

KPMG LLP
Restructuring
8 Salisbury Square
London EC4Y 8BB
United Kingdom

Tel +44 (0) 20 7694 1864
Fax +44 (0) 20 7694 3126
DX 38050 Blackfriars

To all known creditors and members of
Cotesworth Insurance Services Limited (in
liquidation)

Our ref tar/dc/985

05 April 2007

Dear Sir/Madam

Cotesworth Insurance Services Limited (“in liquidation”) (“CIS”)

1 Introduction

This is the fifth annual report to the creditors and members of CIS. CIS was placed into creditors’ voluntary liquidation on 26 September 2001. The liquidators of CIS are Tom Riddell and John Wardrop, partners of KPMG LLP, UK.

The company is one of a number of companies in the HIH Group of Companies (“HIH Group”) which have been subject to insolvency proceedings in the UK and over which Messrs Riddell, Wardrop and, in some cases Tony McMahon, also a partner in KPMG LLP, are appointed.

2 Brief details of the company

CIS was incorporated in the UK on 21 October 1999 to provide underwriting and management services for the Cotesworth companies and Lloyd’s syndicates. In particular it acted as managing general agent for syndicate 228’s Protection and Indemnity (“P&I”) business. The company continued as a managing general agent until the failure of the group in September 2001.

Prior to the failure of the group, staff formerly employed by CIS transferred to Cotesworth & Co Limited and continued to carry out some run-off work on the old P&I business written by syndicate 1688 as well as continuing to act for syndicate 228.

The directors of the company who held office at the time of its failure or in the previous two years were as follows:

Directors: NW Britten

 G Davies

BG Devereese

D Fodera (resigned 16/2/01)

RR Williams (resigned 16/2/01)

DA St John Cope (resigned 19/11/99)

NSB Gould (resigned 19/11/99)

Company secretary: W Scott

Shareholding: The company is a wholly owned subsidiary of Cotesworth Holdings Limited. The ultimate beneficial owner is HIH Insurance Ltd which was publicly listed in Australia and is now in liquidation.

3 Details of the relationships with HIH and background to the failure

The principal UK operations of the HIH Group comprised HIH Casualty & General Insurance Limited (“HIH C&G”), writing business in the UK through a branch operation, and the Cotesworth Group of Companies, writing business in the UK through membership of Lloyd’s syndicates.

The HIH Group acquired the Cotesworth group in October 1998 to benefit from the global underwriting licences available to Lloyd’s syndicates. The acquisition consisted principally of a Lloyd’s corporate capital vehicle (Cotesworth Capital Ltd (“CCL”)) and an associated managing agent (Cotesworth & Co Limited) which wrote business through five Lloyd’s syndicates. CCL held interests in one newly formed syndicate (1688) and majority interests in four others (535, 536, 228 & 1069). Prior to the acquisition, CCL was owned by approximately 14 individuals.

In order to participate in a syndicate’s underwriting, a corporate name must maintain funds at Lloyd’s (FAL) as security. The FAL required to be maintained by Cotesworth at Lloyd’s varied but at December 2000 the FAL requirement stood at £110 million. This FAL security took the form of letters of credit collateralised by assets from HIH Group companies in Australia.

With the insolvency of HIH Group companies in March 2001, the Cotesworth FAL security of £110m with Lloyd’s remained in place. However, it was then clear that no further HIH support would be available, and that the Cotesworth group would need to secure alternative sources of backing if it wanted to expand its business, or if it incurred losses. The Cotesworth syndicates had in fact already incurred significant losses, and accordingly CCL needed further funding for its 2002 underwriting at Lloyd’s if the syndicates were to continue underwriting. Cotesworth & Co engaged Noble & Co to seek a buyer and worked closely with the joint provisional liquidators of HIH C&G and Lloyd’s to determine whether a sale of the group could be achieved.

During the following six months the Cotesworth syndicate losses continued to escalate, and no buyer was found. Further major losses included exposures to insolvent debtors and the Petrobras platform loss. Accordingly, the Cotesworth syndicates suspended underwriting on 17 August 2001 and ceased underwriting on 3 September 2001.

On 26 September 2001, the Deputy Chairman of Lloyd’s exercised power to replace Cotesworth & Co as the managing agent of the Cotesworth syndicates. Lloyd’s By-laws do not allow an insolvent company to act as a managing agency. Capita Syndicate Management Limited (“Capita”) was appointed as the substitute managing agent for the syndicates. Companies in the Cotesworth group had no future prospects and directors of each of the companies resolved to place them into insolvency proceedings.

CIS was placed into creditors’ voluntary liquidation on 26 September 2001.

4 Assets

Asset	Note	Statement of Affairs	Updated Trial Balance as at 25 September 2006
		£	£
Inter-company debtors/LOCs	4.1	-	46,471
Corporation tax	4.2	16,658	-
VAT refund	4.3	5,051	-
Cash	--	79,898	90,267
Premium receivable	4.4	307,449	-
Management fees	4.5	517,309	-

4.1 Inter-company debtors/LOCs/Guarantees

Three LOCs were written under the HIH Casualty & General (“C&G”) facility with RBS where CIS is understood to have reimbursed C&G for the collateral.

Funds of £232,355 have been returned to C&G’s collateral accounts at RBS to which the liquidators have no access. The Liquidators took legal advice as to who should retain the funds once those funds are released by RBS to the liquidators. The advice is that funds should be retained by C&G for the benefit of creditors, but that CIS will have a claim against the C&G estate. The liquidators consider that this asset is 20% realisable (£46,471) as HIH C&G will pay a distribution to its creditors.

There were a further two Guarantees which are held in CIS’s facility at RBS with a combined value of €554,590.77, supported by cash deposits. The Liquidators consider that these funds

should be regarded as held on trust for Syndicate 228 if the funds released by RBS and accordingly CIS now has no further interest in them.

4.2 Corporation tax

No corporation tax refund is expected to be recovered.

4.3 VAT refund

No VAT is expected to be recoverable.

4.4 Premium receivable

CIS collected the premium for the P&I business from the market on behalf of syndicate 228 and paid claims and expenses. Commission was payable to CIS based on 20% of gross premium less third party brokerage.

The liquidators do not consider the premium receivable listed in the report as to Statement of Affairs to be recoverable.

4.5 Management fees

The £517,309 shown on the Statement of Affairs was due from HIH (UK) Ltd for work undertaken by CIS staff for work on the 1999 and prior years P&I business. The directors of CIS and HIH (UK) Ltd subsequently decided that rather than CIS billing HIH (UK) Ltd direct it would bill through Cotesworth & Co. It is understood the reason for restructuring of intercompany balances was to reduce these balances by set-off.

The £517,309 was therefore billed to Cotesworth & Co and is included within the inter-company balance with Cotesworth & Co. The Liquidators do not expect any balance to be recoverable as management fees.

5 Liabilities

5.1 Preferential Creditors

No preferential creditors have been identified.

5.2 Non-preferential creditors

Liability	Note	Statement of Affairs £	Updated Trial Balance as at 25 September 2006 £
Inter-company creditors	5.3	612,229	402,904
Sundry creditors	5.4	474,553	16,052

5.3 Creditors

£211,525 is owed to Cotesworth & Co and £191,379 to Syndicate 1688.

5.4 Sundry creditors

Although £474,553 was shown as owing to sundry creditors in the Statement of Affairs, at this stage only £16,052, being commission owing to brokers, has been identified by the liquidators as a likely provable debt.

6 Dividend prospects

At this stage the liquidators do not consider that any significant dividend will be payable.

7 Other Issues

7.1 Taxation

7.1.1 Corporation Tax

All tax returns have been submitted up to 26 September 2005. To date no queries have been raised by the Inland Revenue.

7.1.2 VAT

The HIH VAT group has 10 members of which HIH C&G is the representative member. As such, CIS will continue to be jointly and severally liable for any unpaid VAT debts that arise from other group members’ activities. No liability is expected for CIS.

8 Receipts and Payments

A summary of the liquidators' receipts and payments from the commencement of the liquidation to 25 September 2006 is set out below.

Cotesworth Insurance Services Limited (in liquidation)	
Receipts and Payments for the period 26 September 2001 to 25 September 2006	
<u>Receipts</u>	
Proceeds from company bank accounts at 26 September 2001	79,898
Other receipts	32,854
Total receipts	<u>112,752</u>
<u>Payments</u>	
Other professional fees	10,696
Secretary of State	1,466
Legal fees	4,624
VAT & Tax	5,495
Other payments	204
	<u>22,485</u>
<u>Funds held at 25 September 2006</u>	<u>90,267</u>

9 Liquidators' remuneration

The liquidators' remuneration in a creditors' voluntary liquidation is normally fixed by the Liquidation Committee (if one exists) or the creditors, if no Committee exists. At the Section 98 meeting held on 11 October 2001 it was resolved that no Liquidation Committee be established. A circular prepared by the Association of Business Recovery Professionals (R3) explaining remuneration in insolvencies is attached for creditor information.

At the annual creditors' meeting held on 10 December 2002 a resolution was passed to fix the liquidators' remuneration by reference to the time properly given by the liquidators and their staff in attending to matters arising in the insolvency, at the same rates as are approved from time to time by the Court for the principal insolvencies in the HIH group in the UK.

For the year to 25 September 2006 £6,624.00 excluding VAT has been charged by the joint liquidators and their staff representing 36.9 hours of their time.

A detailed breakdown of the time charged and the nature of the work conducted is attached. The breakdown details changes to the hourly staff rates which occurred during the year. These fees have not yet been drawn.

10 Meetings of Creditors and Members

The fifth annual meetings of creditors and members will be held in London on 04 May 2007 at 11.30am and 11:45am respectively at KPMG LLP, 1-2 Dorset Rise, London EC4Y 8EN. Creditors and members will have the opportunity to question the liquidators over matters in this report. In order that we may anticipate numbers attending, please contact Michael Maccallum on +44 (0) 20 7694 3459 or by email at Michael.Maccallum@kpmg.co.uk if you intend to attend either meeting. Notice of each meeting is enclosed with this report together with a proxy form and proof of debt form.

Yours faithfully
for CIS

TA Riddell
Joint Liquidator

Enclosures: A Creditors guide to liquidators’ fees
Schedule of liquidators’ fees and expenses
Notice of meeting
Proxy form
Proof of debt form