



To Scheme Creditors

30 June 2020

Dear Sirs or Madams

Proposed Scheme of Arrangement in relation to Stronghold Insurance Company Limited (In Administration) (the “Scheme Company”) pursuant to Part 26 of the Companies Act 2006 (the “Scheme”)

This letter is important. It concerns matters which may affect your legal rights and entitlements.

Introduction

1. The Scheme Company proposes to enter into a scheme of arrangement pursuant to Part 26 of the Companies Act 2006 (the "**Part 26**") with its creditors, subject to certain limited exceptions described in paragraph 17 below, (collectively the "**Scheme Creditors**"). The Scheme is being proposed for the purposes of bringing closure to the Scheme Company's business following the commencement of administration proceedings on 27 June 2019 due to its insolvency.
2. We are sending you this letter because we believe that you are:
 - (a) a Scheme Creditor with a claim arising under or pursuant to insurance, reinsurance and/or retrocession contracts and therefore may be affected by the Scheme; or
 - (b) a broker who placed relevant business of the Scheme Company with Scheme Creditors. Brokers are requested to forward a copy of this letter to any clients which may be affected by the Scheme; or
 - (c) another party which may potentially be involved in the creditor claim process; or
 - (d) a trade creditor or ex-employee who may have pre-administration outstanding sums due from the Scheme Company.
3. We ask that you read this letter, consider its contents carefully and take legal advice if you consider it appropriate to do so.

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Background

4. The Scheme Company was incorporated on 28 September 1962 and wrote Excess of Loss and Stop Loss business (excluding windstorm), and risks of a similar nature. Originally formed to write exclusively non-proportional insurance and reinsurance, in the 1970s the Scheme Company extended its activities into some proportional treaty business.
5. The Scheme Company ceased active underwriting in 1985 and entered solvent run-off. In terms of London market insurance coverage, the Scheme Company is one of the smallest participants.
6. Upon introduction of the European Solvency II directive in 2016, the Scheme Company was no longer able to meet the capital requirements imposed under that directive. In 2018, a solvent scheme of arrangement pursuant to Part 26 was proposed but was not implemented.
7. Following this, the Board re-examined the Scheme Company's financial position and, after careful review, concluded that the Scheme Company did not have sufficient assets to meet its liabilities and was insolvent on a balance-sheet basis. The Scheme Company ceased paying creditors' claims as of 31 May 2019.
8. On 27 June 2019, following an application to the Court by its directors, the Scheme Company was placed into administration under section 8 and Schedule B1 of the Insolvency Act 1986 (the "**Administration**") and Dan Yoram Schwarzmann and Douglas Nigel Rackham of PricewaterhouseCoopers LLP were appointed as joint administrators of the Scheme Company (together the "**Joint Administrators**").
9. The purpose of the Administration is to achieve a better result for the Scheme Company's creditors as a whole than would be likely if the Scheme Company were wound up (without first being in administration). The Scheme Company cannot be rescued as a going concern as it has been determined that it is balance sheet insolvent and the options available to return it to solvency are not feasible.
10. Details on the progress of the Administration have been sent to creditors and are available on the Scheme Company websites www.strongholdinsco.co.uk; and www.pwc.co.uk/services/business-restructuring/administrations/stronghold.html (the "**Websites**").

The objective of the Scheme

11. The primary objective of the Scheme is to bring closure to the Company's business given its insolvency. Accordingly, the Scheme provides a mechanism for determining Scheme Creditors' claims and making appropriate payments in respect of them.

12. Since their appointment, the Joint Administrators have considered various alternative exit options, including: (a) the commutation of liabilities on an ad hoc basis; (b) an informal arrangement with creditors; (c) an insolvent liquidation; and (d) a distribution in administration. These alternatives, whilst capable of being utilised to tackle the problems of an insurance company in financial difficulties in appropriate circumstances, have significant disadvantages which render them inappropriate for the Scheme Company.
13. Given the difficulties in assessing contingent, unquantified and/or future claims and the fact that no deadline for submitting claims could be imposed in a liquidation proof process by a claims submission deadline, and the requirement that a liquidator could not safely make a distribution until knowing the fixed assessment of provable claims for Direct Scheme Claims first, and only afterwards Non-Direct Scheme Claims, there is likely to be significant delay if a liquidation distribution were utilised. If such claims were left to mature in the ordinary course, the Scheme Company has estimated that it would take approximately 25 years for all claims to be determined, meaning creditors would be kept out of their money during this process. In order to ensure that an equal and fair distribution can take place to Direct Scheme Creditors (as defined in paragraph 16(a) below) it is necessary that all Direct Scheme Claims (as also defined in paragraph 16(a) below) are assessed and known. The claims of Non-Direct Scheme Creditors (as defined in paragraph 16(b) below, primarily reinsurance creditors / cedants), since they are subordinated to the claims of Direct Scheme Creditors, cannot even be sensibly assessed for payment until the claims of the Direct Scheme Creditors are dealt with. The proposed Scheme, by contrast, by utilisation of a deadline for submitting claims would provide an alternative quicker, but fair, process for resolving the claims, meaning creditors ought to be paid sooner than in the comparator scenario of an insolvency distribution. As a result the Scheme Company wishes to crystallise its outstanding liabilities and intends to achieve this by implementing the Scheme with its Scheme Creditors. In addition, the Scheme proposes to allow creditors to be paid in US dollars, where the liability to them was incurred in US dollars, or £ sterling where the liability to them was incurred in £ sterling, thus differing from the requirements in an insolvency distribution to pay only in £ sterling (rule 14.21 of the Insolvency (England and Wales) Rules 2016, and see further below at paragraph 16 (i)).
14. The Scheme has been proposed to offer Scheme Creditors the most effective and economical method for having their claims against the Scheme Company agreed or otherwise determined in the shortest practicable time thereby maximising the potential returns to Scheme Creditors, whilst at the same time achieving finality and certainty.
15. The Scheme Company has discussed the main proposals of the Scheme with the creditors' committee established pursuant to the Scheme Company's Administration ("**Committee**") and has taken account of their views along with those of its advisers, where possible. Furthermore, a near-final draft of the Explanatory Statement (as

defined below) and the Scheme were provided to the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA"), who have not objected to the proposals contained in the Scheme.

What does the Scheme do?

16. The Scheme provides that:

- (a) Scheme Creditors with claims arising under direct insurance contracts ("**Direct Scheme Creditors**") will be required to submit a claim form within 180 calendar days of the Scheme becoming effective, notifying the Scheme Company of such claims (the "**Direct Scheme Claims**"). A Direct Scheme Creditor which fails to submit a claim form in respect of any Direct Scheme Claim within this timeframe shall not be entitled to receive any payment in respect of it;
- (b) given the priority afforded to direct insurance creditors by regulation 21 of the Insurers (Reorganisation and Winding Up) Regulations 2004 (the "**2004 Regulations**"), which regulations apply to the Scheme Company, Direct Scheme Claims are required to be paid, or otherwise provided for, in full before payments can be made to a Scheme Creditor (a "**Non-Direct Scheme Creditor**") with a claim arising otherwise than under a direct insurance contract (the "**Non-Direct Scheme Claims**"). Accordingly, it is expected that a claims submission deadline ("**Final Claims Time**") will only be set in respect of Non-Direct Scheme Claims where the Scheme Company determines that it will be possible to pay or otherwise provide for all Direct Scheme Claims (once ascertained) and all Excluded Liabilities, in full and that there will be sufficient assets available to make payments in respect of Non-Direct Scheme Claims which become ascertained otherwise than on a *de minimis* basis. Non-Direct Scheme Creditors will then be given 180 calendar days' notice of this new Final Claims Time and their claims must be notified to the Scheme Company by such date in order to be eligible to receive a payment;
- (c) Direct Scheme Claims and, where a Final Claims Time has been notified in respect of thereof, Non-Direct Scheme Claims (together, "**Scheme Claims**") will be valued by the Scheme Company (as well as any amounts to be set-off against those Scheme Claims) using on the guidelines described in the Scheme (the "**Estimation Guidelines**"). A copy of the Estimation Guidelines will be made available on the Websites once finalised;
- (d) in the event that the Scheme Creditor does not agree with the value placed on its Scheme Claim by the Scheme Company it shall have the right to challenge the valuation;
- (e) if the Scheme Company and the Scheme Creditor are not able to reach agreement as to the value of the relevant Scheme Claim, the dispute shall be referred to an independent adjudicator appointed under the Scheme (the "**Scheme**

Adjudicator") to determine the value. The determination of the Scheme Adjudicator will be based on the Estimation Guidelines and will be final and binding on both the Scheme Company and the Scheme Creditor;

- (f) once the value of a Scheme Claim has been agreed or determined in accordance with the Scheme, the resulting value of the claim, if any, will be the amount of the Scheme Creditor's claim (the "**Ascertained Claim**");
- (g) as soon as possible following the deadline for submitting completed claim forms in respect of Direct Scheme Claims, the Scheme Company shall determine whether all Direct Scheme Claims which become Ascertained Claims ("**Direct Ascertained Claims**") can be paid in full. If the Scheme Company determines that such claims can be paid in full, it shall make payment in full in respect of all Direct Ascertained Claims as soon as reasonably practicable. In the event that the Scheme Company determines that all Direct Ascertained Claims cannot be paid in full, it shall determine what percentage of the Direct Ascertained Claims (the "**Direct Payment Percentage**") can be paid taking into account the amounts required to meet all Excluded Liabilities (as defined below), all other liabilities of the Scheme Company ranking in priority to the Direct Scheme Creditors and the need to ensure that the same percentage is paid in respect of all Direct Ascertained Claims. Once a Direct Payment Percentage has been set, the Scheme Company shall pay the Direct Payment Percentage in respect of each Direct Ascertained Claim;
- (h) Where all Direct Ascertained Claims can be paid or provided for in full, the Scheme Company shall determine whether it is possible to make any distribution in respect of Non-Direct Scheme Claims which become Ascertained Claims ("**Non-Direct Ascertained Claims**") otherwise than on a *de minimis* basis. Where such a distribution can be made, the Scheme Company will determine what percentage of the Non-Direct Ascertained Claims (the "**Non-Direct Payment Percentage**") can be paid, and pay the Non-Direct Payment Percentage in respect of each Non-Direct Ascertained Claim as soon as reasonably practicable;
- (i) Scheme Creditors will be paid their Ascertained Claims in either United States Dollars ("**USD**") or British Pounds ("**GBP**"), USD and GBP each being a "**Relevant Currency**" and together, the "**Relevant Currencies**". Where a Scheme Creditor has an Ascertained Claim in both Relevant Currencies, their entire Ascertained Claim will be paid in the Relevant Currency in which it has its largest Ascertained Claim (using the rate of exchange applicable as at the Administration Date). Where a Scheme Creditor has Ascertained Claims in currencies other than a Relevant Currency, such Ascertained Claims will be converted into USD; and
- (j) Scheme Creditors will retain such rights as they currently have in respect of any

security, including but not limited to any deposit or reserve of funds or assets established by the Scheme Company, guarantee provided by a third party, letter of credit or any other funds held or otherwise retained by or on behalf of a Scheme Creditor.

Liabilities excluded from the Scheme

17. The Scheme does not apply to claims arising from the following liabilities (the "**Excluded Liabilities**"):
 - (a) preferential claims, being, in summary, those claims against the Scheme Company that have preferential status under section 386 of the Insolvency Act 1986. These claims, which included outstanding salary and accrued holiday for ex-employees of the Company, have been fully repaid prior to the date of this letter;
 - (b) pre-Scheme expenses, being, in summary, the expenses reasonably incurred by the Scheme Company in connection with the promotion and preparation of the Scheme;
 - (c) Scheme costs, being, in summary, the costs incurred by the Scheme Company in the course of implementing the Scheme and complying with the provisions of the Insolvency Act, including the remuneration and expenses of the office holders appointed in the Scheme; and
 - (d) Administration costs, being, in summary the costs incurred on behalf of the Scheme Company by the Joint Administrators as administration expenses or determined as administration expenses by the Court, including the remuneration and expenses of the Joint Administrators.

The Scheme process

18. The Scheme Company will make an application to the Business and Property Courts of England and Wales (the "**Court**") for an order granting permission to it to convene the meetings of the Scheme Creditors to vote upon the proposed Scheme (the "**Scheme Meetings**"). At the hearing to consider that application (the "**First Court Hearing**"), the Court will be invited to consider the constitution of classes of Scheme Creditors and therefore the number of Scheme Meetings that should be held to vote on the Scheme. The application is expected to be heard on 21 July 2020. Once the exact date for the hearing of the application is fixed, the Scheme Company will advertise it on the Websites.
19. If the Court gives the Scheme Company permission to convene the Scheme Meetings, the Scheme Company will send you information about how to access a copy of the

Scheme and the explanatory statement in respect of the Scheme required by Part 26 (the "**Explanatory Statement**"). Scheme Creditors will be requested to complete and submit a voting and proxy form in accordance with the procedures described in the Explanatory Statement.

20. If the required majorities of the Scheme Creditors vote in favour of the Scheme at the Scheme Meetings, the Scheme Company will ask the Court to “sanction” (or approve) the Scheme at a second Court hearing. In deciding whether to sanction the Scheme, the Court will consider whether it is fair to Scheme Creditors as a whole.
21. If the Scheme is sanctioned by the Court, the Scheme Company will file a copy of the order sanctioning the Scheme with the English Registrar of Companies, at which time the Scheme will become effective. The process for creditors to make claims will be explained in the greater detail in the Scheme and Explanatory Statement.

The proposed voting classes at the Scheme Meetings

22. In order for the Scheme to be implemented, it must be approved by a majority in number, representing not less than 75% in value, of those creditors who vote at the meetings.
23. Where scheme creditors have rights which are so different as to make it impossible for them to consult together with a view to their common interest, the law requires them to be split into separate classes and to vote at a separate meeting for each class.
24. The Company has considered the rights of Scheme Creditors in respect of their Scheme Claims, and the way in which those rights will be affected under the proposed Scheme and concluded that there should be two classes for the purpose of voting on the Scheme, namely:
 - (a) Direct Scheme Creditors; and
 - (b) Non-Direct Scheme Creditors.
25. The Scheme Company has reached this conclusion because, in the event that this Scheme is not implemented, the alternative to the Scheme will be a valuation and distribution mechanism in an insolvency procedure. As described in paragraph 16 (b) above, the 2004 Regulations provide that, amongst other things, in an insolvency, direct insurance creditors have priority over other classes of unsecured creditors of a UK insurer, including reinsurance creditors. This priority is reflected in the Scheme.
26. The Scheme Company does not consider it necessary to split Direct Scheme Creditors and Non-Direct Scheme Creditors into further classes, for example on the basis of whether they have agreed claims, notified outstanding claims and incurred by not reported claims.

Next steps

27. If permission to convene the Scheme Meetings is granted by the Court at the First Court Hearing, known Scheme Creditors, known brokers and other interested parties identified by the Company will be sent a letter summarising the key Scheme terms and explaining how to access a document containing, amongst other things:
- (i) the Explanatory Statement;
 - (ii) the terms of the Scheme; and
 - (iii) a notice confirming the date, time and place of the Scheme Meetings.

The letter will also include a voting and proxy form (including guidance notes).

28. To disseminate information about the Scheme and to facilitate its implementation, Scheme Creditors may download documents relating to the Scheme from the Websites once they become available.
29. If your name, address or contact details have been incorrectly or incompletely stated, or if you would like correspondence about the Scheme to be addressed to someone else in your organisation, please let us know by using the contact details below.

Questions and contact

30. If you have any concerns regarding the proposed constitution of classes of creditors, you are requested to contact the Joint Administrators as soon as possible and in any event, at least seven days prior to the date of the First Court Hearing. You also have the right to attend the First Court Hearing for the purpose of making representations and, if requested, we will be pleased to provide you with further information on arrangements for this. Please note that if the Scheme is approved at the Scheme Meetings, it will be possible for Scheme Creditors to raise objections regarding the constitution of classes at the Court hearing to sanction the Scheme. However, in this event, the Court would require Scheme Creditors to demonstrate why the objections were not raised at an earlier stage.
31. If you have any questions in relation to this letter or the Scheme, please contact the Joint Administrators at:

Stronghold Insurance Company Limited (In Administration)
c/o PricewaterhouseCoopers LLP
7 More London Riverside,
London, SE1 2RT
England

Contact: John Baker
Email: uk_stronghold@pwc.com

32. Scheme Creditors are encouraged to make contact with the Scheme Company using agregory@strongholdinsco.co.uk or +44 (0)7801 968033 if they require further information regarding their insurance policies/contracts in relation to the Scheme Company, or if they wish to discuss their claims for voting purposes prior to the Scheme Meetings.
33. This Practice Statement Letter is being emailed and posted to all known creditors to inform them of the proposed classes for the Scheme. Any further notifications required or considered desirable for the purposes of the Scheme, its timetable or other matters arising will be posted on the Websites (see paragraph 10 above), so creditors are requested to keep themselves updated by reference to the website in so far as possible.

Yours faithfully



Dan Schwarzmann

Joint Administrator acting as agent for and on behalf of Stronghold Insurance Company Limited (In Administration) without personal liability

Dan Yoram Schwarzmann and Douglas Nigel Rackham have been appointed as Joint Administrators of Stronghold Insurance Company Limited to manage its affairs, business and property as agents and without personal liability. Dan Yoram Schwarzmann and Douglas Nigel Rackham are all licensed in the United Kingdom to act as insolvency practitioners by the Institute of Chartered Accountants in England and Wales.

Stronghold Insurance Company Limited is authorised by the Prudential Regulation Authority and regulated by the Prudential Regulation Authority and the Financial Conduct Authority, reference number 202552.

The Joint Administrators are bound by the Insolvency Code of Ethics which can be found at: <https://www.gov.uk/government/publications/insolvency-practitioner-code-of-ethics>.

The Joint Administrators may act as controllers of personal data as defined by UK data protection law depending upon the specific processing activities undertaken. PricewaterhouseCoopers LLP may act as a processor on the instructions of the Joint Administrators. Personal data will be kept secure and processed only for matters relating to the Joint Administrators'. Further details are available in the privacy statement on the PwC.co.uk website or by contacting the Joint Administrators.

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