MARKET CONDITIONS

Whilst for most of us early 2010 manifested itself in snow and ice, for a small corner of the City of London there has been a distinct thawing. We refer of course to conditions in the market for buyers of financial institutions professional lines insurance. There are some clear signs that the difficult conditions of 2008 and 2009, where premium increases and cuts in capacity were prevalent, are going to improve during 2010. Already we have seen a number of renewals with no premium increase and in certain cases discounts have also been achieved.

As we predicted in the last Willis Index, these more favourable conditions have centred upon small to medium sized financial institutions purchasing fairly low limits of liability i.e. GBP 5 million – 25 million. However, that said, the speed of change in the market has been quicker than we predicted in quarter four of 2009. We had initially thought that a softening wouldn’t occur until at least the summer of 2010. So given this revised outlook it seems a fair assumption that some larger financial institutions renewing larger limits may also start to see the benefits of a softer market earlier than we had originally thought.

Some observers are questioning why, with underwriter results for 2007 and 2008 in considerable deficit, the market has moved in the way it has? The reason is two-fold. Firstly, the aura of concern amongst insurers that prevailed during the credit crunch has in some areas reduced. Certainly, many insurers still harbour concerns from mounting losses but these tend to relate now to claims that have already occurred and there is an increasing contingent of underwriters prepared to relax their underwriting criteria. The increasingly held perception is that the risk environment for financial institutions has improved and a number of carriers are now comfortable to reflect this in the renewal terms they offer. This stance is not universal, which is why we turn to the second reason – the influx of new capacity in the market place. From January 2010 we have seen five new entrants writing financial institutions business, all of whom have a budget to fill and a need to secure premium income. This new capacity is a welcome tonic and vastly improves our ability to generate competition between insurers.

Without tempting fate, it is worth considering how steadfast these conditions are i.e. to what extent could they be threatened. The reason we have seen the increase in new capacity is that the financial institutions market place has been fairly unique when compared to other specialty classes for having sustained comparably high premiums for the last couple of years, hence it is seen as an attractive class to new entrants. If we were to see a significant hardening in other classes of specialty business (something which most likely would be triggered by an extremely severe natural disaster or similar catastrophic event) this might cause capital to flow out from the financial institutions market place to other specialty classes. Alternatively, a new severe and systemic loss to the financial institutions market place could wipe out any new-found confidence causing underwriters to revert back to more conservative strategies.

So, how best to take advantage and make the most of the current conditions? The core strategies for a harder market are preparing for renewal early and having a clear strategy to tackle renewal. This approach will also reap rewards in a softer market. Having ample time and quantified objectives enables the most effective competition to be driven between insurers, thus delivering the best terms from the market.
Over the past 18 months Willis have seen a substantive increase in the number of claims (and circumstances which may give rise to claims – see box) relating to the management of funds being notified to professional indemnity insurers.

**WHY DO CLAIMS ARISE?**
The types of scenarios that typically arise in this sector may include the following allegations:

- Breach of mandate, e.g. investing in products which are not expressly permitted;
- Failure to advise on the structure of products and the risk in relation thereto;
- Failure to execute redemptions in a timely manner, or doing so at the wrong price;
- Failure to execute trades in accordance with instructions or in accordance with the constitution of the fund;
- Failure to undertake adequate due diligence and therefore to identify potentially fraudulent schemes.

We set out in the box below some real claims examples and our experience of how the insurance industry and the courts are responding to claims.

**SOME GOOD NEWS FROM THE INSURANCE INDUSTRY**
Professional indemnity policies protect financial institutions against the cost (both in terms of damages and reasonable legal costs) of civil liability incurred in breach of their obligations to third parties. Many of the claims which are presented to insurers can be readily seen to fall within the relevant insuring clause (in so far as it is clear that there has been negligence which has caused an underlying investor a loss for which the fund manager is liable). In these cases financial institutions making valid and effective claims under their insurance policies can expect their insurers to respond positively.
SOME GOOD NEWS FROM THE COURTS
In very many cases, of course, it is less obvious that there has been a breach of duty to a third party on the part of the insured. That will be examined in the course of litigation, arbitration or mediation. In these cases, insurers will expect the claim to be appropriately managed and defended and will likely become very closely involved, in larger cases with the appointment of lawyers of their own to advise on and monitor progress.

In our experience the likelihood of the insured being able to rebuff allegations made (and prove that there is no such liability) depends on many factors, including an assessment of the underlying fact pattern, legal arrangements and interpretation.

MAXIMISE YOUR CLAIMS SUCCESS
We should emphasise how vitally important it is to comply strictly with terms of the policy, both as claims and circumstances which may give rise to a claim are notified and in the course of the ongoing management of the claim.

One of the most effective ways to improve your claims success is to look at past claims performance of your selected carrier. At Willis, the Willis Quality Index has been developed to capture, analyze, and share vital carrier information. This invaluable tool combines qualitative opinions from Willis Associates across the globe with quantitative data and measurements from our various tracking systems. Performance of carriers is measured on:

- Policy Administration, including speed and quality of policy issuance.
- Claims, including the time taken to agree and settle claims.

Willis clients thus have the opportunity to make better informed choices, tailored to their specific placement needs, based not only on financial strength but also on superior service.

SEE THE RISKS BEFORE THEY ARISE
Willis also has experience of risk mapping in relation to potential loss events and would be happy to provide this service, if required, on receipt of the specific scenarios. This is often done in conjunction with your ICAAP review and operational risks you have identified. However, Willis also maintains an operational risk database ("WORLD") from which it is possible to extrapolate additional scenarios. The purpose of this service is to review the scenarios provided against your financial lines policies and advise whether the scenarios reviewed are ‘insured, uninsurable, insurable or uninsurable’. We would specifically need to agree a mandate for this service and discuss the fee element applicable to it.

For more information on ways to mitigate your risk please contact:

James Baird
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Email: jbaird@willis.com

Claims Notification Check List
- **Who to notify**
  All notifications to Insurers, in writing, should be *forwarded directly* to your insurance broker.

- **When to notify**
  As soon as you first become aware of a claim or of a circumstance which may give rise to a claim, notification should be made immediately irrespective of:
  - The amount which may be involved.
  - Your views or opinions on liability under the policy.
  - Whether you consider the claim or circumstances may be spurious or without merit.

- **What to notify**
  Please ensure the following information, at least, is provided to Insurers.
  - Brief details of the nature of the claim or circumstances, including name(s) of actual or potential claimant(s) *together* with your views on the claim or circumstances and any allegations made or anticipated being made against you.
  - Date of your first awareness of a claim or circumstances which might give rise to a claim.
  - Your estimate on the quantum which may be involved.
  - Copies of any correspondence or documents in which a claim is made or allegations are implied or expressed against you.

- **Your duties in the event of a claim or circumstances which may give rise to a claim**
  - Do not admit liability.
  - Do not settle or make or promise any payment.
  - Do not disclose you have made or are intending to make a notification under your Policy.
  - Do not take any action which might prejudice Insurers’ position or their ability to investigate a claim or circumstance which is expected to be notified under your Policy.
  - If you are in any doubt, then please contact your Willis contact/Account Executive who will assist/guide you in determining the appropriate course of action.
FINEX National, has entered into a strategic alliance with Dominion, the leading provider of trustee, advisory and wealth management services to the hedge fund industry, to form a Hedge Fund Practice Group for fund management organisations.

The new business unit within Willis will be led by Paul Richards, head of the recently expanded FINEX National Financial Institutions division, which provides insurance broking services to financial and professional services firms.

Under the alliance, Willis will be responsible for the client-facing aspects of the general insurance arrangements for Dominion's clients, delivering the full spectrum of financial and executive risk solutions, including Directors' and Officers' (D&O), Professional Indemnity and Employment Practices liability insurance. These services will also be available to other companies in the fund management sector. The relationship will, in turn, give FINEX National's clients access to the extensive range of services that Dominion provide to the hedge fund sector.

Commenting on the alliance, Richards said, "In the wake of the financial crisis, hedge funds have become a lot more institutionalised, and they are facing greater regulatory scrutiny and increased investor demands. A holistic risk management programme is key to safeguarding the reputation and assets of hedge funds, investment management companies, and the supporting industry service sector. Backed by the global resources of the Willis Group, with the expertise of FINEX National, the alliance will offer clients a one-stop boutique broker service for all their financial and executive insurance needs."

A dominion spokesperson said, "Willis has been successfully providing insurance broking and document production services to Dominion and ASF Financial Services, a company recently acquired by Dominion, for a number of years now. We are confident that their proactive, personalised service and in-depth knowledge of financial and executive risk insurance will complement our expertise in financial planning, employee compensation and benefit structures, giving our clients the best advice possible."

Willis will provide the following broking services as part of the alliance:

- D&O liability insurance.
- Fund D&O insurance including 'prospectus' liability.
- Professional indemnity (PI)/civil liability insurance.
- Crime insurance.
- Employment practices liability insurance.
- Pension fund trustee liability insurance.
- Commercial general (office and liability) insurance.
- Risk mapping of exposures.

Dominion will provide the following services:

- Trustee administration services.
- Consulting on design and implementation of corporate compensation structures and tax planning.
- HR outsourcing.
- Corporate wealth management.
- Personal wealth management.

For more information please contact

Paul Richards
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Email: prichards@willis.com

To discuss your insurance arrangements with the Willis FI team please call Derek Reeves on +44 (0)20 3124 6944.