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To all known creditors, potential creditors and  
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13 October 2009

Dear Sir/Madam

**HIH Casualty & General Insurance Limited (In Provisional Liquidation and subject to  
Scheme of Arrangement)  
English Scheme Administrators' Annual Report to Creditors**

**1 Introduction**

This is the 3<sup>rd</sup> Annual Report to creditors of HIH Casualty & General Insurance Limited ("HIH C&G") by the English Scheme Administrators. It will be published on the HIH website as a supplement to the Annual Report to creditors of the Australian Scheme Administrators, for the year ended 30 June 2009.

Background information in relation to the failure of HIH C&G is contained in Appendix 1. The purpose of this report is to provide creditors with information on the progress of the English Scheme to date.

**2 Key developments since the last report**

- The current Scheme Payment Percentage for HIH C&G under the English Scheme for those claims which are Insurance Liabilities not in the Australia is 16.28%. The remaining creditors of the English Scheme have been paid 9%. Scheme distributions are paid quarterly for those Scheme Creditors with Established Scheme Claims (see section 3.1).
- The English Scheme Administrators have focussed more efforts during the year on paying an increasing number of reinsurance creditors, although always conditional upon the Scheme Creditor undertaking to repay any overpaid distribution in the event of significant offset developing (see section 3.4).

- Following negotiations by the Scheme Administrators, the House of Lords costs have been finalised and settled at £750,000 compared to an initial claim of £1,268,000. Further details of the effect on English Scheme Creditors are set out in section 3.2 of this report.

### **3 Scheme Payment Percentages**

#### *3.1 Current Scheme Payment Percentages*

The current Scheme Payment Percentage for claims which are Insurance Liabilities not in Australia is 16.28%. This is an increase from 9% set out in the 2<sup>nd</sup> Annual Report to creditors (which was a pari passu distribution paid prior to the House of Lords decision) and is made up of an 8% distribution out of reinsurance assets not in Australia and a 9% distribution on the residual balances out of non reinsurance assets not in Australia.

The current Scheme Payment Percentage for the remaining UK creditors is 9%. This is unchanged from the 2<sup>nd</sup> Annual Report to creditors.

The Australian Scheme Administrators have also made equal distributions of 16.28% and 9% to Australian Insurance and non-insurance creditors respectively. Also, a Scheme Payment Percentage of 16.28% for those US domiciled creditors eligible to be paid from US Trust Fund assets has now been paid.

The current Scheme Payment Percentages for the various classes of assets for all of the HIH Scheme companies, of which HIH C&G is one, are set out on the HIH website, [www.hih.com.au](http://www.hih.com.au).

#### *3.2 House of Lords costs*

As outlined in the 2<sup>nd</sup> Annual Report to creditors, the House of Lords ruled that the English assets will be distributed in accordance with Australian priorities. In addition, the Lords awarded the Australian Insurance Creditors (Amaca Pty Limited and Amaba Pty Limited, formerly known as the James Hardie Trust) their costs. The costs award covers all the proceedings including the initial High Court hearing, the appeal to the Court of Appeal, the action in the House of Lords and the final hearing in the High Court to implement their Lordships' Order.

The total of Clifford Chance's claim (acting on behalf of the Australian Insurance Creditors) against the English Scheme Administrators in relation to the House of Lords action was approximately £1,268,000. Following negotiations, the Scheme Administrators agreed on a figure of £750,000 in full and final settlement of these claims.

#### *3.3 How the Scheme Payment Percentages are set*

The Australian Schemes (and, following the House of Lords decision, the English Schemes) reflect the distribution priorities which apply to liquidations of insurance companies in Australia. This requires particular classes of assets to be distributed in priority to particular classes of creditor claims.

Under the terms of the Schemes, the Australian and English Scheme Administrators review the Scheme Payment Percentage for each relevant class of asset in consultation with the Creditors' Committees. Factors taken into account include current cash held, expected future asset realisations, expected future claims agreement levels and the remaining potential volatility of the account.

The objective in setting the Scheme Payment Percentages is to make interim distributions to creditors currently holding Established Scheme Claims, whilst ensuring that HIH C&G will be capable of meeting that same percentage on all eligible liabilities reasonably expected to be admitted in the future.

#### *3.4 Scheme Payments for reinsurance creditors*

Agreed claims (described as "Acknowledged Creditor Claims" under the Scheme) of HIH C&G's reinsurance creditors have generally not yet been accepted as Established Scheme Claims by the Scheme Administrators, and so the majority of reinsurance creditors have not yet been paid any Scheme distributions.

The reason for this is the difficulty in identifying all potential future set-off. The HIH companies wrote both inwards and outwards reinsurance business, in more than one location, and significant set-off is expected. In common with many solvent insurers, prior to insolvency the HIH Group did not maintain their insurance records on a principal to principal basis which means that the Scheme Administrators are not able to readily identify all transactions with a particular principal. However, considerable improvements to information management have now been made through the introduction of a P to P system

During the year, the Scheme Administrators have focussed efforts on paying an increasing number of reinsurance creditors, although always conditional upon the Scheme Creditor undertaking to repay any overpaid distribution in the event of significant offset developing. Other factors driving this increased focus are more reinsurance creditors demanding payment, particularly if their debt has been assigned to a purchaser, and reinsurers making a dividend payment a condition of collecting a UK or Australian outwards balance. Scheme Creditors interested in this should contact either the appointed UK run-off agent or the English Scheme Administrators. Contact details are contained in Section 8 of this report.

#### *3.5 Estimated ultimate Scheme Payment Percentages*

The summary estimates of the ultimate Payment Percentages per company given by the Scheme Administrators are shown below and compared to the original estimates. These estimates are dependant on a wide range of factors including the volatility of claims; levels of set-off; litigation outcomes; levels of reinsurance recovery; and the class of creditor claim. It is possible that the ultimate Payment Percentages could vary significantly either above or below those predicted.

In addition the final result for individual creditors will vary according to whether their claims are insurance or non-insurance, and whether their claims are Liabilities in Australia or Liabilities not in Australia. As a generalisation, creditors with insurance Liabilities in Australia are expected to receive higher ultimate distributions than creditors with Liabilities not in Australia.

Most creditors who wrote their business with the UK branch of HIH C&G will not have those claims classed as Liabilities in Australia, and can expect to receive distribution rates towards the lower end of the range for HIH C&G.

<b>Scheme Company</b>	<b>Initial Estimated Ultimate Scheme Payment Percentage</b>	<b>Revised Estimated Ultimate Scheme Payment Percentage</b>
HIH C&G	15% to 25%	12% to 35%
FAIG	40% to 50%	45% to 55%
FAII	Less than 5%	30% (insurance creditors) 8% (non insurance creditors)
WMG	10%	30% to 95%
CIC	40% to 50%	55% to 65%
FAIT	Less than 5%	Less than 5%
FAI Re	More than 50%	100%
HIH U&I	5% to 10%	5% to 25%

Additionally, the Australian and English Scheme Administrators have modelled the expected return for the differing types of claims against HIH C&G. These are shown below:

	<b>Range of estimated Scheme Payment percentage</b>
Creditors with insurance liabilities in Australia	25% - 35%
Creditors with insurance liabilities not in Australia (including the beneficiaries of the US Trust fund)	20% - 30%
Creditors with non insurance liabilities in Australia	20% - 25%
Creditors with non insurance liabilities not in Australia	12% - 15%

#### **4 Interaction between Australian and English Schemes**

##### *4.1 Claiming under the Australian and English Schemes*

All creditors worldwide are entitled to claim in both the Australian and English Schemes for HIH C&G. The Australian and English Scheme Administrators co-operate fully and Scheme Creditors need to lodge claims in one location only, which is then effective under both schemes. The place a Scheme claim is lodged has no bearing on whether it is a liability "in Australia" or "not in Australia".

The Australian and English Scheme Administrators and their respective run-off managers operate a unified principal to principal ledger system and a unified dividend payment system. The entitlements of individual creditors under both schemes are automatically calculated, and when a Scheme payment is made, the creditor receives a statement showing how their liability has been classified, and therefore from which classes of assets their distribution has been paid.

#### **5 Financial position**

##### *5.1 Gross Liabilities*

The English Scheme Administrators currently expect the gross undiscounted liabilities of HIH C&G to be approximately £2bn, of which approximately £270m relates to business written through the former UK branch. Approximately £207m of UK branch liabilities have been agreed as Acknowledged Creditor Claims to date.

5.2 *Receipts and payments to 30 June 2009*

A summary of the English Scheme Administrators' receipts and payments from 1 July 2008 to 30 June 2009 is set out below.

<b>HIH Casualty &amp; General Insurance Limited</b>		
<b>Receipts and payments for the period 1 July 2008 to 30 June 2009</b>		
	<b>1 July 2008 to 30 June 2009 £'000</b>	<b>1 July 2007 to 30 June 2008 £'000</b>
<b>Receipts</b>		
Insurance and reinsurance recoveries	8,447	31,532
Gains and interest on funds invested	2,485	3,182
Tax refunds	92	317
Recoveries from Intergroup Companies	-	1,965
LOC collateral refunded	315	-
<b>Total receipts</b>	<b>11,339</b>	<b>36,995</b>
<b>Payments</b>		
Officeholders' fees and expenses	1,577	1,182
Run-off managers' fees	1,042	1,485
Legal fees	1,661	481
Other professional and agents' fees	301	321
VAT	312	335
IT and market processing costs	135	200
Other payments	204	129
Priority Payments to the Australian Estate	-	6,019
<b>Total Payments</b>	<b>5,232</b>	<b>10,152</b>
<b>Balance before Scheme Payments</b>	<b>6,107</b>	<b>26,843</b>
Exchange Gain/(Loss) on Currency Conversion as at 30 June 2009 & 2008	(3,495)	2,071
Scheme Payments to creditors	(6,176)	(3,685)
<b>Total</b>	<b>(3,564)</b>	<b>25,229</b>
<b>Equivalent GBP funds held as at 30 June 2009</b>	<b>75,574</b>	

## 6 Closure

The Scheme for HIH C&G provides for a planned Estimation Date of seven years after the Australian Scheme became effective, which means that the Estimation Date is expected to be in June 2013. By that time the Scheme Administrators expect that the majority of the reinsurance asset will have been collected or commuted, and the remaining tail of insurance liabilities will be sufficiently small to justify closure of the Scheme on cost benefit grounds. Under the terms of the Scheme all Scheme Creditors will be given notice of the actual Estimation Date between six and three months prior to that time.

The Schemes provide that the Estimation Date may be moved two years either way from the expected seven years (to be as early as five years or as late as nine years after the Effective Date) by special resolution of Scheme Creditors, on the recommendation of the Scheme Administrators and Creditors' Committees.

Following the Estimation Date all remaining outstanding and IBNR creditor claims will be crystallised by estimation, to allow for the closure of the Scheme.

## 7 Responsibilities

### 7.1 *Scheme Administrators*

The English Scheme Administrators of HIH C&G are John Wardrop and Tom Riddell, partner and senior advisor respectively of KPMG LLP, based in London. The Australian Scheme Administrators are Tony McGrath and Chris Honey, partners of McGrathNicol, based in Sydney.

### 7.2 *Run-off Managers*

The day to day claims handling and reinsurance recovery activities of HIH C&G have been outsourced to specialist run-off organisations in London and Sydney, who work in close co-operation. The run-off managers for all business written by the UK branch of HIH C&G are Whittington Insurance Services Limited. The run-off managers for all other business of the company are Capita CMGL.

### 7.3 *Creditors' Committee*

The interests of creditors in the English Scheme are represented by a Creditors' Committee. The Committee sanctions significant transactions (such as commutations), is involved in the setting of the Scheme Payment Percentage, and approves the Scheme Administrators' fees. It is reported to, and meets on a quarterly basis. The current constitution of the Committee is as follows:

<b>Member</b>	<b>Represented by</b>
Financial Services Compensation Scheme	Mr K Jefferies
Groupama (represented by Grant Thornton)	Mr E Walker
Markel International Insurance Company Limited	Mr G Appleton/Ms S Crofts
Riverstone Management Limited	Mr M Bannister
Syndicate 435, Faraday	Mr J Bond

**8 Contact details**

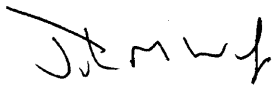
Contact details for the Australian Scheme Administrators, the English Scheme Administrators, and the Australian and English Run-Off Managers are set out on the HIH website, [www.hih.com.au](http://www.hih.com.au).

*8.1 Creditor enquiries*

Scheme Creditors with claims adjustment queries in relation to UK branch business should call Whittington on +44 (0) 20 7743 0900. Written claims adjustment queries should be directed in the first instance to Whittington at the following address: Whittington Insurance Services Limited, 33 Creechurch Lane, London, EC3A 5EB, Fax +44 (0)20 7743 0979.

Scheme Creditors with enquiries in relation to the Scheme or Scheme Payments should call the Scheme Administrators on +44 (0) 20 7694 3703. Written Scheme queries should be directed to the Scheme Administrators at the following address: KPMG LLP, 8 Salisbury Square, London EC4Y 8BB.

Yours faithfully  
*For HIH Casualty & General Insurance Limited*



John Wardrop  
*English Scheme Administrator*



Tom Riddell  
*English Scheme Administrator*

## Appendix 1

### Background information on the insolvency

- The HIH Group failed on 15 March 2001. HIH C&G was one of the 3 major licensed insurers in the group.
- Summary details of the history of the group; its failure; and other background information are available on the website maintained by the Australian Scheme Administrators at [www.hih.com.au](http://www.hih.com.au).
- Extensive information on the failure including the final report of the HIH Royal Commission established by the Australian Federal Government is available on the website [www.hihroyalcom.gov.au](http://www.hihroyalcom.gov.au)
- On 30 May 2006, Schemes of Arrangement became effective for the eight licensed insurance companies in the HIH Group in Australia. Complementary Schemes of Arrangement became effective for four of those companies in England on 13 June 2006, following approval by creditors and the courts. Copies of the Scheme documents are available on the HIH website [www.hih.com.au](http://www.hih.com.au).
- For at least the first five years, the Schemes will be “reserving” Schemes, under which claims are made in the normal course of business. During this reserving period, interim Scheme distributions will be paid to creditors with Established Scheme Claims at the current applicable Scheme Payment Percentage.
- The Australian and English Scheme Administrators co-operate fully. A unified principal to principal ledger system is operated, together with a unified dividend payment system. Creditors need to lodge claims in one location only, which is then effective under both Schemes.
- The Record Date (the date at which liabilities are measured) for each of the Schemes is 27 August 2001.
- There is no bar date for the Schemes during the reserving period. The earliest bar date permissible under the terms of the Schemes is in June 2011.