
***Highlands Insurance
Company (U.K.) Limited –
In Liquidation***

Joint Liquidators' progress report to
members and creditors for the year
ended 16 April 2013

12 June 2013

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Section 1 **Summary information**

The Company	Highlands Insurance Company (U.K.) Limited (in Liquidation) (the “Company” or “Highlands UK”)
Registered number	01190948
Registered office and trading address	c/o Pro Insurance Solutions Limited (“Pro”) Bruton Court, Bruton Way, Gloucester GL1 1DA United Kingdom
Activity	Insurance and reinsurance run-off
Court reference	High Court of Justice, Chancery Division, Companies Court. Case No. 7896 of 2007
Liquidators’ names and address	Dan Schwarzmann and Mark Batten (the “Joint Liquidators”) of PricewaterhouseCoopers LLP (“PwC”), 7 More London Riverside, London SE1 2RT
Date of appointment of Liquidators	17 April 2012

Contact details for queries

General queries relating to the liquidation:

Gary R Bray
PricewaterhouseCoopers LLP
7 More London Riverside
London SE1 2RT
+44 (0) 20 7213 8900
gary.bray@uk.pwc.com

Claims related queries:

Dani Rosser
Pro Insurance Solutions Limited
Bruton Court
Bruton Way
Gloucester GL1 1DA
+44 (0) 1452 782 726
dani.rosser@proisinsurance.com

Section 2 ***Joint Liquidators' progress report***

Introduction

On 1 November 2007 Dan Schwarzmann and Mark Batten of PwC were appointed Joint Administrators of the Company.

The Administration was concluded on 17 April 2012, being the date the Company went into Creditors' Voluntary Liquidation. On 17 July 2012 the Joint Administrators were discharged from liability in respect of their actions as administrators by Order of the Court.

In accordance with Rule 4.49C of the Insolvency Rules 1986 ("IR86"), this is the Joint Liquidators' first progress report to members and all known creditors.

Overall strategy

The key aspects of the strategy have been detailed in the progress reports provided to creditors by the Joint Administrators. This included the development, approval and implementation of schemes of arrangement to deal with the claims of all policyholders and other creditors of the Company. The Joint Liquidators continue to implement the scheme of arrangement pursuant to Part 26 of the Companies Act 2006 in relation to creditors with claims arising from contracts or policies of reinsurance or retrocession and non-insurance creditors (the "Cedant Scheme"). This became effective during the Administration, with a Claims Submission Date of 20 March 2012, and further details are provided below.

Liquidation Committee

The members of the Creditors' Committee established in the Administration and the Cedant Scheme continue to act in the Liquidation as the Liquidation Committee.

The Joint Liquidators have continued to consult with the Liquidation Committee in relation to all significant issues. The most recent meeting of the Liquidation Committee was held on 29 October 2012. The Joint Liquidators remain very grateful of the members and observer of the Liquidation Committee for their continued assistance and support.

Summary of the Liquidators' actions to date

Cedant Scheme

Following the Claims Submission Date on 20 March 2012, Pro commenced the claims agreement process in accordance with the terms of the Cedant Scheme under the direction of the Joint Liquidators (also the Joint Scheme Administrators). The claims agreement process has been progressed to an advanced stage and it is currently anticipated that all claims submitted in the Cedant Scheme will be agreed by late summer 2013.

Although, as previously reported, the Company was able to pay the claims of direct creditors in full, the dividend payment to reinsurance creditors continues to be subject to a number of significant uncertainties.

Further information and copy documents (including a full text of the Cedant Scheme) can be obtained at www.ukhighlands.co.uk

Asset management

On completion of the Administration, surplus funds of approximately £2.07m and US\$13.31m were released to the Joint Liquidators.

The Company's US dollar investments are under the direct control of the Joint Liquidators' specialist treasury team, who continue to manage the assets in a portfolio of interest bearing investment accounts. The investment strategy is reviewed on a regular basis to ensure that the risk profile remains acceptable. Interest of

US\$1,717,278.94 and £258,561.87 was earned on the Company's cash and investment assets during the Administration and a further US\$5,074.15 and £3,606.88 has been earned to date during the Liquidation.

The Joint Liquidators have continued to liaise with the New York Liquidation Bureau in order to obtain the release of the National Association of Insurance Commissioners trust fund of US\$2,500,000. Significant progress has been made and it is anticipated that this matter will be successfully concluded within the next few months.

Pro, under the guidance and direction of the Joint Liquidators, has continued to progress the implementation of our reinsurance collection strategy. During the Administration, reinsurance recoveries, including collections from brokers, amounted to US\$5,653,032.12 and £100,238.10 and a further US\$175,955.81 and £65,412.14 has been recovered to date during the Liquidation.

Statutory reporting

The Insurance Directorate of the Financial Services Authority ("FSA") had responsibility for monitoring all insurance entities continues to be advised of material developments in relation to the liquidation. Following the FSA reorganisation, the Company is classified as a dual regulated firm and will be regulated by both the Financial Conduct Authority and the Prudential Regulation Authority.

Investigations

The Joint Liquidators reviewed the affairs of the Company prior to Liquidation and complied with their obligations under the Company Directors' Disqualification Act 1986 ("CDDA").

Other matters

The Joint Liquidators filed the corporation tax returns for the year ended 31 December 2011 and for the final Administration period up to 16 April 2012.

The Joint Liquidators have also filed notice of directors' resignations.

Professional advisers

For ongoing matters the Joint Liquidators have retained the professional advisers that were engaged in the Administration as shown below:

Service provided	Name of firm / organisation	Reason selected	Basis of fees
Legal advice	Clifford Chance LLP	Specialist insolvency and industry knowledge	Time costs, subject to pre agreed budget
Actuarial	PricewaterhouseCoopers LLP	Specialist industry knowledge	Time costs; subject to pre agreed budget and Liquidation Committee approval
Insurance run-off management	Pro Insurance Services Limited	Pre insolvency and specialist industry knowledge	Time costs, subject to pre agreed budget

The Joint Liquidators' choice was based on an evaluation of the advisers' experience and ability to perform this type of work, their knowledge of the complexity and nature of the assignment and the basis of the fee arrangement with them. The Joint Liquidators continue to review the fees charged and are satisfied that they are reasonable in the circumstances of the case.

Liquidators' remuneration and expenses

During the Administration, in accordance with the resolutions passed at the initial Creditors' Committee meeting held on 12 February 2008, the Joint Administrators' fees were fixed under Rule 2.106 IR86 by reference to time properly given by the Joint Administrators and their staff in attending to matters arising. In accordance with Rule 4.127 IR86, the remuneration basis agreed in the Administration will continue in the Liquidation.

In accordance with Rule 4.127 IR86, the Liquidation Committee passed the following resolutions:

- For the three month period commencing 1 April 2012, the Liquidation Committee passed resolutions approving the Joint Administrators' costs for the period up to 16 April 2012 and the Joint Liquidators' fees from 17 April 2012 to 30 June 2012; and
- For the three month periods commencing 1 July 2012, 1 October 2012 and 1 January 2013, approving the Joint Liquidators' costs for the respective periods.

In addition, a resolution has recently been submitted to the Liquidation Committee for approval of budgeted costs for the three month period commencing 1 April 2013.

Fees have been drawn pursuant to these resolutions and full analyses of costs, together with details of the Joint Liquidators' charging and disbursements policy, have been provided to the Liquidation Committee in accordance with the requirements of Statement of Insolvency Practice No.9 ("SIP9").

A summary of the Joint Liquidators remuneration and expenses is as follows:

	Fees £
Approved by the Liquidation Committee and drawn:	
For the period 17 April to 30 June 2012	141,523.75
For the period 1 July to 30 September 2012	192,121.50
For the period 1 October to 31 December 2012	204,343.50
For the period 1 January to 28 February 2013	86,141.40
Liquidation Committee approval obtained, but not yet drawn:	
For the period 1 March to 31 March 2013	35,244.95
Liquidation Committee approval not yet obtained:	
For the period 1 April to 16 April 2013	10,794.80
Total	670,169.90

In addition to the information provided above, a further £25,730 was incurred and drawn for time costs for the period 1 April 2012 to 16 April 2012, being the period while the Company was still in Administration but after the reporting period of the Joint Administrators' Final Progress Report.

In accordance with the requirements of SIP9, an analysis of the Joint Liquidators' time costs incurred for the period 17 April 2012 to 16 April 2013 is provided in Section 4.

In addition to the information required by SIP9, the Joint Liquidators also provide the Liquidation Committee with a detailed budget and analyses of costs by work activity to enable the Liquidation Committee to fully assess the reasonableness of requests for authority to draw remuneration made by the Joint Liquidators.

The receipts and payments account in Section 3 details expenses met from funds in the Liquidation to 16 April 2013.

Statement of creditors' rights

An explanatory note providing creditors with a statement of their rights in relation to the Liquidators' remuneration and expenses, and their rights to request further information, can be found online at:

<http://www.icaew.com/~media/Files/Technical/Insolvency/creditors-guides/creditors-guide-liquidators-fees-final.pdf>. A copy may also be obtained free of charge on request to the Joint Liquidators.

Next report and enquiries

The Joint Liquidators will circulate their next report in 12 months time. If any creditor has any queries in the meantime, please contact Gary Bray on +44 (0)20 7213 8900.

Signed:



D Y Schwarzmman
Joint Liquidator
Highlands Insurance Company (U.K.) Limited

Dan Schwarzmman and Mark Batten were appointed as Joint Liquidators of Highlands UK to manage its affairs, business and property as agents without personal liability. Both are licensed in the United Kingdom to act as insolvency practitioners by the Institute of Chartered Accounts in England and Wales.

The Joint Liquidators are Data Controllers of personal data as defined by the Data Protection Act 1998. PricewaterhouseCoopers LLP will act as Data Processor on their instructions. Personal data will be kept secure and processed only for matters relating to the Liquidation.

Section 3 Receipts and payments accounts

Sterling Receipts and Payments Account for the periods 1 April 2012 to 16 April 2012 and 17 April 2012 to 16 April 2013

	<i>Administration</i> 1 April 2012 – 16 April 2012	<i>Liquidation</i> 17 April 2012 – 16 April 2013	
Receipts	£	£	
Balance brought forward / transferred from the Administration	2,170,518.74	2,073,083.59	
Interest received	233.43	3,606.88	(i)
Reinsurance collections		65,412.14	
VAT recoveries	21,376.07	95,574.75	
Transfers from US dollar account		1,500,000.00	(ii)
Total receipts	2,192,128.24	3,737,677.36	
Payments			
Administrators' remuneration		77,702.45	(iii) & (iv)
Administrators' disbursements		261.55	
Liquidators' remuneration		624,130.15	(iv)
Liquidators' disbursements		1,467.18	
Other professional costs	95,709.05	650,669.31	(v)
Run-off fees		1,096,588.11	
Legal fees		206,408.54	
Legal settlements		54,000.00	(vi)
Statutory and other costs		35,902.45	(vii)
VAT	23,335.60	314,155.62	
Total payments	119,044.65	3,061,285.36	
Closing balance	2,073,083.59	676,392.00	

Notes

- (i) Includes interest from fund manager, money market deposits and current account.
- (ii) Represents transactions undertaken to manage foreign exchange exposures.
- (iii) Relates to outstanding invoices from the Administration which were paid for in the Liquidation.
- (iv) Relates to the Joint Liquidators and their staff at their charge out rates. These rates are applicable to staff who are employees of PricewaterhouseCoopers Services Ltd and, where appropriate, parties who are otherwise contracted with PwC.
- (v) Includes actuarial and tax services provided by PwC, amounting to £634,290.31 and £16,379.00 respectively.
- (vi) Settlement with the FSCS in order to conclude HUK's potential exposure to Employers' Liability policies.
- (vii) Includes costs relating to advertising, printing, postage and directors and officers insurance.

USD Receipts and Payments Account for the periods 1 April 2012 to 16 April 2012 and 17 April 2012 to 16 April 2013

	<i>Administration</i> <i>1 April 2012 –</i> <i>16 April 2012</i>	<i>Liquidation</i> <i>17 April 2012 –</i> <i>16 April 2013</i>
Receipts	US\$	US\$
Balance brought forward / transferred from the Administration	13,307,103.93	13,308,328.99
Interest received	1,225.06	5,074.15 (i)
Reinsurance collections		175,955.81
Total receipts	13,308,328.99	13,489,358.95
 Payments		
Other professional costs		2,479.88
Letter of Credit draw down		2,500,000.00 (ii)
Bank and investment management charges		9,467.26 (iii)
Transfer to sterling account		2,408,700.00 (iv)
Total payments		4,920,647.14
Closing balance	13,308,328.99	8,568,711.81

Notes

- (i) Includes interest from bank account, Letter of Credit and money market deposits.
- (ii) The National Association of Insurance Commissioners trust fund of \$2.5m was drawn down by the Conservator, in accordance with the Conservation Agreement.
- (iii) Includes bank charges from current account and Letter of Credit charges.
- (iv) Represents transactions undertaken to manage foreign exchange exposures.

Section 4 **Information in support of the Joint Liquidators' time costs and disbursements from 17 April 2012 to 16 April 2013**

The time charged to the Liquidation is by reference to the time properly given by the Joint Liquidators and their staff in attending to matters arising.

It is the Joint Liquidators' policy to delegate tasks in the Liquidation to appropriate members of staff considering their level of experience and any requisite specialist knowledge, supervised accordingly, so as to maximise the cost effectiveness of the work performed. Matters of particular complexity or significance requiring more exceptional responsibility are dealt with by senior staff or the Joint Liquidators themselves.

Set out below are the relevant maximum charge-out rates per hour worked for the grades of the Joint Liquidators' staff actually or likely to be involved on this assignment. Time is charged by reference to actual work carried out on the assignment. There has been no allocation of any general costs or overhead costs.

Grade	£
Partner	609
Director	549
Senior Manager	424
Manager	354
Senior Associate	304
Associate	196

Specialist departments within the Joint Liquidators' firm such as Tax and VAT may charge a small number of hours if and when the Joint Liquidators require their expert advice. Such specialists' rates do vary but the figures below provide an indication of the maximum rate per hour.

Grade	£
Partner	1,025
Director	940
Senior Manager	820
Manager	520
Senior Associate	390
Associate	165

All staff who work on this assignment (including cashiers, support and secretarial staff) charge time directly to the assignment and are included within any analysis of time charged. Each grade of staff is allocated an hourly charge out rate which is reviewed from time to time. Work undertaken by cashiers, support and secretarial staff is charged for separately and is not included in the hourly rates charged by partners or other members of staff. Time is charged by reference to actual work carried out on the assignment in six minute units. The minimum time chargeable is three minutes (i.e. 0.5 units).

In common with many professional firms, the scale rates used by the Joint Liquidators may increase to cover annual inflationary cost increases.

There is no statutory requirement for the Joint Liquidators to seek approval to draw expenses or disbursements. However, professional guidance issued to insolvency practitioners requires that, where the Joint Liquidators propose to recover costs which, whilst being in the nature of expenses or disbursements, may include an element of shared or allocated costs (such as room hire, document storage or communication facilities provided by the Joint Liquidators' own firm), they must be disclosed and be authorised by those responsible for approving their remuneration. Such expenses are known as "Category 2" disbursements and they must be directly incurred on the case and subject to a reasonable method of calculation and allocation.

The Joint Liquidators' expenses policy allows for all properly incurred expenses to be recharged to the case. Category 2 disbursements are approved by the Liquidation Committee.

In the period 17 April 2012 to 16 April 2013 there were no Category 2 disbursements.

Other matters

No work has been carried out by subcontractors that could otherwise have been undertaken by the Joint Liquidators or their staff.

The Joint Liquidators have no business or professional relationships with parties responsible for approving the basis of their remuneration or who provide services to the Liquidation where the relationship could give rise to a conflict of interest.

Summary of the Joint Liquidators' time costs

Aspect of assignment	Hours							Cost £	Average hourly rate £/hr
	Partner	Director	Senior Manager	Manager	Senior Associate	Associate	Total		
Strategy and planning	44.0		72.0	134.5	198.8	51.0	500.3	174,787	349
Collections / commutations	2.0		46.4	109.7	27.3	4.8	190.2	68,899	362
Creditor claims	3.0	2.0	89.3	194.0	265.3	0.4	554.0	190,074	343
Run-off management			38.7	41.0	36.9	9.5	126.1	43,727	347
Accounting and treasury	0.5	0.7	5.0	27.2	75.0	73.2	181.6	48,814	269
Reporting to Liquidation Committee	12.0	2.0	45.3	110.8	75.4	18.7	264.2	93,453	354
Statutory and compliance	1.5		8.4	66.4	13.0	14.8	104.1	34,539	332
Tax and VAT			0.2	3.4	5.2	0.5	9.3	2,981	321
Legal matters			8.4	22.1	5.3		35.8	12,898	360

Total	63.0	4.7	313.7	709.1	702.2	172.9	1,965.6	670,170	341
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Narrative explanation of the Joint Liquidators' work

Strategy and planning

- Considered and developed strategy, including in relation to eventual closure Conducted internal progress and project management meetings
- Consulted periodically with second partner in relation to key issues and progress
- Undertook resource planning and management
- Maintained case information and files

Collections / commutations

Due to the ongoing nature and commercial sensitivity of certain aspects of work in connection with collections / commutations with some reinsurers, the following is intended to provide a high level overview. Further detail has been provided to the Liquidation Committee.

- Considered and pursued recovery strategies in relation to the Company's reinsurance assets, including negotiations with certain reinsurers
- Oversaw and directed preparations for the sale of the Company's residual reinsurance assets
- Worked with the New York Liquidation Bureau in order to seek release of the funds held in the National Association of Insurance Commissioners trust fund

Creditor claims

- Managed and directed Pro and the actuarial advisors in reviewing and agreeing claims submitted in the Cedant Scheme
- Reviewed and agreed claims submitted in the Cedant Scheme in accordance with the claims agreement protocol
- Conducted regular claims agreement progress review meetings
- Liaised with Cedant Scheme Creditors in relation to their claims and any other matters Finalised the settlement agreement with the FSCS in order to conclude HUK's potential exposure to Employers' Liability policies

Run-off management

- Liaised with Pro on a daily / monthly basis as appropriate to manage and monitor assignment progress and relevant issues
- Attended progress meetings with Pro
- Oversaw preparation and circulation of Pro's quarterly reports to the Liquidation Committee

Accounting and treasury

- Managed liquidity and cashflow on a monthly basis, including periodic review of foreign exchange exposures
- Monitored performance of investments on a monthly basis
- Reviewed and processed incoming invoices and recorded receipts
- Reviewed and monitored budgets for professional service providers
- Undertook quarterly bank reconciliations
- Assisted the Joint Liquidators' actuarial advisors in updating the Cedant Scheme dividend estimate

Reporting to Committee

- Organised, prepared for and attended Liquidation Committee meetings
- Prepared and circulated professional services fees reports on a quarterly basis and dealt with queries and matters arising
- Provided periodic updates in relation to key issues
- Responded to ad-hoc queries

Statutory and compliance

- Prepared, reviewed and submitted an unqualified CDDA return to The Insolvency Service
- Updated the FSA, UK Court and Companies House regarding estate progress and other general compliance requirements

Carried out ad-hoc company secretarial responsibilities

Tax and VAT

- Liaised with the Joint Liquidators' tax team in relation to the Corporation Tax returns for the year ended 31 December 2011 and the 2012 period while the Company was still in Administration
- Liaised with Joint Liquidators' tax team in relation to the submission of quarterly VAT returns

Legal matters

- Liaised with Clifford Chance in respect to ad-hoc legal matters

Section 5 *Expenses incurred in the period*

For the period 17 April 2012 to 16 April 2013

	£
Paid	
Legal fees	206,408.54
Run-off fees	1,096,588.11
Sub total	<hr/> 1,302,996.65
Unpaid	
Legal	2,976.67
Sub total	<hr/> 2,976.67
Overall total	<hr/> <hr/> 1,305,973.32

Note: VAT is excluded



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