

Schedule 1

Estimation guidelines

1. INTRODUCTION

2. VALUATION METHODOLOGY FOR OTHER DIRECT INSURANCE CREDITORS

I. UNPAID AGREED CLAIMS

II. NOTIFIED OUTSTANDING CLAIMS

III. DISCLAIMER DAMAGES CLAIMS

a) VALUE OF FUTURE LOSS

- REPLACEMENT COVER**
- RETURN OF PREMIUM**
- IBNR ESTIMATE**

1. INTRODUCTION

1.1 The Estimation Guidelines are intended to make the valuation process, which the Company will follow in valuing Scheme Claims, as transparent as possible to Other Direct Insurance Creditors. The Estimation Guidelines describe the approach that the Company will expect Other Direct Insurance Creditors to follow in valuing their Scheme Claims. Under the terms of the Scheme, the Estimation Guidelines will be applied by the Company when seeking to assess the estimated value of those claims.

Other Direct Insurance Creditors should read this Appendix in its entirety.

1.2 FSCS Protected Creditors should only submit a claim for voting purposes. They are not required to submit a Scheme Claim and should continue to submit claims arising under their FSCS Protected Policies in the ordinary course until the Cut-Off Date. The submission and determination of FSCS Protected Liabilities and Cut-Off Liabilities shall be governed by PART 5 of the Scheme.

1.3 The Estimation Guidelines are designed to be of assistance to Other Direct Insurance Creditors in developing their estimations of their Scheme Claims by setting out estimation techniques that are generally accepted within the insurance market.

1.4 Other Direct Insurance Creditors are not, however, prevented from using other approaches where appropriate and provided that such approaches are well supported and assumptions used can be reasonably justified by the Other Direct Insurance Creditor. If the Company considers that such techniques can be justified, then those techniques may be used in valuing the relevant Scheme Claims of the Other Direct Insurance Creditor concerned.

1.5 If the Company is unable to reach agreement with an Other Direct Insurance Creditor for any element of their Scheme Claim, the Company will refer the Disputed Scheme Claim to the Scheme Adjudicator for determination by them in accordance with the provisions of the Scheme.

1.6 All Other Direct Insurance Creditors' policies have been disclaimed. Any Other Direct Insurance Creditor submitting a Claim Form for damages arising from the disclaimer of the policy is required to take reasonable steps to mitigate their losses sustained as a result of the disclaimer. For example, by taking reasonable steps to obtain comparable replacement insurance cover for the remaining period of the contract of insurance which has been disclaimed.

1.7 The scope and application of the Estimation Guidelines and the required evidence to support a claim differ according to the type of insurance contract and Scheme Claim being made. The supporting evidence that Scheme Creditors should provide in support of their estimates of Scheme Claims is set out in Schedule 2.

1.8 The Company will not, unless legally obliged to do so, be bound by, or obliged to follow, any settlement made between a Scheme Creditor and another insurer or third party.

- 1.8.1 If, at any stage of the claims agreement process, an Other Direct Insurance Creditor has any queries relating to the application or potential application of the Estimation Guidelines to its claim, it should contact the Company's Claims Handling Agent using the below contact details for further guidance.

Email: Elite-insurance.scheme@quest-group.co.uk

Post: Elite Insurance SoA, c/o Quest Consulting, 52 – 54 Gracechurch Street, London EC3V 0EH, UK

Telephone:

English Helpline: 0800 327 7278

Non-UK Helpline: +33 8 05 98 54 71

Website: www.pwc.co.uk/elite-insurance

- 1.9 Other Direct Insurance Creditors may also wish to consult appropriate professional advisers in understanding these guidelines and valuing their Scheme Claim against the Company.

2. VALUATION METHODOLOGY FOR OTHER DIRECT INSURANCE CREDITORS

- 2.1 An Other Direct Insurance Creditor's claim against the Company may consist of one or more of the following claim elements, subject to appropriate steps being taken by a creditor in mitigating its losses:

- (a) ***Unpaid Agreed Claim***, which is a claim that has been agreed by or on behalf of the Company prior to submission as a Scheme Claim but which has not been paid by the Company or where a residual amount remains unpaid following payment by a compensation scheme and where subrogation does not exist.

Other Direct Insurance Creditors with an Unpaid Agreed Claim need to submit a Claim Form to the Company but are only required to provide a copy of their Offer Letter as Supporting Information, unless the creditor wishes to change the value of the Scheme Claim, submit a new Scheme Claim, or otherwise wishes to share additional Supporting Information. In accordance with section 3.6, the Scheme Managers may, at any time, request further information or evidence reasonably required to assist them.

- (b) ***Notified Outstanding Claim***, which is a claim against the Company in respect of a loss or liability which has been reported to or discovered by the Company prior to the Disclaimer Date of the relevant Scheme Insurance Contract but not agreed by the Company before submission as a Scheme Claim.

Other Direct Insurance Creditors with a Notified Outstanding Claim must submit a Claim Form with details of the amount of any estimated claim which was notified to the Company before the Disclaimer Date

but which has not become an Unpaid Agreed Claim. Other Direct Insurance Creditors must provide supporting evidence of their Notified Outstanding Claim.

- (c) **Disclaimer Damages Claim**, which is a claim representing the actual or estimated value of any loss sustained by the policyholder due to their policy being disclaimed.

A Disclaimer Damages Claim is expected to be valued based on a **Future Loss**, which is the estimated value of a loss arising as a result of the disclaimer. This loss may not yet have been sustained by an Other Direct Insurance Creditor and has not yet been reported to the Company or discovered by the Company.

Further details of the estimation methodologies for a Future Loss are provided in paragraph 2.2 below.

Where new claims have been notified or discovered after the Disclaimer Date, this will be classified as a Future Loss.

2.2 Future Loss

2.2.1 The value of the loss to an Other Direct Insurance Creditor as a result of their policy being disclaimed should be estimated using one of the following estimation methodologies:

- (a) **Replacement cover** - the cost of comparable replacement cover for the remaining period of the contract of insurance which has been disclaimed;
- (b) **Return of premium** - an estimate of a prorated return of premium based on the unexpired portion of any policy; or
- (c) **IBNR estimate** - an estimate of an incurred but not reported (“**IBNR**”) claim in relation to the policy disclaimed.

These estimation methodologies are explained in more detail below.

2.2.2 Replacement cover

- (a) The value of a Future Loss may be estimated using the cost of replacement cover (a “**Replacement Cover Claim**”). The estimate of a Replacement Cover Claim will be equal to the premium payable for a comparable policy, relating only to the remaining period of the Scheme Insurance Contract which has been disclaimed, with an alternative insurance company.
- (b) For a Replacement Cover Claim to be accepted by the Company, Other Direct Insurance Creditors must provide at least one insurance quote or a replacement policy schedule in respect of a policy that is as close as possible to the original policy provided by the Company. Key criteria for likeness include:
- original term of policy;

- remaining term of policy;
- sum insured;
- property, content or service at risk; and
- policy wordings, including, in particular, the heads of damage and any policy limits or exclusions.

This will be considered and evaluated by the Company accordingly.

2.2.3 Return of premium

(a) For an Other Direct Insurance Creditor’s Scheme Insurance Contract which has been disclaimed prior to the date on which the policy had been due to end (the “**Original Policy End Date**”), the value of the Future Loss may be calculated on the basis of a return of premium (a “**Return of Premium Claim**”). The value of a Return of Premium Claim is equal to the value of premium paid for the portion of the policy that the policyholder has not benefited from due to the disclaimer (the “**Unearned Premium**”). The relevant time period to calculate this portion of the policy is from the date at which the policy was disclaimed (“**Disclaimer Date**”) to the Original Policy End Date. For each policy the estimation process may involve the following steps:

- The policy information for any policy with an Original Policy End Date after the Disclaimer Date should be collated by the relevant Other Direct Insurance Creditor. This includes, but is not limited to, the Policy Start Date, the Original Policy End Date and the value of original premium paid. Where the exact Policy Start Date, Original Policy End Date or premium information is not available, a reasonable and justifiable estimate may be presented to the Company for consideration.
- A return of premium calculation should be used to estimate the amount of Unearned Premium as at the Disclaimer Date. This should be calculated by:

- $$\text{Total Premium Amount} \times \frac{\text{Remaining Policy Days}}{\text{Total Policy Days}}$$

Where

Total Premium Amount is equal to the value of the total premium paid to the Company for the Scheme Insurance Contract

Remaining Policy Days is the number of calendar days (as an absolute amount) between the Disclaimer Date and the Original Policy End Date; and

Total Policy Days is the number of calendar days (as an absolute amount) between the Policy Start Date and the Original Policy End Date.

For example: the original premium paid for a 1 year (365 day) policy started 1 January was £100. The Original Policy End Date is 31 December. The Disclaimer Date is 30 June. The return of premium should be calculated as:

$$£100 \times \frac{184}{365} = £50.41$$

Note: Where insurance policies are perpetual, meaning that there is no end to the period of cover, Other Direct Insurance Creditors will be required to make a reasonable assumption about the end date of the policy. Assumptions will be considered by the Company on a case-by-case basis.

- (b) If making a Return of Premium Claim, Other Direct Insurance Creditors must provide supporting evidence to support their claim. Where relevant, this includes, but is not limited to, underlying data, return of premium calculation and selected assumptions as well as proof that the original premium value was paid and information on the policy duration.

2.2.4 **IBNR Claim estimate**

- (a) The value of a Future Loss may be estimated on the basis of an estimate of loss which has been incurred under the Scheme Insurance Contract but has not been reported to the Company or discovered by the Company. IBNR Claims aim to capture losses which may reasonably be expected to be (or have been) suffered by the policyholder, but which have either not yet been reported to the Company or have not yet been discovered.

All claims that have not been notified to the Company, including all potential future claims that may reasonably expect to occur in the period between the Scheme Effective Date and the Original Policy End Date, if any, should be considered in the IBNR estimate. Claimants are required to have taken sufficient steps to mitigate such potential future claims and, when making an IBNR Claim, should demonstrate those steps taken and why an IBNR Claim is still appropriate.

- (b) The approach the Company considers should be taken under the Scheme in respect of estimating an IBNR Claim is to apply a “frequency and severity” method as explained below.

A frequency and severity method requires an Other Direct Insurance Creditor to estimate the total number of claims anticipated to be incurred under their Scheme Insurance Contract and make a best estimate for the future liabilities (including costs) in line with policy terms and conditions that apply to each claim. This can be estimated for each relevant insurance policy held by the Other Direct Insurance Creditor prior to the disclaimer to establish the total estimate of all its IBNR Claims against the Company.

The final estimate of an IBNR Claim excludes Unpaid Agreed Claims and Notified Outstanding Claims which are considered separately

above. It should include claims that have been notified or discovered after the Scheme Effective Date.

An IBNR Claim may include any adjustments to a Notified Outstanding Claim to the extent that any estimate of a claim included as a Notified Outstanding Claim may prove to be inadequate or excessive.

- (c) The following steps should be applied in respect of each relevant policy held by the Other Direct Insurance Creditor:

Estimate the total number of claims that the Other Direct Insurance Creditor may reasonably expect to incur before the Original Policy End Date and that are expected to be covered by the Scheme Insurance Contract but have not yet been notified to the Company.

Estimate the claim amount for each such claim. Other Direct Insurance Creditors should refer to previous claims experience to support the selected claim amount estimates, for example Unpaid Agreed Claims where available and relevant.

Apply any relevant policy terms to the expected claims, such as policy limits or exclusions.

The sum of the estimated claim amounts will constitute the Other Direct Insurance Creditor's total IBNR Claim.

Apply any relevant discounting for the present value of money.

- (d) Any IBNR Claim should be valued as a "best estimate", meaning that it is not intended to be either optimistic or conservative and is intended to represent the most likely outcome of the range of possible outcomes.

2.2.5 **Alternative approaches**

- (a) If an Other Direct Insurance Creditor has evidence that it has sustained a loss as a result of the disclaimer of its policy for which it has no current claims experience, it may under certain circumstances be appropriate to use information which is not based on past claims history to support such a claim. A suitable methodology is likely to involve elements from industry comparisons, trend lines or demographic studies. Other methods, provided that the rationale and basis for the assumptions are clearly explained, might also be suitable.
- (b) The approach taken will need to draw from the information available to the Other Direct Insurance Creditor. The Other Direct Insurance Creditor should consider what information and supporting evidence it can gather and thus what approach should be developed which maximises its ability to provide backing information and justification for the assumptions used.
- (c) In all scenarios, consideration needs to be given to the likelihood of claims actually emerging to the extent indicated by the Other Direct Insurance Creditor's methodology. The final claim will need to be adjusted to take this factor into account, all of which will need to be

explained and documented in full via the supporting evidence submitted alongside their Claim Form.

2.3 **Adjustments**

In order for the Other Direct Insurance Creditor to complete its Claim Form, the Other Direct Insurance Creditor should initially estimate its Scheme Claim as at the Scheme Effective Date and then adjust these estimates to allow for:

- any Notified Outstanding Claim which has changed value since its original submission;
- any amounts due to the Company that act to offset the Other Direct Insurance Creditor's Scheme Claim, for example, defence fees, unpaid premium; and
- any new information received by the Other Direct Insurance Creditor after the Scheme Effective Date.

The value of the Other Direct Insurance Creditor's claim after these adjustments, if any, should be the value that is included on that Other Direct Insurance Creditor's Claim Form.

If the estimated value of a Notified Outstanding Claim has changed since the original submission to the Company and ahead of the Claims Submission Deadline, then this change must be supported with supporting evidence. This must be presented with the Other Direct Insurance Creditor's Claim Form. Supporting evidence includes, but is not limited to, underlying data, methodology and selected assumptions. The Notified Outstanding Claim amount will then be valued by the Company based on the merits of the claim submission.

After the Claims Submission Deadline, Other Direct Insurance Creditors are not entitled to make or revise a Scheme Claim and any Supporting Information received after the Claims Submission Deadline (unless requested by the Company) will only be considered at the Company's discretion.

2.4 **Supporting evidence**

The supporting evidence that Other Direct Insurance Creditors should provide in support of their estimates of Scheme Claims is set out at Schedule 2 and can also be found on the Website.