



AA Mutual International Insurance Company Limited

**Administrators' report in accordance with
Rule 2.47 of the Insolvency Rules 1986
22 August 2006**

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I Summary Information

The Company	AA Mutual International Insurance Company Limited (“AAMI” or “the Company”)
Registered number	01432586
Registered office and trading address	Hampden House, Great Hampden, Great Missenden, Buckinghamshire HP16 9RD
Activity	Insurance company in run-off since 1987
Court reference	High Court of Justice number 4748/04
Date of the Administration Order	23 July 2004
Date of approval of proposals	10 September 2004
Purpose of the Administration Order	Achieving a better result for the Company’s creditors as a whole than would be likely if the Company were wound up (without first being in Administration).
Joint Administrators	Nigel Rackham and Dan Schwarzmann Any function required or authorised under any enactment to be exercised or performed by an Administrator may be done by all or any one or more of the persons for the time being holding that office.

II Progress Report

Purpose of report

This report has been prepared in accordance with Rule 2.47 of the Insolvency Rules 1986. It has been prepared to provide creditors with an update on the progress of this Administration since our previous report dated 15 February 2006. It is also to deal with the extension of the Administration. Copies of our previous reports sent to creditors may be requested from Caroline Turnbull or Adam Loveday. The report dated 15 February 2006 may also be reviewed on the PwC website at www.pwc.com/uk/aamii.

The following attachments accompany this report:

Appendix A - Administrators' proposals as approved

Appendix B - Receipts and payments account for the period 23 January 2006 to 22 July 2006

Appendix C - Financial Services Compensation Scheme ("FSCS") – brief summary

Appendix D - Notice of conduct of business by correspondence – Form 2.25B

Appendix E - Statement of claim form for voting purposes only

Creditors' Committee

As you are aware from our previous reports, at the creditors' meeting held by correspondence on 10 September 2004, a Creditors' Committee was established comprising four members. In March 2006 we were advised by Aon, one of the members of the Committee, that it was unlikely to be a creditor under the terms of the proposed Scheme. As it was proposed that the existing Committee Members formed the Committee within the Scheme, Aon tendered its resignation as member of the Creditors' Committee and this was accepted. The Joint Administrators have, as required, notified Companies House of this change to the Committee membership. I would like to take this opportunity to record my thanks to Aon for acting in the Administration and also the remaining Committee Members for all of their assistance to date in the Administration and for agreeing to act as the Committee in the Scheme.

Overall strategy

The purpose of the Administration Order was to achieve a better result for the Company's creditors as a whole than would be likely if the Company were wound up (without first being in Administration). It was anticipated that this would be achieved by the sanctioning, under section 425 of the Companies Act 1985, of a compromise or arrangement between the Company and its creditors, namely a Scheme of Arrangement ("Scheme").

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Summary of work done

The focus of work in the last six months is summarised below.

Scheme

Since our appointment as Joint Administrators, our primary objective has continued to be to investigate the feasibility of a Scheme whilst minimising the ongoing costs and pursuing any asset recoveries.

On 13 March 2006 the Administrators circulated to creditors details of the proposed Scheme and a meeting of creditors was summoned for 26 April 2006.

In summary the proposals for the Scheme provided for two distinct classes of creditors reflecting the priorities in a liquidation under the provisions of The Insurers (Reorganisation and Winding Up) Regulations 2004:

- (i) Direct insurance claimants (excluding Employer's Liability ("EL"))
- (ii) Other claimants (including reinsurance and trade creditors)

After settling the costs of the Administration and the Scheme, direct policyholders (excluding EL) are expected to be paid in full. Of the remaining funds available to creditors, a specific reserve of £50,000, representing known or anticipated EL claims, is to be paid to the FSCS. In addition, a further 50% of the balance, after payment in full of the direct policyholders and the specific reserve of £50,000, will also be paid to the FSCS for possible, unknown future EL claims. Any EL claimant will be entitled to protection from the FSCS under its rules and such claimants are therefore excluded from the Scheme. The remaining 50% of the balance will be paid to other creditors (including reinsurance and trade creditors) on a pari passu basis. The estimation methodology requires creditors to submit an estimate of their claims (including incurred but not reported claims), discounted for the time value of money (5% in line with the winding up procedures). If a claim cannot be agreed by the Company and a creditor then an Adjudicator will determine its value. Full details are to be set out in the Scheme, copies of which, including claim forms, can be obtained from the website www.pwc.com/uk/aamii.

The creditors voted overwhelmingly in favour of the insolvent Scheme. By an Order dated 21 June 2006 made in the High Court of Justice in England and Wales, the Scheme was sanctioned. On 22 June 2006 an office copy of the Court Order sanctioning the Scheme was delivered to the Registrar of Companies for registration. The Effective Date of the Scheme is therefore 22 June 2006.

In accordance with the terms of the Scheme, Scheme Creditors must now complete and submit a claim form to reach the Scheme Administrators on or before the final claims submission date.

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The final claims submission date is 23:59 London time on 23 October 2006. If a Scheme Creditor fails to submit a properly completed claim form by the final claims submission date, his claim, if any, will be valued at zero.

Claim forms can be downloaded from the website at www.pwc.com/uk/aamii or obtained direct from Adam Loveday at PricewaterhouseCoopers LLP, Plumtree Court, London EC4A 4HT.

Scheme Creditors who submitted a voting form at the Meetings of Scheme Creditors on 26 April 2006 had the opportunity to elect for the information provided on their voting form to constitute the basis of their claim in the Scheme. If you made such an election then your voting form will be used as your claim form and you are not required to submit a separate form in order to make a claim in the Scheme.

Asset management

Since our appointment, our treasury team has managed the Company's cash assets in a portfolio of high interest bearing investment accounts and interest of just over £70,000 has been generated.

As previously advised a review of the outwards reinsurance programme has been carried out with a view to generating reinsurance recoveries where possible. This review suggested that because of the commutation activity prior to Administration, little, if any, recoveries were readily available.

We have to date made recoveries totalling £31,407 from brokers. It is not anticipated that any further recoveries will be made.

Claims processing

In view of the minimal impact on the reinsurance programme and in order to keep costs to a minimum the company has ceased to process all inwards claims for all classes of business as at 30 June 2000. All claims will now be dealt with as provided for under the terms of the Scheme.

Tax

Following our review to identify potential tax assets it was ascertained that there were no pre-appointment tax assets to be realised. The only potential recovery available will be in respect of the group relief of the trading losses incurred by AAMII. It is not currently possible to determine whether there may be any recoveries in this regard.

The Administrators have complied with their statutory duties of filing tax returns to 31 December 2004 and have obtained the agreement of the tax authorities that no tax is payable for the post-appointment period to 31 December 2004.

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Statutory reporting

This report has been filed with the High Court and the Registrar of Companies as required by the Insolvency Rules 1986. The Financial Services Authority, which supervises authorised insurers in the UK, has also been advised of all developments throughout the Administration.

Nil returns under the Company Directors Disqualification Act 1986 have also been submitted.

Administrators' remuneration

Full details of professional costs have been provided to the Creditors' Committee. Since my previous report we have drawn £96,486.40 plus VAT (a total of £113,371.52) in accordance with the schedule of resolutions passed by the Creditors' Committee in November 2005. These resolutions allowed for the Administrators to draw £18,610.50 plus VAT for time costs for the period 1 July 2005 to 30 September 2005 and a further £77,875.90 plus VAT representing 80% of budgeted time costs for the period 1 October 2005 to 30 April 2006. In addition the Administrators have drawn £602.22 plus VAT (a total of £707.61) in accordance with a further resolution allowing the Administrators in-house treasury services be charged on a % basis, at a rate of 0.1% per annum calculated on a forecast weighted average balance of funds held, payable quarterly in advance.

Fees have been agreed by reference to the time properly given by the Joint Administrators and their staff in attending to matters arising in this Administration and the Scheme of Arrangement.

III Proposal to extend the Administration

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Under the provisions of the Insolvency Act 1986, Administration proceedings automatically come to an end for an insurance company 30 months after the date of appointment of the Administrators, unless an extension (of no more than six months) is granted by the consent of the creditors or by the Court on an application by the Administrator. It is therefore due to end on 23 January 2007.

However for the following reasons, the Administrators are proposing an extension to the Administration. During the period of an Administration the Company is not required to file annual audited accounts with the Registrar of Companies, this requirement being replaced by the submission of Receipts and Payments Accounts with the Administrators' six monthly reports. However, once the Administration has come to an end, the Company in Scheme will be required to file audited accounts from the date the last accounts were filed. This will be an extremely costly exercise. The Administrators believe that requesting creditors' consent to the extension is the most cost effective manner to avoid having to incur the additional costs of having to file accounts, and that any additional costs which might be incurred in extending the Administration will be much less than those which would be incurred in filing audited accounts. Please note that extending the Administration will in no way affect the Scheme and, indeed, it is anticipated that the Scheme will be concluded within the additional six month period, that is by 23 July 2007.

Section 76(2) of Schedule B1 of the Insolvency Act 1986 states that an Administrator's term of office may be extended for a specified period not exceeding six months by consent of the creditors. Section 78(3) of the Insolvency Act 1986 requires that the consent must be obtained in writing or signified at a creditors' meeting and a majority of 50% in value of the creditors voting must approve the proposed extension.

In order to keep costs to a minimum it is not my intention to summon a formal meeting of creditors. Instead I intend to deal with the proposed resolution by post. Creditors who wish to vote on the resolution must have lodged a claim in either the Administration or Scheme proceedings. For the purposes of this meeting and not in order to ascertain their claim in the Scheme, creditors, who have not yet lodged a claim, may lodge a simplified claim on the form attached as Appendix E. In addition all creditors who wish to vote at the meeting must appoint a proxy, and therefore must complete Form 2.25B at Appendix D as required by Rule 2.48 of the Insolvency Act 1986, and return it by 11 September 2006 as this meeting is being conducted by post.

The Administrators will review all proxies received as at 11 September 2006 and the proposals will be accepted or rejected based on the forms returned by this date. In order to keep costs to a minimum it is not my intention to circularise creditors with the results of the meeting, but I will post the results on the website at www.pwc.com/uk/aamij.

Appendix A

Administrators' proposals as approved

The following proposals were approved by the creditors on 10 September 2004 for achieving the purposes of the Administration Order dated 23 July 2004.

- (i) That as Joint Administrators, we continue to manage the business, affairs and property of the Company in such manner as we consider expedient with a view to achieving the purpose for which the Administration Order was made.
- (ii) That we continue to investigate the affairs of the Company with a view to, amongst other matters, determining its financial position in order to formulate and put to meetings of the creditors proposals for a Scheme under Section 425 of the Companies Act 1985, if thought to be in the best interests of the Company and creditors.
- (iii) That we investigate and, if appropriate, pursue any claims that the Company may have under the Companies Act 1985 or The Insolvency Act 1986. The Administrators will investigate transactions in the period leading up to the date the Company entered into Administration, typically preferences and transactions at undervalue.
- (iv) That we may apply for the discharge of the Administration Order once meetings of the Company's creditors have been held to consider the proposals for a Scheme.
- (v) That a formal Creditors' Committee be established.
- (vi) That the Joint Administrators' fees and disbursements be agreed by the Creditors' Committee or at the meeting of creditors to consider the Scheme.

Appendix B

AA Mutual International Insurance Company Limited - In administration
Receipts and Payments account for the period 23 January 2006 to 22 July 2006

Receipts	US\$	£	CAN\$
Brought forward from previous abstract	2,497,469.36	1,183,629.40	40,804.67
Reinsurance recoveries	6,544.66		
* CAN\$ now held in GBP		20,156.74	
**CAN\$ now held in GBP		33.85	
Interest received gross	13,520.46	15,605.31	76.30
Total receipts	<u>2,517,534.48</u>	<u>1,219,425.30</u>	<u>40,880.97</u>
Payments			
Brought forward from previous abstract	1,667,832.69	470,022.90	36.19
Joint administrators' fees		113,371.52	
Treasury services		707.61	
Legal & professional fees		40,985.89	
Run-off service provider		4,256.26	
Storage costs		2,010.00	
Statutory advertising		11,857.97	
Printing costs		2,271.96	
* CAN\$ converted to GBP (see above)			40,767.00
**CAN\$ converted to GBP (see above)			69.08
Bank charges	8.22	28.67	8.70
Total payments	<u>1,667,840.91</u>	<u>645,512.78</u>	<u>40,880.97</u>
Closing balance	<u>849,693.57</u>	<u>573,912.52</u>	<u>0.00</u>

Appendix C

FSCS – brief summary

FSCS is the UK's statutory fund of last resort for customers of authorised financial services firms. It protects deposits, insurance and investments. FSCS can provide compensation if an authorised insurance Company is unable or likely to be unable to meet claims against it. The Scheme was mainly set up to assist private individuals and small businesses, although all policyholders are protected for claims under compulsory (eg. EL) insurance policies.

Re-insurance, marine, aviation, transport business and credit insurance are excluded. Also excluded are risks outside the European Economic Area.

There are maximum levels of compensation a policyholder can receive from the FSCS and compensation may not cover all of an insured's loss.

The levels of compensation which may be payable to eligible insurance creditors are as follows:

- (i) Liability subject to compulsory insurance, 100% of the claim.
- (ii) In all other cases 100% of the first £2,000 and 90% of the remainder of the claim

For more information on the role of FSCS, insurance creditors should refer to the FSCS website (www.fscs.org.uk).