contract was entered into.

Legal Aid, Sentencing and Punishment of Offenders Act 2012 ("LASPO") & After The Event Insurance ("ATE")

Much has been written about the removal of the exemption to insolvency litigation from the LASPO Act. The effect of this change is generally well understood, although arguably not by policy makers.

So what does the landscape look like in 2016?

First of all ATE Insurance is here to stay - it is still available in the post 6th April 2016 environment, but with premiums no longer recoverable from the defendant, the financial impact on recoveries will in all likelihood see the number of policies being taken out significantly reduced for smaller value claims. The cost of ATE premiums is now borne by the claimant, and therefore in reality only cases where there are significant recoveries available will see an impetus to resort to litigation.

On the basis that all else remains unchanged, the role of the insurance broker is to ensure that the premium is well capitalised and that strong competition is present in the market. This will ensure that where there is a robust case for litigation there is an ATE premium which is competitive and represents good value for clients.

With the removal of the exemption, ATE insurers now have a direct financial interest in the level of recoveries. A common sentiment and not one that is necessarily entirely without foundation, is that ATE premiums are relatively high for the amount of coverage provided. It is therefore incumbent upon brokers to ensure that ATE insurers deliver value more than ever.

All of this assumes that we operate in the same framework as we did prior the the exemption expiring, but as history shows us, where there is demand but no supply in a market, innovation occurs and new solutions become available. Currently it looks like the most likely source of this innovation is in the litigation funding space. The ability to assign claims and a flood of new capital into the market means that there is more activity involving Third Party Funders funding and even buying litigation rights. However, there is a perception that ATE premium (and particularly success fees) applied by funders is sometimes very high. Market forces again dictate that with more funders coming into the market and an increasing number of different funding options being offered, that risk appetite will increase and/or the premiums/success fees charged will fall. It will take some time for the pricing to change, but with funding to date largely supplied by hedge fund capital, the inevitable influx of more traditional sources of risk capital will soon occur and these capital providers with history of operating within the insurance market will often operate lower margins models. All of this is to the benefit of ATE capacity and Third Party Funders.

It is also worth mentioning Damages Based Agreements ("DBA's") as some commentators have suggested they may become more prevalent post 1st April 2016. But what is a DBA?

Essentially it is an agreement between a client and his solicitor to share the litigation risk. A definition of success is agreed and upon that success a pre-agreed proportion of the recovery from the other side is deducted from the client's final recovery and goes to pay off the various legal fees and costs (solicitors', counsel's and VAT)

In order to compensate for the risk of losing and there being no funds to cover the associated legal costs, the client may have to agree to part with a significant proportion of their recovery. This again means that the motivation to pursue claims where the size of the potential recovery is minimal will likely be diminished. Not many solicitors currently act under a DBA, but with some firms likely to be less inclined to act under a CFA after 1st April many will probably look at DBAs, or a variation of them.

So with all of the above in mind where are we? Officeholders will need to weigh up the value of any litigation closely, but to support them in making litigation

viable in as many cases as possible, the insurance industry needs to ensure that value is being delivered and new solutions developed. At Willis Towers Watson we have access to leading ATE markets, have strong relationships with a wide range of existing Litigation Funders and have a enviable legacy of introducing new risk capital to markets and facilities. These tools mean we are well equipped to assist the insolvency industry through what is going to be a difficult period of transition.

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Preparing insolvency practitioner's (IP's) for the Surprising Bite of the new health & safety enforcement regime?

The new sentencing guidelines for health & safety offences are in force from 1 February 2016. The sentences are now based on turnover and will dramatically increase the level of fines, particularly for larger organisations. This could be very serious for the larger IP firms, now facing potential fines in excess of £100million for health & safety breaches.

Worse still, IPs are particularly vulnerable to criminal prosecution as individuals because they take appointments in a personal capacity and they are an attractive prosecution target. Unintended consequences of the way punishments are now calculated mean that IPs are much more likely to be imprisoned for breaching health & safety laws.

The Four Inflations

For most health & safety and food hygiene breaches, the criminal law laid down by Parliament does not set an upper limit to the size of the fine, so it is left to judges and magistrates in Court to decide how the fine should 'fit the crime'. To help the Court set a fair, transparent and consistent tariff for these offences, the eminent judges and lawyers on the Sentencing Council have created a specific set of guidelines now coming into force.

Close inspection of the new sentencing guidelines shows that four inflationary factors are going to increase radically the level of fines, yet only 1 of these factors was intended. Similarly, the threshold for imprisonment will be reached very much more easily than before. Let's look briefly at the four inflationary factors:

1st Inflation

The sentencing guidelines introduce a structured approach that the Court must follow. This involves plugging 'culpability', 'likelihood' and 'harm' factors into a series of tables to reach recommended starting point fines, as well as ranges of fines above and below the starting points. Similarly for imprisonment of individuals, a table stipulates ranges of prison sentences above and below various starting points.

These tables were calculated by reviewing past sentences and then increasing the punishment. This 1st inflation was intended. It was designed to accommodate the Court of Appeal's repeated view that health & safety fines have generally been too low and need to be increased sufficiently to send a message to directors and shareholders. Indeed, the Court of Appeal envisages fines exceeding £100million for the worst health & safety breaches by the largest organisations.

But the Court of Appeal has not recommended massive increases across the board, even for less serious offences by smaller companies and by individuals. Yet this will be the effect of the next three inflations.

2nd Inflation

TThe sentencing guidelines switch from a mainly outcome based approach (what was the seriousness of the injury) to a risk based approach (how serious was the harm that was risked). There are justifiable reasons for this switch but its inflationary effect on sentences was not factored into the calculations. How does this 2nd inflation work?

Suppose an IP is organising an asset sale at a factory and the purchaser of a hydraulic press allows it to drop from a first floor ledge, crushing the toes of someone below. Traditionally, that would be prosecuted and sentenced very much more leniently than if the same object had hit someone's head and caused a fatality. Under the new risk based approach, the toe injury is seen as having involved a high risk of death or disability and is plugged into the computation at the level calculated for a fatality.

The majority of non-fatal incidents could have been more serious, so these will be inflated up to the level of fine corresponding to that more serious injury.

3rd Inflation

If the offence exposed not just one but a number of people to the risk of harm, the Court is directed to ramp the punishment up to the next level. For example, if other people could have been hit by the hydraulic press falling from the ledge, this 3rd inflation will apply.

4th Inflation

Finally, if there was actual harm (unless more minor than could be expected), the Court is also directed to ramp the punishment up to the next level. Since most prosecutions arise after someone has been injured, this 4th inflation will usually apply.

In summary, the combined effect of these last 3 unintended inflations will mean that criminal sentences will tend to converge at the higher end of a scale that has already been substantially increased by the 1st intended inflation. The Court is given some discretion but not enough to depart materially from the stipulated calculations.

For example, it is going to be difficult for an individual convicted offender to escape a jail sentence if he or she was aware of a risk of being in breach, nobody suffered an injury but several people were exposed to a 'medium' likelihood of death or disability. This is a very significant reduction in the threshold for imprisonment for health & safety offences.

This means it has never been more important to train IPs and their staff on what to do to protect their firm from the greatly increased potential fines and to keep them out of jail. Please don't hesitate to contact Willis Towers Watson Insolvency Services for further information on bespoke training and on site assessments, Willis I Quest and Willis Fire Quest.

We would like to thank Simon Joyston-Bechal, Director at Turnstone Law for his input into this Technical Bulletin.

turnstonelaw

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Launching our New Open Cover Insurance Scheme in the Republic of Ireland

We are delighted to announce the launch of our new open cover insurance scheme in the Republic of Ireland (ROI).

This scheme will complement our existing market-leading UK scheme; providing insurance solutions for clients based in Ireland and for our UK based clients undertaking cross-border appointments.

The ROI scheme provides similar benefits to those of our UK scheme. To ensure assets are protected on day one we provide immediate insurance solutions with 30 days automatic cover from the date of appointment. The scheme provides wide cover for vacant property and has low policy excesses to reduce the creditors' exposure to uninsured losses.

Key features include:

- Flexible payment terms
- €12,500,000 limit for property damage and rental income combined
- €10,000,000 property owners' liability limit
- All risks cover for unoccupied property (subject to compliance with the Code of Practice)
- 30 day's automatic cover from the date of appointment (within the scope of the scheme)

The flexible payment terms enable you to realise assets before paying insurance premiums without any compromise to insurance cover. The scheme also provides short term cover ensuring you only pay for the insurance that you need, supporting you in managing the overall costs of the appointment.

Should you require any further information regarding the ROI scheme please contact

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Bad Debt Protection

In addition to the recent launch of our Open Cover facility into the Republic of Ireland, we are also very proud to have partnered with Credebt, a leading industry ledger realization firm, to provide a ledger audit and collection service, secured by insolvency and default insurance.

Credebt offer a debt collection service to Insolvency Practitioners on all appointments. Their service can be bought on a case by case basis and all ledger 'clean up' administration will be done by them giving Insolvency professionals a clear view of what return to expect. Furthermore, should a debtor fail to pay or become insolvent themselves there is a Credit Insurance policy provided by a market leading insurer to pick up the claim.

Totally unique in this market, Credebt are able to offer Insolvency Practitioners access to Bad Debt Protection on all ledgers subject to evaluation giving far more robust projections for debt realisation

Designed to protect your appointment creditors from unforeseen losses on one of the most uncertain and largest asset realisations, and an opportunity to provide a more robust realisation strategy.

Once Credebt are instructed they:

- conduct a free of charge audit of ledger in order to crystallise the total amount due and confirm what falls within the Credebt Protect + product
- site visits within 48 hours of appointment to collate all the required books and records
- report monthly on progress and ensure their clients are kept fully informed of any issues that may impact on collections
- protect the Insolvency Practitioners position by maximising recoveries quickly and effectively on all ledgers for all industries (including Construction)
- Use effective and tried and tested measures to collect debt, with most ledgers collected within 3 months

If you wish to discuss this in more detail with us, please contact either your usual Client Service Director, or Samantha Taylor.

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Industry insight

It comes as no surprise that the Oil and Gas industry is under particular strain following the recent slump in oil prices, but whilst there have already been a few notable casualties in the offshore production industry, the roots of these failures arguably lay before the most recent slide in prices so it seems likely that more will end up in distressed positions as a result of the market conditions through the end of 2015 and beginning of 2016.

Whilst the Super Majors may have enough strength in their balance sheets and the ability to increase their gearing, in order that they can weather the storm, the Independents who operate on a tighter margin, with higher risk assets are often at the mercy of their creditors. When these companies enter a formal insolvency process the risks to the Insolvency Practitioner may on the face of it seem prohibitive, but in fact this may not be the case and with proper management of the insurance programme these risks can be managed to the same level as would be expected outside of insolvency.

Energy risks are almost exclusively insured in the London Market. The key insurance lines that are required (Property, Operators Extra Expense and Liabilities) are combined together under what is termed an 'Energy Package'. These packages usually schedule out the exposure amongst several insurers. The insurance programme within the market is led by one or two insurers and all other insurers follow them in terms of agreed pricing, wording and endorsements.

It may be obvious but it is worth re-affirming that due to the specialist nature of the cover required, Open Cover facilities are not an option for anything other than the more straight forward onshore property risks i.e. offices, computers and employees. Therefore steps should be made to maintain the Energy Package and ensure it recognizes the Insolvency Practioners personally, indeed on this latter point, pre-emptive endorsements can be agreed and put into place prior to any insolvency, that automatically come into force upon appointment, making the required changes and meaning that even if the appointment occurs outside of normal business hours, the coverage, like Open Cover, is automatically provided.

Willis Towers Watson have led the industry in advising on Oil & Gas insolvencies within the last 12 months and are able to provide confidential advice for any practitioner in a planning stage as to what the options available to them are and how best to manage the Energy Package and associated covers though either a restructuring or insolvency process.

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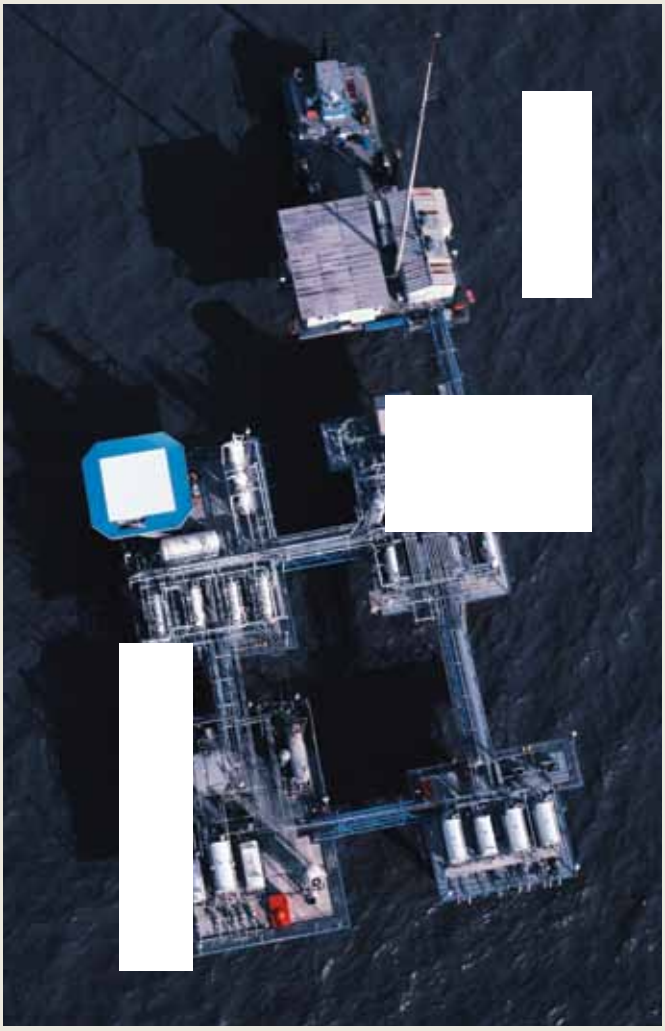

New member of the team

Damien Frost
Sales Director

On the 1st February the Insolvency team was joined by Damien Frost. Damien joins us as our new Sales Director and brings with him a wealth of experience from previous roles servicing the sector.

Damien comes from a strong footballing family and enjoys not only watching the beautiful game but also gets involved with coaching. Whilst his brother plays for West Ham United, Damien swears allegiance to Tottenham, which makes for interesting family get togethers!

"I am really excited to be joining a firm as well-known as Willis Towers Watson and at such a key point in its history. Whilst we are a market leader there is significant opportunity for growth and on top of an excellent legacy we have some great new products and services which I am keen to let the market know about in more detail"

Damien Frost:

About Willis Towers Watson

Willis Towers Watson (NASDAQ: WLTW) is a leading global advisory, broking and solutions company that helps clients around the world turn risk into a path for growth. With roots dating to 1828, Willis Towers Watson has 39,000 employees in more than 120 countries. We design and deliver solutions that manage risk, optimize benefits, cultivate talent, and expand the power of capital to protect and strengthen institutions and individuals. Our unique perspective allows us to see the critical intersections between talent, assets and ideas – the dynamic formula that drives business performance. Together, we unlock potential. Learn more at willistowerswatson.com.

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