EXPERTISE

The Newsletter of GBRW Expert Witness

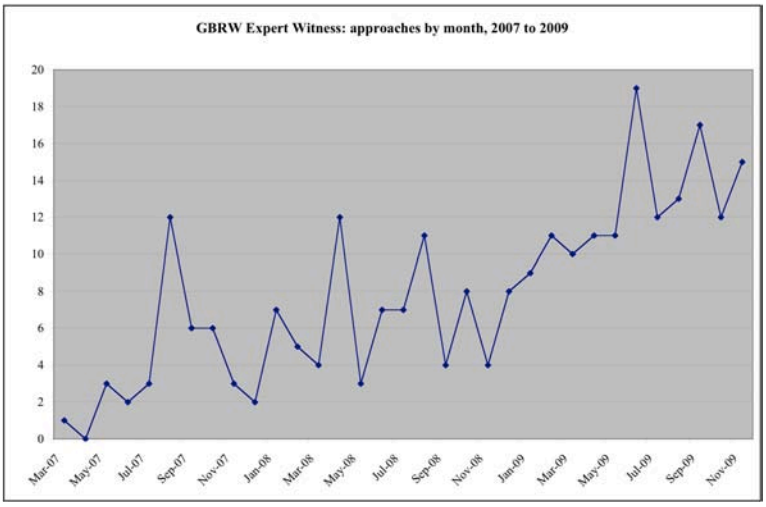
Expert advice - demand grows sharply

In the 11 months to the end of November, GBRW received 140 approaches for expert advice – almost twice the figure for 2008, which itself was double the previous year. While part of this growth reflects the inclusion of the insurance practice of Associated Insurance Experts in this year's numbers, the driving factor has undoubtedly been the increased number of disputes moving through the judicial process.

We have been analysing the timing and results of approaches from law firms, which throws up some interesting results:

- As the graph below shows, there are major spikes in demand in the July-August period each year, with a secondary spike early in the New Year. These are of course times when many experts are likely to be on holiday (some, but not all, ensuring that they are still contactable).
- This year's summer demand has continued through to the end of November – we're waiting with interest to see when the legal profession starts to wind down in the run-up to Christmas.
- Roughly a third of approaches lead to instructions of the candidates we put forward. We believe that this reflects the fact that we're doing something right – specifically, responding as rapidly as possible and ensuring that we propose individuals who are well matched to the requirements for expert evidence.

The conclusion? If at all possible, try to start searches for potential experts well ahead of the summer holiday and post-New Year peaks. You'll find them easier to contact, more receptive to new instructions and (hopefully) not already conflicted by an approach from the other side.



Areas of Expertise include:

BANKING & FINANCIAL:
- Corporate Lending
- Personal Lending
- Risk Management
- Investment Banking
- Corporate Finance
- International Banking
- Correspondent Relationships
- Commercial Property
- Residential Mortgages
- Syndicated lending
- Loan Workouts
- Recoveries and Realisations
- Back Office Procedures
- Trade Finance
- Letters of Credit
- Leasing
- Credit and Debit Cards
- Know Your Customer
- Anti Money Laundering
- Anti Terrorist Financing

INVESTMENT MANAGEMENT
- Investment Services
- Investment Advice
- Fund Management
- Structured Investment Funds
- Stockbroking
- Hedge Funds
- Options, Swaps, Derivatives
- Treating Customers Fairly
- Pensions

FINANCIAL MARKETS:
- Money Markets
- Commodities Markets
- Securities Trading
- Financial Instruments

INSURANCE:
- Property Insurance
- Professional Indemnity
- Life Assurance
- Broking
- Underwriting
- Reinsurance
- Regulation
- Actuarial issues
- Loss Adjustment
- Treating Customers Fairly

BUSINESS FINANCE:
- Limited Companies
- Partnerships
- Private Companies
- Sole Traders
- Mergers & Acquisitions
- Treasury Management
- Sales of businesses
- Property Finance
- Business Planning
- Company Valuation
- Venture Capital

OTHER AREAS:
- Employment Disputes
- Loss of Earnings
- Compensation Calculations
- Arbitration and Mediation

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You wouldn't sell option contracts - would you?

It is a basic principle that selling options is far more risky than buying them, for one simple reason – the buyer of an option gets the *right* to undertake the transaction but does not have the *obligation* to do so; the seller on the other hand has an obligation to honour the transaction if the buyer of the option wishes to exercise it. The risk is heightened if there is no underlying commercial exposure to match the option sold – the so-called selling of a "naked" option.

It makes little sense for most companies to sell options given this risk/return profile and, as you would expect, very few non-financial companies will do so.

...selling options is far more risky than buying them...

However, over the last few years a new range of derivatives products sold by banks to protect against interest or exchange rate risks has grown up. One that we have seen increasingly is a structure where a company buying protection against movements in interest rates simultaneously sells options which are used to enhance the rate that the bank offers. For example, a floating to fixed interest rate swap may offer a fixed rate which is lower than the market rate for fixed loans of that maturity. The bank achieves this by "embedding" one or more interest rate options in the bank's favour in the swap documentation – and it is the premiums from the sale of those options which are used to reduce the interest rate.

The headline rate may therefore look attractive, but what has been lost is full protection if interest rates go up. After an initial grace period (which will generally be shorter than the maturity of the underlying financing), the bank has the right to exercise its option if the fixed rate on the swap is lower than prevailing market rates – at which point the customer loses the protection which was the rationale for entering into the swap.

The bank's documentation may be factually accurate, but also may not highlight the implications of the transaction structure under different scenarios. In some cases, the bank's own officers may not have fully understood these implications – or may not have asked themselves whether the transaction is in the customer's best interests.

Some clients involved in property investment or development may also be experiencing a "double whammy", where the value of their underlying asset has declined while the protection supposedly offered by an interest rate swap has fallen away.

Lawyers whose clients complain that they have been mis-sold a hedging product should bear in mind the possibility that the rate has been enhanced by the use of embedded options.

It should be emphasised that not all products of this type will have been mis-sold and in many cases the client will have entered the transaction with their eyes wide open – but this will not always be the case.

If you need help to analyse such products or to assess potential evidence of mis-selling, GBRW Expert Witness can provide the necessary expertise.

New Experts

In previous newsletters we have talked about the need to identify new experts to address current requirements for expert evidence. In this section we introduce two people who have started working with GBRW Expert Witness this year - Robert Owen and Richard Palette.

Robert Owen has over 30 years experience in financial services, with a specific focus on retail finance, including mortgages and personal lending. This has included 8 years as Managing Director of Matlock Bank and Kensington Personal Loans, prior to which he held senior positions with Lloyds TSB and a number of Building Societies.

In addition to his expert work with GBRW, Robert is Chief Executive of a consultancy firm which specialises in the financial services sector, providing corporate governance, compliance, risk management and strategic planning/implementation. He is also a Non-Executive Director of the Islamic Bank of Britain plc.

Continued Overleaf...

Richard Palette has just retired from RBS after nearly 40 years experience in retail financial services, banking operations and internal audit.

His career has spanned both “front line” experience handling personal customers and small to medium sized businesses and wide ranging “back office” internal audit work. Richard’s most recent position prior to retiring from RBS was as Head of Professional Practices, Group Internal Audit.

It will come as no surprise that there has been a steady demand this year for Richard’s and Robert’s experience and we anticipate that mortgage and personal lending and banking fraud will continue to keep them busy over 2010!

In our next edition:

Legal Aid

By the time we publish our next edition, the Legal Services Commission’s proposals to reduce the costs of expert evidence may have crystallised. We plan to comment on the impact of these proposals on our own work in the legally aided field.

Micro Insurance

GBRW also has an active financial services consulting practice which complements our expert work. Our colleague John Pott describes a pioneering micro-insurance project which he has been working on for the past four years. It provides a sobering contrast to some of the disputes which we see in our expert practice.

Most people are aware of microcredit and of the work done by Grameen Bank in Bangladesh. Micro-insurance is a much more recent development, having only emerged in the past five years as a new component of the broader microfinance sector. However, it holds great potential for helping poor families cope with the risks to which they are vulnerable. In India, for instance, one third of poor families who are unfortunate enough to have a member of the family admitted to hospital for treatment descend into absolute poverty for several years, sometimes up to a decade.

Micro-insurance presents traditional insurance providers with a whole new set of challenges. Firstly, low income families have a short financial horizon, requiring insurance products that promise tangible benefits within a short period of time. Secondly, with affordable premiums of only a few dollars a year, the only economic way of selling insurance and servicing claims is through promoting a group insurance scheme using a distributor such as a Microfinance Bank - equipped with the systems and personnel which are well attuned to the needs of the micro-market.

GBRW has been providing consultancy advice since mid-2005 to the Aga Khan Agency for Microfinance on the development of innovative insurance products and services in two countries: Pakistan and Tanzania. In 2008 the First Micro-insurance Agency was established in the Pakistan market. The Agency manages product development, marketing, sales, and claims management for a leading private sector insurer, which retains the insurance risk. This partnership with an established commercial insurer has enabled AKAM quickly to begin providing dedicated Micro-insurance products to poor families. A similar arrangement has recently been established in Tanzania.

A mixture of simple and complex products is being tested in both countries, including credit-linked life insurance, a short term savings/insurance product, low-cost hospitalisation cover and a more comprehensive health product which offers full in-patient and childbirth coverage. The fact that more than 70% of individuals in the micro-market either own or have access to a mobile phone promises substantial technological advances for insurance providers serving this market.

Hospitalisation insurance products are being offered to the micro-market at around $5 per person per year...

Insurance products which help address the health concerns of the micro-market are proving the most popular both in Pakistan and Tanzania. The hospitalisation insurance products are being offered to the micro-market at around $5 per person per year, providing simple but acceptable care for poor families and encouraging them to visit hospital earlier rather than later. Without insurance, families frequently delay hospital visits, in the vain hope that they will get better. Instead, this leads more often than not to more expensive, more complex treatments and in some cases permanent damage to health.