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To all known creditors, potential creditors and  
brokers of FAI Insurances Limited

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30 September 2010

Dear Sir/Madam

**FAI Insurances Limited (In Provisional Liquidation and subject to Scheme of Arrangement)  
English Scheme Administrators' Annual Report to Creditors**

**1 Introduction**

This is the fourth annual report to creditors of FAI Insurances Limited ("FAI Insurances") 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 2010, and should be read in conjunction with that Report.

Background information in relation to FAI Insurances 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 point**

The focus of the English Scheme Administrators during the year has been negotiating a resolution to FAI Insurances' involvement in the M.E. Ruddy Pool. This pool is a highly complex arrangement involving a number of solvent and insolvent stakeholders. The progress of this resolution has been hampered by long running disputes between the parties with competing objections and divergent interests.

**3 Scheme Payment Percentages**

*3.1 Current Scheme Payment Percentages*

There is no current Scheme Payment Percentage under the English or Australian Scheme for FAI Insurances Limited. The current ultimate expected outcome for creditors given by the Australian Scheme Administrators for FAI Insurances Limited is between 1% and 10% (see para 3.4 below). However these percentages are expected to apply to creditors with liabilities in



Australia only. The ultimate outcome for any creditors with liabilities not in Australia will depend on resolution of the company's involvement in the Ruddy Pool, but is expected to be at the lower end of the range.

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

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

The Australian and 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 FAI Insurances will be capable of meeting that same percentage on all eligible liabilities reasonably expected to be admitted in the future.

### *3.3 Estimated ultimate Scheme Payment Percentages*

The summary estimates of the ultimate Payment Percentages per company given by the Australian Scheme Administrators are shown below and compared to the original estimates of the Scheme Administrators. 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 classed as insurance or non-insurance, and whether their claims are classed as 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.

<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%	16% to 35%
FAIG	40% to 50%	45% to 55%
FAII	Less than 5%	1% to 10%
WMG	10%	40% to 100%
CIC	40% to 50%	60% to 70%
FAIT	Less than 5%	Less than 5%
FAI Re	More than 50%	100%

HIH U&I	5% to 10%	15% to 30%
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## **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 FAI Insurances. The Australian and English Scheme Administrators co-operate fully. Creditors do not need to lodge separate claims in each jurisdiction. Creditors need to lodge claims in one location only, which is then effective under both Schemes.

The Australian and English Scheme Administrators and their run-off manager Capita CMGL, 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 FAI Insurances to be approximately £511m, of which approximately £25.4m relates to business written in the UK through the Ruddy Pool. Approximately £2.4m of UK branch liabilities have been agreed as Acknowledged Creditor Claims to date. The English Scheme Administrators have not yet published an estimate of the assets ultimately expected to be available for collection.

## 5.2 Receipts and payments to 30 June 2010

A summary of the English Scheme Administrators' receipts and payments from 1 July 2009 to 30 June 2010 is set out on the next page. For comparison, a receipts and payments for the period from 1 July 2008 to 30 June 2009 is also shown.

<b>FAI Insurances Limited</b>		
<b>Receipts and payments for the period 1 July 2009 to 30 June 2010</b>		
	<b>1 July 2009 – 30 June 2010</b>	<b>1 July 2008 – 30 June 2009</b>
		<b>£</b>
<b>Receipts</b>		
Insurance and reinsurance recoveries	145	394
Bank Interest and Sundry Receipts	2,307	26,787
Total receipts	2,452	27,181
<b>Payments</b>		
Officeholders' fees and expenses	26,548	9,492
Bank Charges	17	36
VAT expense	4,200	
Total payments	30,764	9,528
Total	(28,312)	17,653
<b>Funds held as at 30 June 2010</b>	<b>750,942</b>	

## 6 Closure

The Scheme for FAI Insurances 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 creditors will be given notice of the actual Estimation Date between six and three months prior to the 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 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 FAI Insurances 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 FAI Insurances have been outsourced to a specialist run-off organisation in Sydney. The run-off managers for all business written by FAI Insurances 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.

The current constitution of the Committee is as follows:

<b>Member</b>	<b>Represented by</b>
FAI (NZ) General Insurance Company (In Liquidation)	Mr K Downey
HIH Casualty and General Insurance (NZ)(In Liquidation)	Mr K Downey
Markel International Insurance Company Limited	Mr G Appleton/Ms S Crofts

## **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 business should call Capita CMGL on +61 (0) 2 9650 5777. Written claims adjustment queries should be directed in the first instance to Capita CMGL at the following address: Capita CMGL, Level 2, 117 Clarence Street, Sydney, NSW, 2000, Fax +61 (0) 2 9650 5710.



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 FAI Insurances 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. FAI Insurances was one of the 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.