

The Guardrisk Update

Incorporating Life Update

August 2011

NEW legislation for the micro-insurance sector could come into effect by 2014 (*Business Day, 29 Jul*). Although 74% of South Africans recognised the need for insurance, 34% had not made plans to address threats to their livelihoods.

THE enforcement committee of the FSB has fined seven insurance companies in June and July for contravening laws governing the industry (*Business Report, 19 Jul*). In instances where patrimonial loss had resulted the committee might, in addition to imposing a financial penalty, order a company to pay compensation to any person who suffered loss or damage as a result of the contravention.

NEW regulations and corporate governance practices have put pressure on companies to increase their focus on tax risk management (*Business Day, 27 Jun*). According to a recent report it appears that large businesses are not transparent with their tax affairs, with an average of 37,6% indicating that they report appropriately to stakeholders.

A CORE set of principles recently adopted by the International Forum of Independent Audit Regulators will promote investor confidence and improve the quality of audit practices worldwide (*Business Day, 27 Jul*). This comes in the wake of different legal and regulatory structures internationally, which have made effective co-operation between audit regulators globally difficult.

EMPLOYEES committed undetected economic crimes, such as procurement fraud, during recessions because companies inadvertently weakened their internal controls (*Business Day, 5 Jul*). According to recent South African Police Service crime statistics, 84 842 cases of commercial crime were reported from April 2009 to March last year, a 51,8% rise since 2003.

THE Unemployment Insurance Fund posted a nine billion rand surplus in the year to March, which far exceeded the fund's target of three billion rand (*Business Report, 29 Jul*).

One company's rescue may be another's ruin

One of the new Companies Act's more contentious provisions relates to the "efficient rescue of financially distressed companies". Section 133 of the Act, which came into effect on 1 May 2011, provides that (apart from for certain specified exceptions) during business rescue proceedings, no legal proceedings, including enforcement action, may be taken against the company undergoing business rescue, or against any property belonging to the company. Once a company is placed under business rescue, a qualified business rescue practitioner is given full management control. The business rescue practitioner has the power to suspend an entire agreement or part of an agreement (excluding employment agreements) to which the company is party.

Effectively, this means that the rights and obligations which the company's suppliers and service providers rely on to protect their business dealings may not necessary be enforceable during the rescue period. Thus, it is not inconceivable that the business rescue proceedings, aimed at aiding the rehabilitation of a financially distressed company, could effectively put the businesses of the company's suppliers and service providers at risk.

Earlier this year, Trade and Industry Minister, Rob Davies, lauded the rescue process as one of the major innovations in the new act. And, on the face of it, the rescue process is a welcome alternative to judicial management, which is an expensive and lengthy process. As Davies says, holding creditors at bay, while stakeholders work to rescue the company, does seem to make more sense. But what about the supplier or service provider that simply cannot afford to wait to enforce certain contractual rights while the company is being rescued?

However, business rescue cannot be viewed by directors as an 'easy way out': directors who vote to begin business rescue proceedings when it is not justified can also be penalised. In fact, the concept of business rescue puts significantly more pressure on a company's directors. In terms of the new act, directors who fail to see to it that their company's creditors are paid after liquidation can be punished and even declared delinquent – the latter remains in place for the lifetime of the person who has been declared delinquent.



A court may even place an 'errant' director under probation. Such an order, which is similar to a suspended sentence, may be made with certain conditions and can be in place for up to five years. The conditions could include attending a designated programme of remedial education, community service or paying compensation to any person who has been adversely affected by the director's conduct.

The fact that court permission is required before the business rescue practitioner can suspend or cancel agreements will offer some small degree of comfort to risk managers and their boards. But, despite the fact that, the request for cancellation by the business rescue practitioner will be judged according to the standards of reason and fairness, taking into account all the facts, companies will no doubt be scratching their heads as to how they can build extra protections into their contracts and agreements.

Risk Barometer

CATASTROPHES worldwide caused an unprecedented \$260 billion in economic losses and \$55 billion in insured losses during the first half of 2011 (*Business Insurance*, 17 Jul). The March 11 earthquake in Japan contributed \$210 billion to the economic losses so far this year.

INVESTMENT in renewable energy is outstripping that for traditional fossil fuels, underscoring the growing importance of the sector within a global insurance framework as insurers insist "carbon-free is not risk-free" (*Insurance Day*, 5 Jul). In particular it is the constantly evolving technology that is one of the greatest risks to insurers.

THE Federation of European Risk Management Association has warned the European Commission about over regulating corporate governance (*Captive Review*, 27 Jul). The EU should focus on the implementation and robust enforcement of existing EU corporate governance rules on risk management rather than creating new ones.

NEARLY 10% of European insurers would need to raise fresh capital in the event of a severe economic shock accompanied by a plunge in share prices, tumbling interest rates and a property market crash (*Business Insurance*, 4 Jul).

THREE years after the start of the credit crisis there is still no sign of the much-predicted avalanche of lawsuit-prompted insurance claims and 2011 could be on course for the second lowest number of securities class actions in 14 years (*Insurance Day*, 26 Jul). There were only two credit-crisis-related filings in the first half of this year and the total number of federal securities fraud class actions was 9.6% down on the second half of last year.

THE average cost of rectifying a data security breach for a malicious or criminal attack in 2010 was \$318 per compromised record, up 48% from 2009 (*Insurance Day*, 29 Jul). Malicious or criminal attacks are the most expensive cause of data breaches, involving nearly a third of all cases. The potential liabilities for the insurance market are therefore significant.

DIRECTORS and officers liability insurance continues to be intensely competitive but some observers see pockets of rising pricing (*Business Insurance*, 3 Jul). On the primary side, rates generally are flat to down about 5%. On the excess side, rates are flat to down as much as 15%, and there's broader terms and conditions available in the marketplace as well.

Life Update

Local

RETIREMENT fund trustees and advisers have become accustomed to choosing retirement with-profit annuities based on the initial cost (*Business Day*, 14 Jul). However, considering initial pricing alone could be extremely misleading. Issues such as bonus policy, asset allocation, investment strategy, mortality risk, cost of guarantees and capital charges all come into play.

NEARLY 10 years after the introduction of surplus apportionment legislation, designed to regulate the allocation of funds' surpluses to various pension fund holders, not all funds have completed their surplus apportionments (*Business Day*, 7 Jul). 87 funds have yet to do this and 305 have withdrawn their applications following queries from the FSB. The total surplus distribution so far has been R20bn, well below the R80bn estimate of 10 years ago.

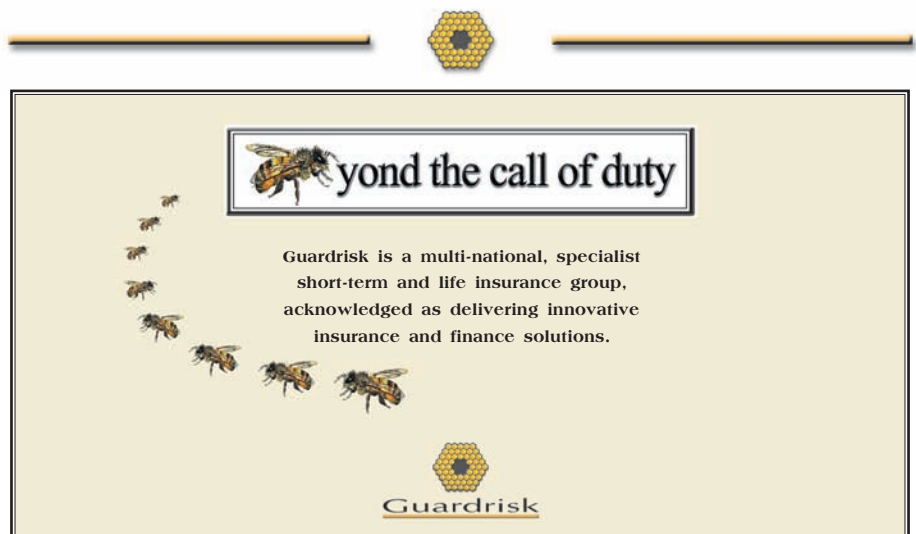
ONLY 53% of employed metropolitan South Africans contribute to a pension or provident fund to save for their retirement (*Business Report*, 20 Jul). One in three respondents surveyed feel the government will take care of them once they are unable to take care of themselves, while 33% also believe their children will do so. This attitude is consistent across all age groups.

IN September the Board of Healthcare Funders (BHF) is taking the Council for Medical Schemes to court over the definition of PMBs (*Business Day*, 14 Jul). At issue is the regulation which says PMBs must be paid for "in full" and at cost by medical schemes. The BHF says the PMB package, covering 270 medical and 25 chronic conditions, has the potential to bankrupt the R85bn industry. Medical schemes want PMB payments to be based on scheme rates and not service provider rates.

International

MID-SIZE employers stung repeatedly by sizable increases in their insured health programmes should be asking their brokers why they haven't suggested self-funding (*Business Insurance*, 24 Jul). Benefit costs for self-funded employers have grown 26% over the past five years compared with 35% for those that buy health insurance. By self-insuring, small and midsize companies could get a better handle on health care costs because they would have access to aggregated claims data—something insurers rarely share with insured employers.

AS long as employers have used safety incentive programmes to reduce injuries and lost work time, there has been debate over the best way to administer them, because some models can produce short-lived or artificial results (*Business Insurance* 31 Jul). The market's reluctance to use a reward system usually is driven by the cost and complication of building an incentive programme that works, and the potential consequences of implementing one that does not.



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