

AUDIT COMMITTEE

5 December 2011

MUNICIPAL MUTUAL INSURANCE - LIABILITY AS MEMBER

REPORT OF HEAD OF FINANCE

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RECENT REFERENCES:

CAB1836 – Insurance Reserve Review, 7 April 2010

AUD008 – Statement of Accounts 2010/11 (pre-audit), 29 June 2011

AUD013 - Statement of Accounts 2010/11 & Letter of Management Representation,
26 September 2011

EXECUTIVE SUMMARY:

At its last meeting the Audit Committee requested an investigation to assess the possibility of the Council buying out its liability as a member of the Municipal Mutual Insurance Company (MMI).

The Council's Actuary has been consulted and an investigation undertaken of the financial and insurance market.

Arising from the Council investigation it is resolved that there is no option for the Council to obtain an indemnity for its MMI member liability. However the situation remains under review and the Audit Committee will be informed of any progress.

RECOMMENDATIONS:

That the Committee take note of the report.

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1. Background

- 1.1. Municipal Mutual Insurance (MMI) is an insurance company limited by guarantee and not having a share capital, which was established by a group of local authorities and incorporated under the Companies Acts 1862 to 1900 on 13 March 1903. The Company suffered substantial losses between 1990 and 1992. These losses reduced MMI's net assets to a level below the minimum regulatory solvency requirement. In September 1992 MMI ceased to write new, or to renew, general insurance business.
- 1.2. Since going into run-off in September 1992 numerous business and corporate disposals have taken place including the right to seek renewal of the larger part of MMI's direct personal and commercial lines insurance business to Zurich Insurance Company along with a number of MMI's assets and many members of its staff.
- 1.3. A contingent Scheme of Arrangement under section 425 of the Companies Act 1985 became effective on 21 January 1994 but remains held in reserve because a surplus at the conclusion of the run-off period continues to be foreseen by the Directors. A commission for risk of up to £30,000,000 due to Scheme Creditors is not payable until the conclusion of the run-off.
- 1.4. More information can be found on the Company's website:
<http://www.mminsure.co.uk/>.

2. Introduction

- 1.1 The Council is a member of the Municipal Mutual Insurance Ltd. The Council's maximum exposure in connection with the 'run off' of the Company insurance business, including a scheme of arrangement, is a liability of £185,000.
- 1.2 MMI produce a six monthly statement to members. The conclusion of MMI's liability is mainly focussed on its obligations arising from asbestos and the asbestos related disease of mesothelioma. These claims relate to 78% of MMI's total liabilities. Without certainty regarding MMI's obligations no action can be taken to conclude the Company's affairs and resolve whether there is any MMI member liability.
- 1.3 To try to achieve certainty, MMI has been party to a combined court action known as the 'Employers' Liability Policy Trigger Litigation'. The case involves the apportionment of insurance claim costs, during the period of risk

exposure, between various insurers arising from the overlapping of indemnities within three different policy wordings.

- 1.4 In November 2008 the High Court handed down judgement against MMI. The case was then referred to the Court of Appeal in November 2009 and judgement handed down in October 2010. Whilst MMI achieved some benefit, no progress was made on the substantive issue of exposure to financial loss. The case has been referred to the Supreme Court and judgement is expected in June 2012.

2. Current Position

- 2.1 This potential liability of £185,000 is recognised in the Council's Statement of Accounts for 2010/11 as a contingent liability, as settlement of this possible obligation is uncertain and not within control of the Council.
- 2.2 To be prudent the Council has for some considerable time made a provision in the accounts for the full £185,000 should the worst case scenario arise, so that it could be settled without further charge to General Fund. As a consequence of the accounting changes made with the implementation of International Financial Reporting Standards (IFRS) accounting rules, the funds for the worst case scenario are now being held as an Earmarked Reserve.
- 2.3 According to the Council's Actuary the outcome of the court case may significantly influence the exposure to financial loss and this will impact on members such as the Council.
- 2.4 Whilst in theory it would be possible for MMI to negotiate a commutation with individual members in order to crystallize a financial position, in practice, for a commutation to proceed with any member, MMI would need to demonstrate that such commutation would be in the best interests of creditors and the scheme administrator. There is no evidence of any MMI member seeking to obtain a commutation with any prospect of success.
- 2.5 The Council Actuary's current view is MMI would not be able to demonstrate a commutation is in the best interests of all concerned, whilst simultaneously providing terms deemed attractive to the Council.
- 2.6 The Council's officers have enquired of its insurers whether there is any possibility of buying out its MMI member liability. The response received is currently no facility is available however the matter remains under review. Contact with members of Association of Local Authority Risk Managers (ALARM), the Hampshire Insurance Forum and Insurance Brokers has not revealed any appetite within the insurance market to protect a MMI member liability.
- 2.7 Arising from the Council investigation it is reasonable to conclude there is currently no facility for the Council to obtain an indemnity for its MMI member liability. However the situation remains under review and the Audit Committee informed of any progress.

3. Risk Assessment

- 3.1 The outcome of the EL Trigger Litigation case in the Supreme Court will help the MMI Board obtain certainty over its affairs and whether a solvent run off can be achieved. As a consequence MMI members, including the Council, will have a better understanding of the potential liability. In addition the financial and insurance market may have more confidence to assess the risk and better placed to consider a commercial proposition for the Company and/or MMI members to consider.
- 3.2 MMI is of the view that there is a realistic expectation of prevailing at the Supreme Court. However the Company has not reflected the prospect of success within its accounts.
- 3.3 The Council's Actuary has assessed MMI's Annual Report and Accounts for the year ended 30 June 2011 and provided an indication of the potential liability of the Council. If the EL Trigger Litigation case at the Supreme Court was lost, MMI's assessment of future claims was adequately reserved and current claims were settled immediately, the estimated financial liability for the Council would be in region of £19,000.
- 3.4 The Council's assessment of its MMI member liability has been reconsidered with its adoption of the International Financial Reporting Standards (IFRS). The uncertainty in respect of the MMI litigation and the exposure to financial loss has meant the exposure is being treated as a Contingent Liability.

OTHER CONSIDERATIONS:

4. SUSTAINABLE COMMUNITY STRATEGY AND CHANGE PLANS (RELEVANCE TO):

- 4.1 The Council's maximum exposure in connection with the 'run off' of the MMI insurance business will not affect its contribution to the Strategy or Change Plans.

5. RESOURCE IMPLICATIONS: - As discussed in the report.

6. RISK MANAGEMENT ISSUES

- 6.1 The exposure of MMI member liability has been assessed within the corporate risk register (CR5004) and will remain under review.
- 6.2 The Council will continue to explore the financial and insurance markets to ascertain whether any commercially viable option is available to buy out the Council's exposure to MMI member liability.

BACKGROUND DOCUMENTS:

Municipal Mutual Insurance Limited Annual Report and Accounts for the year ended 30 June 2011.

Various documents held within the Governance Group.