



**Highlands Insurance Company (U.K.) Limited (in Administration)**

**Joint Administrators' Report in accordance with  
Rule 2.47 of the Insolvency Rules 1986  
for the period 1 May 2011 to 31 October 2011**

**November 2011**

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### Contact details for queries

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|---|--------------|---|----------------------|---------------------------------|----------------------|
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## I Summary Information

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|  |   |
|--|---|
| <b>The Company</b>                                       | Highlands Insurance Company (U.K.) Limited (in Administration)<br>(the "Company" or "Highlands UK")   |
| <b>Registered number</b>                                 | 01190948  |
| <b>Registered office and trading address</b>             | c/o PRO Insurance Solutions Limited ("PRO")<br>Bruton Court<br>Bruton Way<br>Gloucester<br>GL1 1DA<br>United Kingdom  |
| <b>Activity</b>  | Insurance and reinsurance run-off   |
| <b>Court reference</b>                                   | High Court of Justice, Chancery Division, Companies Court, Case No. 7896 of 2007  |
| <b>Administrators</b>                                    | Dan Schwarzmann and Mark Batten of PricewaterhouseCoopers LLP ("PwC")   |
| <b>Date of appointment of the Administrators</b>         | 1 November 2007   |
| <b>Date of approval of the Administrators' proposals</b> | 8 January 2008  |
| <b>Purpose of the Administration</b>                     | The purpose of the Administration is to achieve one of the following objectives:<br><br>(a) rescuing the Company as a going concern or, failing that,<br>(b) 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) or, finally,<br>(c) realising property in order to make a distribution to one or more secured or preferential creditors |

## II Progress Report

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### Purpose of this 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 the Administration since the last report to creditors dated May 2011. Copies of the previous reports sent to creditors, together with general information and other key documents in relation to the Administration of Highlands UK, may be accessed on the Highlands UK website which can be found at [www.ukhighlands.com](http://www.ukhighlands.com).

The following appendices accompany this report:

|            |   |
|------------|---|
| Appendix A | Joint Administrators' Proposals as approved by Creditors on 8 January 2008      |
| Appendix B | Receipts and Payments Account for the period 1 November 2007 to 31 October 2011 |

## II Progress Report

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### **Overall strategy**

The purpose of the Administration is to achieve one of the objectives set out on page one of this report. Accordingly, following my appointment as Administrator, my primary objective has been to oversee the run-off of Highlands UK's business whilst actively assessing the possibilities available to creditors.

In my last update I reported that all claims, submitted in accordance with the scheme of arrangement for creditors with claims arising from contracts or policies of direct insurance, and not contracts of reinsurance (the "Direct Scheme"), had been paid, or provided for, in full. Further details are provided below.

Following my last update I am also pleased to report that a 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"), has been issued, approved by the requisite majority of creditors and sanctioned by the UK High Court. In addition, a successful application has been made in the US pursuant to Chapter 15 of the US Bankruptcy Code for a permanent injunction recognising and giving effect to the Cedant Scheme. Further details are provided below.

### **Creditors' committee**

I have continued to consult with the creditors' committee in relation to all significant issues and the development and implementation of the requisite strategy. The most recent formal meeting of the creditors' committee was held on 23 May 2011. I remain very grateful to the members and the observer of the committee for their continued assistance and support.

## II Progress Report

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### Summary of the Administrators' actions to date

#### (a) Direct Scheme

As mentioned above, in my last report I explained that the Company had paid, or otherwise provided for, in full the claims of all direct creditors. On 23 September 2011 letters were sent to all direct creditors formally notifying them that the Direct Scheme had been finally implemented. Also, in accordance with the terms of the Direct Scheme, adverts were placed in a selection of national and international newspapers and journals, and on the Company's website, confirming that the Direct Scheme had been finally implemented.

Further information and copy documents (including a full text of the Direct Scheme) can be obtained at [www.ukhighlands.co.uk](http://www.ukhighlands.co.uk) or on request to the Joint Administrators.

#### (b) Cedant Scheme

In my last report, I advised that a letter had been sent to all known or potential Scheme Creditors to advise them of the proposed Cedant Scheme and the intention to seek permission from the High Court to convene the Scheme Meeting. The purpose of the Scheme Meeting was for Scheme Creditors to consider and, if thought fit, agree to the proposed Cedant Scheme.

I can now report that permission was subsequently obtained to convene the Scheme Meeting and that on 10 August 2011 the proposed Cedant Scheme was approved by the requisite majority of Scheme Creditors. Following this, the Cedant Scheme was sanctioned by the High Court on 15 September 2011 and permanent injunctive relief under Chapter 15 of the US Bankruptcy Code was granted on 22 September 2011, on which date the Cedant Scheme became effective.

On 26 September 2011 notices to all known potential Scheme Creditors, brokers, agents and intermediaries were circulated. This notice requested Scheme Creditors to complete and return a Claim Form in accordance with the terms of the Cedant Scheme by no later than 20 March 2012. Copies of this notice were also placed in a selection of national and international newspapers as well as journals and on the Company's website [www.ukhighlands.co.uk](http://www.ukhighlands.co.uk).

Further information and copy documents (including a full text of the Cedant Scheme) can be obtained at [www.ukhighlands.co.uk](http://www.ukhighlands.co.uk) or on request to the Joint Administrators.

## II Progress Report

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### **(c) Settlement with Highlands Insurance Company**

In my last report I explained that a formal settlement agreement which resolves a number of residual outstanding issues with Highlands Insurance Company (“HIC”) had been concluded subject to Texas Court approval. I am pleased to report that the Texas Court has approved the settlement agreement and that it is now being implemented in accordance with its terms.

### **(d) Financial review**

As mentioned previously and in the Cedant Scheme documents, although 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.

### **(e) Asset management**

PRO, under the guidance and direction of my team, has continued to actively progress the implementation of our reinsurance collection strategy. To date, reinsurance recoveries, including collections from brokers, have amounted to US\$5,575,486.89 and £100,238.10.

As previously reported, the Company’s US dollar investments are under the direct control of my specialist treasury team. My team continue to manage Highlands UK’s sterling and US dollar cash 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\$1,712,794.86 and £254,525.57 has been earned on the Company’s cash and investment assets since the Joint Administrators were appointed.

### **(f) Creditors and claims processing**

My team and PRO have continued to enter into dialogue with reinsurance creditors and have continued to make significant progress in the process of exchanging and reconciling claims information ahead of the Cedant Scheme claims submission deadline. This process will continue during the forthcoming period. Any claims from cedants, brokers, intermediaries and agents should now be presented in accordance with the terms of the Cedant Scheme to Pro Insurance Solutions Limited, Bruton Court, Bruton Way, Gloucester, GL1 1DA.

### **(g) Statutory reporting**

The Insurance Directorate of the FSA (Run-Off Division), which has responsibility for monitoring all insurance entities, continues to be advised of material developments in relation to the Administration.

## II Progress Report

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### (h) Administrators' remuneration

Full details of professional costs incurred by the Joint Administrators and their team in running the Administration have been reported regularly to the creditors' committee. Since my last report, and in accordance with Rule 2.106 of the Insolvency Rules 1986, the creditors' committee passed resolutions dated 11 May 2011 and 4 August 2011 approving the Joint Administrators' budgeted costs for the three month periods commencing 1 April 2011 and 1 July 2011 respectively. In addition we have recently submitted to the creditors' committee for approval a resolution in relation to the Joint Administrators' budgeted costs for the three month period commencing 1 October 2011. Further details of fees incurred to date can be found below.

The value of Joint Administrator's remuneration drawn to date comprises £4,247,035.87 of fees and £65,308.67 of expenses, excluding VAT. In accordance with the provisions of Statement of Insolvency Practice, Statement No. 9, as adopted by the Institute of Chartered Accountants in England and Wales, the following information is provided to you.

- (i) Accumulated time costs incurred as at 31 October 2011 are £4,300,747.77 being 15,241 hours at an average hourly rate of £282.18.
- (ii) Of the hours spent, 3,810 hours relate to directing, managing and liaising with PRO and other internal and external parties, day-to-day project management and general administration; 3,410 hours relate to securing assets (including reinsurance) and managing the finances of the Company; 1,826 hours relate to the development and implementation of the Direct Scheme and development of the Cedant Scheme; 1,783 hours relate to all dealings and negotiations with HIC and the overall strategy of the Administration; 1,208 hours relate to statutory compliance and 3,204 hours relate to dealing with all other matters including actuarial, claims, IT, legal, tax and the creditors' committee.

## Appendix A

### Joint Administrators' Proposals as approved by Creditors on 8 January 2008

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On 20 December 2007 the Administrators circulated to creditors their proposals for achieving the purpose of the Administration. The following proposals were approved by creditors without modification at a meeting held on 8 January 2008.

#### First resolution

- (i) The Administrators will continue to manage the Company's business, affairs and property in such manner as they consider expedient with a view to either rescuing the Company as a going concern or, failing that, 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). This may involve the formulation, promotion and, subject to approval, implementation of a scheme or schemes of arrangement under section 425 of the Companies Act 1985.
- (ii) The Administrators may investigate and, if appropriate, pursue any claims that the Company may have under the Companies Act 1985 or Insolvency Act 1986 or otherwise. In addition, the Administrators shall do all such other things and generally exercise all their powers as Administrators as they in their discretion consider desirable in order to achieve the purpose of the Administration or to protect and preserve the assets of the Company or to maximise realisations or for any other purpose incidental to these proposals.
- (iii) A creditors' committee will be established if sufficient creditors are willing to act on it. The Administrators propose to seek the election of a creditors' committee and to consult with it from time to time.
- (iv) The Administrators may use any or a combination of the "exit route" strategies in Paragraphs 76 to 80 and 83 to 84 of Schedule B1 of the Insolvency Act 1986 in order to bring the Administration to an end. If it is possible to rescue the Company as a going concern it is likely that the Administrators will make an application to Court to end the Administration and return management of the Company back to the Directors. However, if it is not possible to rescue the Company as a going concern and instead the objective is 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 is likely that the Administrators will formulate proposals for a scheme or schemes of arrangement under sections 425 of the Companies Act 1985 and, if so ordered by the Court will put them to meetings of the appropriate class(es) of creditors. If a scheme of arrangement is approved and sanctioned by the Court, the Administration will be brought to an end either:
  - (a) when the scheme of arrangement is brought to an end if it is more cost effective to run both procedures in tandem than for the Administration to be discharged, or
  - (b) by notice to the Registrar of Companies on completion of the Administration under Paragraphs 80 or 84 of Schedule B1 of the Insolvency Act 1986.

## **Appendix A**

### **Joint Administrators' Proposals as approved by Creditors on 8 January 2008**

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#### **Second resolution**

- (v) That if appointed, the creditors' committee will fix the Administrators' fees and Category Two disbursements. It is proposed that the Administrators' fees will be calculated based on time properly spent on the Administration by them and their various grades of staff according to their firm's charge out rates for work of this nature and charged in accordance with their firms' policy. If no creditors' committee is appointed then the Administrators will seek a resolution from creditors that they may be remunerated on a time cost basis at a later meeting of creditors.

## Appendix B

### Sterling Receipts and Payments Account for the period 1 November 2007 to 31 October 2011

|                                       | Notes | Position at 31 October 2011 | Position at 30 April 2011 | Change since 30 April 2011 |
|---------------------------------------|-------|-----------------------------|---------------------------|----------------------------|
|                                       |       | £                           | £                         | £                          |
| <b>Receipts</b>                       |       |                             |                           |                            |
| Opening cash at bank balance          |       | 185,304.45                  | 185,304.45                | 0.00                       |
| Opening value of investment portfolio | 1     | 979,925.78                  | 979,925.78                | 0.00                       |
| Interest received                     | 2     | 254,525.57                  | 247,190.89                | 7,334.68                   |
| Reinsurance collections               |       | 100,238.10                  | 100,238.10                | 0.00                       |
| VAT recoveries                        |       | 372,687.78                  | 236,464.70                | 136,223.08                 |
| Transfers from US dollar account      | 3     | 16,986,715.60               | 16,986,715.60             | 0.00                       |
| <b>Total receipts</b>                 |       | <b>18,879,397.28</b>        | <b>18,735,839.52</b>      | <b>143,557.76</b>          |
| <b>Payments</b>                       |       |                             |                           |                            |
| Administrators' remuneration          | 4     | 4,247,035.87                | 3,876,164.76              | 370,871.11                 |
| Administrators' disbursements         | 4     | 65,308.67                   | 57,497.53                 | 7,811.14                   |
| Run-off fees                          |       | 5,227,384.08                | 4,611,136.73              | 616,247.35                 |
| Other professional costs              | 5     | 3,172,318.57                | 2,930,391.02              | 241,927.55                 |
| Legal fees                            |       | 1,687,032.82                | 1,399,952.48              | 287,080.34                 |
| Legal settlements                     |       | 170,000.00                  | 170,000.00                | 0.00                       |
| Statutory and other costs             | 6     | 174,374.29                  | 132,806.25                | 41,568.04                  |
| Bank and investment charges           |       | 2,125.06                    | 2,101.06                  | 24.00                      |
| Transfer to US dollar account         | 7     | 50,000.00                   | 50,000.00                 | 0.00                       |
| VAT                                   |       | 1,609,198.91                | 1,429,318.52              | 179,880.39                 |
| <b>Total payments</b>                 |       | <b>16,404,778.27</b>        | <b>14,659,368.35</b>      | <b>1,745,409.92</b>        |
| <b>Closing balance</b>                |       | <b>2,474,619.01</b>         | <b>4,076,471.17</b>       | <b>-1,601,852.16</b>       |

#### Notes

- (1) On appointment the investment portfolio comprised a mix of cash, sterling certificates of deposits, Eurosterling bonds and UK gilts
- (2) Includes interest from EPIC, money market deposits, current account and realised gain on investments on closing EPIC account
- (3) Represents transactions undertaken to manage foreign exchange exposures
- (4) PwC charge out rates relate to the Joint Administrators and their staff. These rates are applicable to staff who are employees of PricewaterhouseCoopers Services Ltd and, where appropriate, parties who are otherwise contracted with PwC
- (5) Other professional costs include actuarial and tax services provided by PwC, amounting to £2,946,048.55 and £93,998.90 respectively
- (6) Includes costs relating to advertising, printing, postage, meeting room hire and Directors and Officers insurance premiums
- (7) To provide immediate post appointment liquidity

## Appendix B

### US Dollar Receipts and Payments Account for the period 1 November 2007 to 31 October 2011

|  | Notes | Position at 31 October 2011 | Position at 30 April 2011 | Change since 30 April 2011 |
|--|-------|-----------------------------|---------------------------|----------------------------|
|  |       | US\$                        | US\$                      | US\$                       |
| <b>Receipts</b>                        |       |                             |                           |                            |
| Opening value of cash at bank          | 1     | 3,003,869.67                | 3,003,869.67              | 0.00                       |
| Opening value of investment portfolio  | 2     | 29,002,839.49               | 29,002,839.49             | 0.00                       |
| Interest received                      | 3     | 1,712,794.86                | 1,707,715.60              | 5,079.26                   |
| Reinsurance collections                |       | 5,575,486.89                | 1,908,275.91              | 3,667,210.98               |
| Legal settlements                      | 4     | 12,999,981.23               | 12,999,981.23             | 0.00                       |
| Transfer from sterling account         | 5     | 97,280.00                   | 97,280.00                 | 0.00                       |
| <b>Total receipts</b>                  |       | <b>52,392,252.14</b>        | <b>48,719,961.90</b>      | <b>3,672,290.24</b>        |
| <b>Payments</b>                        |       |                             |                           |                            |
| Legal fees                             |       | 84,055.07                   | 84,055.07                 | 0.00                       |
| Other professional costs               |       | 53,233.61                   | 53,233.61                 | 0.00                       |
| Letter of Credit draw downs            |       | 137,468.89                  | 137,468.89                | 0.00                       |
| Bank and investment management charges | 6     | 218,098.26                  | 189,324.03                | 28,774.23                  |
| Payment to Direct Scheme Creditors     |       | 6,977,808.81                | 6,975,808.81              | 2,000.00                   |
| Legal settlements                      | 7     | 197,000.00                  | 0.00                      | 197,000.00                 |
| Transfer to sterling account           | 8     | 29,738,000.00               | 29,738,000.00             | 0.00                       |
| <b>Total payments</b>                  |       | <b>37,405,664.64</b>        | <b>37,177,890.41</b>      | <b>227,774.23</b>          |
| <b>Closing balance</b>                 |       | <b>14,986,587.50</b>        | <b>11,542,071.49</b>      | <b>3,444,516.01</b>        |

#### Notes

- (1) Includes deposits held at Citibank to the value of US\$2,991,939.41 in relation to a trust fund established and letters of credit issued prior to the appointment of Joint Administrators
- (2) On appointment the investment portfolio comprised a mix of cash, Eurodollar commercial paper, US dollar certificates of deposits, and Eurodollar, corporate and US treasury bonds
- (3) Includes interest on bank accounts and investment portfolio with EPIC
- (4) Relates to the release of the first and second payment tranches of the settlement agreement with HIC following the Direct Scheme Final Claims Submission Date on 15 February 2010
- (5) To provide immediate post appointment liquidity
- (6) Includes bank charges from current account, LoC and EPIC charges
- (7) Relates to payments made in accordance with the second settlement agreement with HIC
- (8) Represents transactions undertaken to manage foreign exchange exposures