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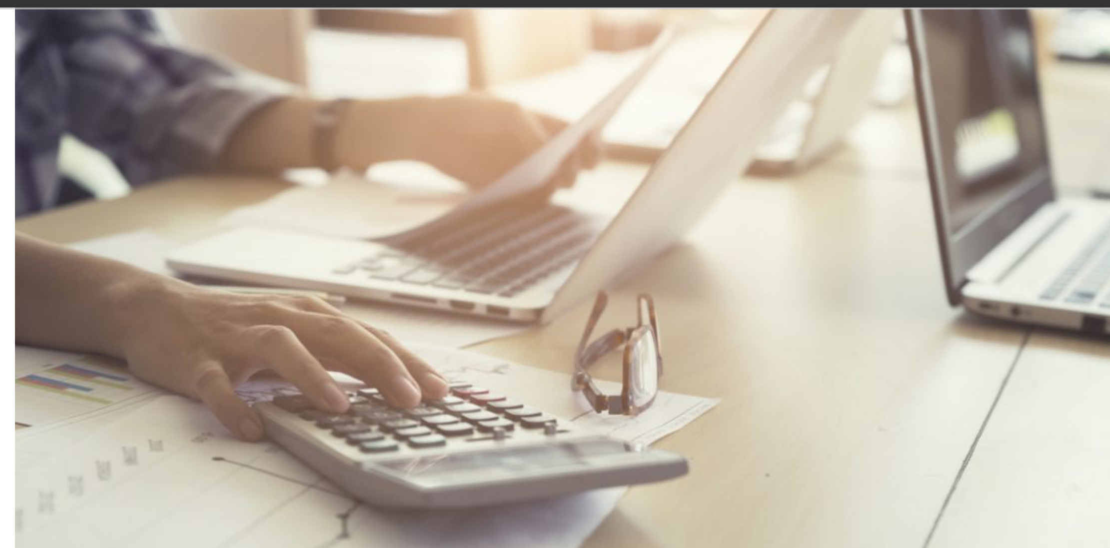

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# Added assurance

**ANDREW SAUNDERS** | FEATURES | ANGUS DENT, ARCHOVER, CHRIS HOY, CMR, INSURANCE, KUFLINK, MARKETINVOICE, NARINDER KHATTOARE, SEAN ALEXANDER

*Why are peer-to-peer lenders split on the attractions of credit insurance? Andrew Saunders investigates...*

ON THE face of it, peer-to-peer lenders and insurance companies make slightly uneasy bedfellows. Rather like the high street banks, traditional insurance companies are seen by many P2P entrepreneurs as part of the financial services establishment – the old order with its outdated methods that P2P is setting out to shake up and disrupt.

But just as many P2P platforms are discovering the benefits of hooking up with one former 'enemy', partnering with those same banks to service borrowers they might not otherwise be able to

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reach, could something similar, if lower-key and as yet less widespread, be happening with insurance?

loan schemes

This is particularly noticeable within credit insurance, which a number of platforms now provide as an option to borrowers and as an added safeguard – in theory at least – to lenders.

One of the first platforms to offer credit insurance was ArchOver, and its original 'secured and insured' lending model remains very popular with lenders – despite the fact that the platform offers higher returns on uninsured borrowers, says chief executive Angus Dent.

"We have five lending models, but secured and insured [which requires borrowers to take out credit insurance] is the original flagship product," he explains. "A good proportion of our customers will only lend secured and insured."

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ArchOver has made around £85m in loans to small- and medium-sized enterprises (SMEs) since 2014 – typically between £100,000 and £15m for working capital. Although loans are secured primarily against a property asset, the additional safeguard of credit insurance is well worth having, according to Dent.

"If a company has a £2m factory, for example, you can bet that it will be fully insured," he comments. "But look at the balance sheet of most businesses and their biggest asset is the money that customers owe them. Why wouldn't you insure that too?

"Credit insurance makes the asset that we usually lend against better quality and more secure. As a lender you always look at the quality of the asset – if you can enhance that then you do."

So what exactly is credit insurance, and how does it work?

"It's business-to-business insurance that insures against bad debts, insolvency, buyer default and political risks," says Chris Hoy,

managing director of broker CMR and the trade insurance representative for the British Insurance Brokers' Association.

"It's for any business from a listed company to a sole trader – anyone who is giving credit terms to anyone else, anywhere around the world."

Credit insurance thus allows a company to insure itself against the risk of one or any of its customers going bust or failing to pay and leaving them in the lurch financially. Insurers assess the risks of both overall sectors and of individual companies, and will set the level of cover they are prepared to offer accordingly. A typical fixed-cost SME policy, says Hoy, might provide a total of £1m of credit cover annually for a premium of around £3,000.

For many potential P2P investors who are not themselves in business, the first time they hear about credit insurance might well be media coverage of a struggling firm which has had its credit insurance cover withdrawn – House of Fraser and Debenhams being a couple of recent high-profile examples.

This happens, says Hoy, because credit insurers set limits to the amount of cover they are willing to underwrite against specific creditors, based on the financial information provided by those creditors. When a business starts getting into trouble, it becomes a larger credit risk and the insurers start to reduce or withdraw that cover. "Credit insurers can get the blame for bringing a company down," he says, "But really they are only making decisions on the basis of information supplied by those companies."

While credit insurance is typically taken up by larger companies, the benefits of being insured are equally, if not more, applicable to SMEs too. “Credit insurance is important for SMEs because one bad debt could take them out,” explains Hoy. It can also help them grow. “An SME can expand its business through taking out credit insurance. It can enable them to offer credit to some suppliers which they have only been dealing with on cash terms,” he adds.

Since 2015, ArchOver has had a deal with French provider Coface – the second-largest provider of credit insurance in the world – to provide a total of £100m cover for its borrowers. It’s an umbrella policy, explains Dent, bought at a wholesale rate and parcelled out by ArchOver as required to individual borrowers. “We get the credit insurance at the rate a big company would,” he says. “We split it down to our SME customers and we don’t charge a mark-up. Borrowers pay 0.14 per cent of annual turnover.”

Business finance provider MarketInvoice also has a credit insurance partnership, offering cover to its borrowers through a deal with Euler Hermes. The deal was established earlier this year as a result of customer interest, says MarketInvoice’s head of risk Sean Alexander. “Initially we didn’t offer credit insurance, the decision was driven by customer demand – it was something they told us they had a need for.”

Not only does credit insurance provide MarketInvoice’s lenders with additional peace of mind, it is also of benefit to borrowers. “We want to encourage our customers to protect their revenues, especially if they work in a sector with a high level of defaults, or are particularly reliant on one or two large customers,” explains Alexander.

Unlike ArchOver’s offering, it’s a referral deal – the platform does not buy cover wholesale and credit insurance is not a requirement of any MarketInvoice loans. “Some lenders take an umbrella policy and parcel it out,” Alexander says. “We decided to go down the individual referral route. We recommend Euler Hermes but it is the borrower’s decision whether to use them.  It’s not a compulsory part of our lending at all.”

It also helps to avoid the risk of bank-style mis-selling, he continues. "In the past, some banks have become too reliant on third-party providers and that has led to mis-selling. Our customers are perfectly free to get quotes from other providers if they wish."

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The advantages of credit insurance don't only apply in the event of default or bankruptcy. It can also provide the insured with access to valuable market intelligence on the creditworthiness of customers.

"None of our borrowers, for example, were caught out by Carillion going down because the credit insurers had been withdrawing their cover aggressively," says ArchOver's Dent. "For SMEs who generally do not have the time or resources to conduct ongoing credit assessments on their customers, that kind of information can be crucial."

But by no means is everyone in the sector as sold on of the benefits of credit insurance. One risk, say some sceptics, is that platforms might be tempted to skimp on vital underwriting because the insurance will cover them for any mistakes.

Narinder Khattoare, founder and chief executive of buy-to-let, development and bridging loan platform Kuflink, remains unconvinced of the need. "Our investors don't really ask about insurance," he asserts. "We already provide a good level of security – all our loans are secured against property anyway and at a maximum LTV of 70-75 per cent."

As a former insurance executive with both Towergate and the Prudential, he has thought long and hard about how insurance might be able to help protect investors.

“When we went in to the market, we looked at what insurance cover we could get,” says Khattoare. “We even talked to Lloyds of London. But it’s difficult, there isn’t much out there.”

So instead, Kuflink takes a five per cent stake in every loan it makes, to ensure that the interests of lenders and the platform remain aligned. “Investors are happy with our five per cent skin in the game, and with our ‘first-in-last-out model,” he says. “They like that.”

To maximise security, Kuflink takes out title indemnity insurance on the properties it lends against. This covers them against any problems with property title as well as making for a slick process, according to Khattoare. “Getting a full title report from a solicitor can take weeks, so that speeds up the process,” he explains.

The relative novelty of P2P as a sector means that it can be harder for platforms to obtain business insurance of all kinds, not just credit insurance. “The insurers look at P2P and they don’t understand who to cover,” he says. “Is it the lenders, or the borrowers?

“Plus all the platforms are very different, there are hardly any two the same.”

It all makes the risks hard to quantify – and thus hard to underwrite. As P2P lending becomes increasingly mainstream and well-regulated, the insurance industry will catch up and start offering new products and services, he says, but it is not there yet.

So within the P2P sector, the jury remains out on whether, right now, credit insurance is really worth the candle. But the post-Brexit vote economic fog is driving an upsurge in interest in the SME community more widely, says Hoy. “There is so much uncertainty at the moment,” he comments. “In the last 24 months we have seen a big increase in enquiries, up to 50-70 a month from maybe 20-30.

Accountants, brokers and financiers are increasingly recommending credit insurance."

MarketInvoice's Alexander agrees that changes in the wider climate make the costs and administrative burden of obtaining credit insurance look increasingly worthwhile, both for lenders and borrowers. "There are higher levels of delinquency and more customers seeking to extend their payment terms," he says. "All of that suggests that it might be a good time to take action.

"If the risk of a failure far exceeds the cost of paying for cover, then you have value for money. Unfortunately, it's only after it starts raining that many SMEs end up wishing they had bought an umbrella."

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**BUSINESS INSURANCE BASICS**

In addition to specialist trading cover such as the credit insurance discussed in the main article, there are also a wide range of more general business insurance policies available either directly or via brokers. Some are legal requirements, but many are not – here is a brief summary of the main types.

**Employers' liability insurance**

This covers compensation claims from employees who are injured or become ill as a result of their work, and also the legal costs of defending any claim.

**Public liability insurance**

One of the most common forms of business insurance, this covers you against third parties being injured in some way by your business, or if you cause damage to someone else's property as a result of your work.

**Professional indemnity insurance**

Provides cover for compensation and legal costs for professionals in the event of a customer losing money as a result of work or advice

provided by them. It can also cover some instances of data loss or infringement of privacy.

**Directors' and officers' insurance**

Covers the directors of a company against personal liabilities arising from business risks such as breach of contract, investigation by regulators, and creditors seeking payment of outstanding debts.


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