HIGH COURT APPROVES AMENDING SCHEME FOR ORION AND LONDON AND OVERSEAS

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Insurance Coverage Alert

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I. INTRODUCTION

On October 29, 2015, the High Court of Justice of England and Wales ("High Court") issued an order ("Order") approving an Amending Scheme of Arrangement ("Amending Scheme") for two insolvent London Market insurers, OIC Run-Off Limited (formerly the Orion Insurance Company Limited) ("Orion") and The London and Overseas Insurance Company Limited ("L&O") (collectively, the "Insurers"). As a procedural matter, the Scheme Administrators[1] must now obtain approval of a U.S. Bankruptcy Court in order for the Amending Scheme to become "effective."[2]

If it becomes "effective," the Amending Scheme potentially will convert the Insurers' existing run-off Scheme of Arrangement ("Original Scheme") (which does not impose a bar date on claims) to a so-called cut-off scheme, subject to various caveats and contingencies. Cut-off schemes used by other insolvent London insurers have imposed bar dates on all claims and have provided a methodology by which policyholders could submit claims not only based on past losses that are covered under their policies, but also based on estimates of future losses.

Here, the Amending Scheme is relatively complex and includes certain features that have not previously been used by insolvent London insurers. The Amending Scheme will impose a bar date (yet to be determined) (the "Bar Date"), but certain policyholders will have the right to opt-out of the Amending Scheme and to continue to submit their claims under the run-off terms of the Original Scheme over the coming decades. If greater than 30 percent of eligible policyholders "by value" elect to opt-out, then the Amending Scheme would cease to have effect and all claims would continue to be handled in run-off under the Original Scheme. In addition, under the terms of the Amending Scheme, the Scheme Administrators will have the option of reverting certain claims under pre-1969 L&O policies to run-off if they are unable to reach an agreement with certain reinsurers after the Bar Date. Given these contingencies, the ultimate scope and impact of the Amending Scheme will not be known until after the Bar Date.

Policyholders with Orion and L&O coverage should carefully monitor developments related to the Amending Scheme and either file claims or exercise potential opt-out rights prior to the Bar Date. Importantly, policyholders should carefully consider whether their claims are "guaranteed" -- meaning that they would receive 100 percent of their claim value -- and if so, pursue full payment on their claims.

II. BACKGROUND

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Orion and L&O are insolvent London insurers that ceased writing new business and entered run-off in 1992. In 1994, the Insurers went into liquidation. On March 7, 1997, the Insurers implemented the Original Scheme,[3] which did not impose a bar date on claims. Since the adoption of the Original Scheme, the Scheme Administrators have been settling claims and making periodic payments on agreed claims. Given that Orion and L&O are insolvent, policyholders generally have received some percentage of their agreed claims, unless such claims are subject to a guarantee, discussed further below. The current payment percentage for non-guaranteed claims is 58 percent.

Certain of the Insurers' policies were written through the Institute of London Underwriters ("ILU") ("Qualifying ILU Policies"). Pursuant to the Original Scheme, a Qualifying ILU Policy is one that was signed and issued by the ILU with an inception date on or after August 28, 1970, for Orion, and on or after March 20, 1969, for L&O. The Original Scheme provides that so-called Qualifying ILU policyholders will receive 100 percent of their established scheme liabilities.[4]

In the past, schemes for other insolvent London insurers have been converted from run-off to cut-off when, in the opinion of Scheme Administrators, it would be in the best interests of scheme creditors to do so. The timing of this conversion is typically driven by factors such as whether the Scheme Administrators have settled with most policyholders, whether the Scheme Administrators have collected most or all available reinsurance, and whether the cost of administering a run-off scheme indefinitely would result in a reduction in payments to policyholders.

The conversion to a cut-off scheme with a bar date generally favors some policyholders, but negatively impacts other policyholders. In particular, the imposition of a bar date favors policyholders who have settled with the Scheme Administrators based on estimates of future losses or who are in a position to do so, but disfavors policyholders who first experience claims after the bar date or who are not in a position to estimate future losses prior to the bar date.

Here, the Insurers have been discussing the implementation of a cut-off scheme for approximately a decade but have encountered numerous delays arising from various issues, including the ability to collect reinsurance.

As noted, the Amending Scheme has now been approved by the High Court. The general purpose of the Amending Scheme is "to allow for the agreement of Scheme Liabilities and distribution of Scheme Assets to Scheme Creditors [subject to certain exceptions] . . . earlier than would be achieved under the Original Scheme."[5]

Under the terms of the Amending Scheme and as noted in the Order, the Amending Scheme will become "effective" only after a so-called "Chapter 15 Order" has been issued by the U.S. Bankruptcy Court to enforce the Amending Scheme under the U.S. Bankruptcy Code.[6] The Scheme Administrators have indicated that the likely timing of the hearing to obtain the Chapter 15 Order will be January 2016.[7]

III. KEY FEATURES OF AMENDING SCHEME

Policyholders should carefully consider their rights under the Amending Scheme. Key issues include the following:

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- The Bar Date: The Amending Scheme will impose a Bar Date generally 240 days after the Amending Scheme becomes effective.[8] Notably, the Bar Date will apply to both policyholders that file claims and eligible policyholders that exercise any opt-out rights. With respect to policyholders filing claims, the Amending Scheme states that policyholders must "complete and return [their] Claim Form(s) … so as to be received by the Companies before the Bar Date…. [Subject to certain exceptions], the Scheme Administrators will consider only Claim Forms submitted … before the Bar Date…. As from the Bar Date, … [policyholders] shall not be entitled to revise [their] … Claim Form," except in response to a specific request by the Scheme Administrators.[9] Prior to the Bar Date, the Scheme Administrators may generate Claim Forms for individual policyholders that identify prior settlements between the specific policyholder and the Insurers and/or other known liabilities of the Insurers to the policyholder. If a policyholder fails to submit a Claim Form before the Bar Date, the policyholder's recovery would be limited to unpaid claims identified by the Scheme Administrators on this pre-populated Claim Form.[10] Similarly, the Amending Scheme generally states that any eligible policyholder that wishes to opt-out of the Amending Scheme "shall complete and return ... an Opt Out Form … before the Bar Date."[11] Failure of an eligible policyholder to submit an Opt Out Form prior to the Bar Date will bind the policyholder to the crystallization and payment provisions of the Amending Scheme.[12]
- Estimation Guidelines: Claim Forms must be submitted in accordance with the so-called Claim Form Guidance Notes and Estimation Guidelines. The Estimation Guidelines provide certain "principles, policies and assumptions" applied by the Scheme Administrators "to seek agreement with Scheme Creditors," including with respect to the estimated value of future claims.[13] Specifically, the purpose of the Estimation Guidelines is to provide assistance with estimating outstanding and future liabilities in accordance with generally accepted insurance practices.[14] Merely to illustrate, for asbestos claims, the Estimation Guidelines provide guidance on how to estimate future costs. The Estimation Guidelines also discuss legal issues impacting the claim value, including issues related to trigger and allocation of loss across multiple triggered policies, stating generally that the Scheme Administrators should consider potentially relevant state law on such issues.[15]
- Dispute Resolution: The Amending Scheme states that "[t]he Scheme Administrators shall use their reasonable endeavors to reach agreement with the Scheme Creditor with regard" to the value of claims.[16] Any disputes will be referred to by the Scheme Administrators to a pre-appointed Scheme Adjudicator for adjudication.[17]
- Payment of Non-Guaranteed Claims: For non-guaranteed claims, payments to Scheme Creditors will be made subject to a yet-to-be-determined payment percentage.[18] Under the Original Scheme, the current payment percentage is 58 percent. In 2014, the Scheme Administrators estimated that the final payment percentage under the Amending Scheme (if approved) would be approximately 78 percent, as compared to the estimated 71 percent under the Original Scheme.[19]
- Qualifying ILU Policyholders: As discussed above, Qualifying ILU Policyholders have the option of either submitting a Claim Form addressing their past and potential future losses or submitting an Opt-Out Form.
    - Claim Form: If a Qualifying ILU Policyholder elects to file a Claim Form, then they would attempt to negotiate a claim settlement in the normal course with the Scheme Administrators. Unlike a policyholder with non-guaranteed claims (who would receive some percentage of the agreed claims),

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a Qualifying ILU Policyholder would receive 100 percent of their agreed claim.[20] In addition, as an incentive to participate in the Amending Scheme (rather than opting-out), a Qualifying ILU Policyholder may receive a premium payment in addition to 100 percent of the value of if its claims (the Qualifying ILU Policyholder Premium), subject to certain exceptions and limitations.[21]

- Opt-Out. Alternatively, Qualifying ILU Policyholders are also "entitled to opt out of the crystallisation and payment provisions contained in . . . the Amending Scheme and instead have [their] Scheme Liabilities under such Qualifying ILU Policies agreed or determined . . . in accordance with . . . the Original Scheme and once so agreed or determined, paid pursuant to . . . the Original Scheme."[22] In other words, rather than attempting to estimate their future losses based on existing claim data prior to the Bar Date, Qualifying ILU Policyholders have the option of opting-out of the Amending Scheme and continuing to submit claims for covered losses as they are incurred over the coming decades. Qualifying ILU Policyholders who opt-out of the Amending Scheme are not entitled to receive payment of a Qualifying ILU Policyholder Premium.[23] Qualifying ILU Policyholders should carefully consider their potential claims and evaluate whether to exercise any opt-out rights. Generally speaking, policyholders who have not incurred significant losses to date or, for whatever reason, are not in a position to attempt to estimate their future losses at this time, should carefully consider the option of preserving their coverage rights by opting out of the Amending Scheme.

- Potential Reversion to Run-Off. If greater than 30 percent of Qualifying ILU Policyholders "by value" opt-out of the Amending Scheme, "the Amending Scheme shall cease to have effect" as to all policyholders.[24] In other words, after all Claim Forms and Opt-Out Forms have been filed, the Scheme Administrators must determine whether the entire Amending Scheme will "cease to have effect" and whether all claims will continue to be handled in run-off under the Original Scheme. Notably, this determination is focused on whether 30 percent of Qualifying ILU Policyholders "by value" opt-out, rather than 30 percent per capita. As such, policyholders who opt-out because they currently have no claims or *de minimus* claims should have little to no impact on the "per value" determination. The determination of whether all claims must revert to run-off due to opt-outs will occur within 160 days after the Bar Date.[25] In any event, until this determination is made, there will be uncertainty as to whether the Amending Scheme will remain in effect.

- Pre-1969 L&O Policyholders: Under the Amending Scheme, there is also a risk that certain claims filed under L&O policies issued before March 20, 1969 ("Pre-1969 L&O Policyholders") will revert to run-off. Under the Amending Scheme, after the Bar Date, the Scheme Administrators must calculate the Gross Liability of each Pre-1969 L&O Policyholder, calculate the amounts payable by certain "Reinsurers" in respect of the Gross Liabilities of the Pre-1969 L&O Policyholders, and send a written statement to the Reinsurers notifying them of the amount payable.[26] If within 90 days the Reinsurers do not agree to pay the stated amount or some other amount proposed by the Scheme Administrators, "then the Scheme Administrators shall determine . . . in consultation with the Creditors' Committee, whether the claims of the Pre-1969 L&O Policyholders . . . are to revert to run-off and be agreed. . . and paid in accordance with the terms of the Original Scheme."[27] There reportedly has been a dispute in the past with the Reinsurers on their obligation to pay based on estimated future claims, but this procedure allows for a potential resolution after all claims are filed and evaluated. In any event, it may again take a significant amount of time after the Bar Date to determine whether such claims will proceed under the Amending

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Scheme or the Original Scheme. If the claims revert to run-off under the Original Scheme, policyholders would return to submitting claims on a regular basis as losses are incurred (and the Bar Date would not apply).

IV. CONCLUSION

Policyholders should carefully monitor the progress of the Amending Scheme and take steps to protect their interests, including the submission of all Claims Forms and/or, if applicable, Opt-Out Forms, prior to the Bar Date.

Notes:

[1] Generally speaking, capitalized terms herein are defined in the Amending Scheme.

[2] *See* Proposal in Relation to an Amending Scheme of Arrangement Between OIC Run-Off Limited, The London and Overseas Insurance Company Limited, and Their Respective Scheme Creditors ("Amending Scheme"), a copy of which is appended to the Order, *available at* https://www.oicrun-offltd.com/, § 7.1.

[3] *See* Scheme of Arrangement Between The Orion Insurance Company PLC, The London and Overseas Insurance Company, PLC, and Their Scheme Creditors, dated November 20, 1996 ("Original Scheme"), *available at* https://www.oicrun-offltd.com/.

[4] *See* Original Scheme, § 17.

[5] *See* Amending Scheme, § 6.1.

[6] *See* Amending Scheme, § 7.1.

[7] *See* OIC Run-Off Limited, https://www.oicrun-offltd.com/.

[8] *See* Amending Scheme, Appendix 1, at 187.

[9] *See* Amending Scheme, §§ 14.1, 14.2, 14.8.

[10] *See* Amending Scheme, § 15.1.

[11] *See* Amending Scheme, §§ 37.1.

[12] *See* Amending Scheme, §§ 37.1, 37.2; *see also* Amending Scheme, § 43, addressing the failure of a policyholder to submit a Claim Form prior to the Bar Date due to the alleged lack of knowledge of the Amending Scheme prior to the Bar Date.

[13] *See* Amending Scheme, § 19.1.

[14] *See* Amending Scheme, Appendix 2, at 200.

[15] *See* Amending Scheme, Appendix 2, at 203.

[16] *See* Amending Scheme, § 17.1.

[17] *See* Amending Scheme, § 18.

[18] *See* Amending Scheme, § 21.

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[19] *See* Proposal in Relation to An Amending Scheme of Arrangement Between OIC Run-Off Limited, The London and Overseas Insurance Company Limited, and Their Respective Scheme Creditors, dated October 8, 2014, § 20.2.3, *available at* https://www.oicrun-offltd.com/.

[20] *See* Amending Scheme, § 21.3.

[21] *See* Amending Scheme, § 21.4.

[22] *See* Amending Scheme, § 37.1.

[23] *See* Amending Scheme, § 41.2.

[24] *See* Amending Scheme, § 39.8.

[25] *See* Amending Scheme, § 37.

[26] *See* Amending Scheme, § 42.1.

[27] *See* Amending Scheme, § 42.2.

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